International Monetary Fund

Union of the Comoros
and the IMF

Union of the Comoros: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

Press Release:
IMF Executive Board Concludes Third Review Under the Extended Credit Facility Arrangement for the Union of the Comoros; Approves Extension of the Arrangement and US$2.37 Million Disbursement
June 15, 2012

May 23, 2012

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

Letter of Intent

Moroni, May 23, 2012

Madame Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Madame Lagarde:

1. Following the bold institutional reforms undertaken over the last two years, the Comoros are gradually returning to peace and national unity. The most recent presidential and island elections were peaceful. These elections confirmed the rotating status of the Union presidency and enabled the country to embark on the road to political stability. As a result, the Comoros can at last focus on the challenges of economic development with technical and financial support from the IMF and other development partners.

2. The major political achievements of the last few years have nonetheless been obtained in a context of disruptions and delays harmful to the implementation of the IMF-supported reform program under the Extended Credit Facility (ECF) arrangement. Consequently, the program reviews for June and December 2011 could not be completed in a timely manner.

3. Encouraged by the more enabling political context, the new government is determined to put the program back on track. To that end, the government has initiated corrective measures in the budgetary and structural areas. These measures and other development actions by the government are coordinated in its Growth and Poverty Reduction Strategy Paper (GPRGF) adopted in 2009, and which we have lately refocused by order of priority of the projects and programs for the period 2011–14. From this strategy is drawn the three-year ECF-supported program, whose major objectives are to expand fiscal space so as to increase spending in priority and growth-supporting sectors, in addition to strengthening the competitiveness of the economy with a view to fostering stronger growth, in particular through the restructuring of public utilities.

4. Our discussions with Fund staff under the third review of the ECF arrangement have established that two performance criteria were not observed. The clearance of domestic payments arrears fell short of program targets for end-2010 and debt service owed to one creditor was honored with a delay, leading to incurrence of external payments arrears.

Furthermore, the existence of these arrears could not be promptly reported to IMF staff, owing to weaknesses in the national foreign debt management system. This led to misreporting for which the government requested and obtained a waiver from the IMF Executive Board in February 2012. Except for those mentioned above, all other quantitative program performance criteria for end-December 2010 were met. No significant progress was made through the latter date on the structural front, with especially a slow pace of reforms of the public enterprises and civil service. The most serious deficiencies in program implementation occurred during the run-up to and aftermath of the 2010 elections.

5. The new government has renewed efforts to achieve fiscal consolidation and to reinvigorate structural reforms, which it intends to expedite. In the medium term, the government is determined to secure its revenue targets under the program. To make the wage bill more compatible with the government's domestic revenue mobilization capacity, the government cancelled the excessive wage increase granted in 2010. Furthermore, the government is more closely monitoring the settlement of domestic payments arrears and the external debt service repayment schedule in particular by strengthening the joint monitoring of these operations by the Directorate of the Treasury, the Public Debt Directorate of the Ministry of Finance, as well as by the Central Bank of the Comoros. More generally, the government has enhanced the performance of the cash flow committee chaired by the Vice-President in charge of finance, with a view to achieving significant improvements in fiscal management. In order to give fresh impetus to its structural reform program, the government has requested and obtained increased technical support from development partners in implementing the reform of public enterprises. Moreover, the stepped-up monitoring of external debt is expected to help improve the reliability of data reporting to Fund staff. Considering all the corrective measures currently in progress, the government is seeking a waiver for the nonobservance of the above-mentioned performance criterion on domestic payments arrears. The government is henceforth requesting the completion of the third review under the ECF arrangement and disbursement of related ECF resources.

6. The country's macroeconomic performance was broadly satisfactory in 2011. Against the backdrop of easing political tensions, foreign aid remained high and domestic credit remained relatively robust. During 2011, private consumption and construction grew strongly, buoyed by remittances from the diaspora, financial aid, and a number of investments from public and private partners in the Gulf region. Thus, the rate of growth in real GDP attained 2.2 percent. Rising inflation reflects a somewhat difficult international context, despite favorable performance of subsistence agriculture. The surge in imports in the face of a rising oil bill, and the recovery of FDI, widened the external current account deficit, which reached 9.5 percent of GDP. The fiscal situation improved in the second half of the year. The domestic primary budget recorded a surplus of 1.6 percent of GDP, reflecting the impact of heightened efforts to mobilize domestic resources in the final quarter, exceptionally large revenues under the economic citizenship program, and wage restraint.

7. The architecture and fundamental objectives of the ECF-supported program remain unchanged. As stated in the attached memorandum of economic and financial policies, the government will continue pursuing a prudent fiscal policy, while endeavoring to protect the resources allocated to the social sectors in support of its poverty reduction efforts. The government also intends to accelerate the structural reforms necessary to enhance the competitiveness of the economy. If necessary, it would consult Fund staff before any revisions are made to the policies outlined in the memorandum, in accordance with the Fund's policy on such consultation.

8. In light of the delays in program implementation, the government requests the extension of the arrangement through December 2013 and rephasing of the third and subsequent ECF reviews and related disbursements. This would provide additional time beyond September 2012—the initial expiry date for the ECF arrangement—to complete the six program reviews and permit the disbursement of related Fund financial support. Accordingly, the fourth review would take place in December 2012 and the fifth review completed by end-June 2013.

9. In line with our commitment to transparency in government operations, we agree to the publication of documents relating to our discussions with Fund staff under the third review of our ECF-supported program.

Sincerely yours,

/s/

Ikililou Dhoinine
President of the Union of the Comoros

/s/

Mohamed Ali Soilihi
Vice-President in charge of the Ministry of Finance, Economy, Budget, Investment, and Foreign Trade

/s/

Mzé Abdou Mohamed Chanfiou
Governor of the BCC

ATTACHMENT 1

MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES FOR 2012

I. INTRODUCTION

1. This memorandum reviews progress made in 2010–11 in implementing the government reform program under the ECF, and sets out the measures and policies which the government is implementing in 2012 in order to achieve its objectives.

II. ECONOMIC DEVELOPMENTS AND PROGRAM PERFORMANCE

A. Recent economic developments and program implementation

2. **While slowly recovering, economic growth remains weak.** Estimated at 2.1 percent in 2010, the rate of growth of real GDP virtually stagnated in 2011, compared to 1.8 percent in 2009. In a context of rising foreign aid and easing political tensions, growth in 2010 was boosted by an upturn in domestic demand buoyed by external assistance and transfers from the diaspora. In 2011, growth was driven by favorable performance of the agricultural sector and transfers from the diaspora, as well as a modest recovery of foreign direct investment. Construction activities benefited from positive developments in the latter two sectors. Despite favorable agricultural food production, inflation was 7 percent on a year-on-year basis in 2011, reflecting domestic price pressures linked to rising world food and oil prices.

3. **Efforts to mobilize domestic resources and strengthen expenditure control in 2010 generated additional gains in fiscal consolidation.** Government revenue was equivalent to the targeted 14.3 percent of GDP under the program as a result of good performance of customs and nontax revenues associated with the economic citizenship program. In spite of overruns on personnel expenditure, the primary budget deficit fell to the programmed level of 1.6 percent of GDP (2.6 percent in 2009), while nonwage expenditure was broadly within projections. However, the late recovery of a large share of revenues delayed the settlement of some of the government's financial commitments and resulted in the accumulation of two months of wage arrears, which were not cleared until the second quarter of 2011.

4. **After deteriorating in the early part of the year, government budget strengthened in the second half of 2011.** Revenue collection was considerably weakened during the first three quarters of the year on account of insufficient taxation of petroleum products, institutional weaknesses in the management of the Port of Moroni, and insufficient performance by the tax and customs administrations. However, thanks to stronger revenue mobilization efforts at year-end, government revenue reached 16.1 percent of GDP including

3 percent of GDP in one-off nontax receipts from the economic citizenship program, compared to a revised projection of 13.1 percent of GDP and an outturn of 14.3 percent of GDP in 2010. The wage bill was brought back to a level more compatible with the government's revenue capacity (8.5 percent of GDP) following the cancellation of the wage increase granted in 2010. Accordingly, the primarily budget balance recorded a surplus equivalent to 1.6 percent of GDP compared to a deficit of 1.6 percent of GDP for 2010.

5. **Having remained stable in 2010, the external current account deficit significantly increased in 2011.** It is estimated at almost 9.5 percent of GDP in 2011 (7.0 percent of GDP in 2010), reflecting the rising global food and oil prices, a pickup in FDI-related imports, and a slight decline in budget assistance. Remittances from the diaspora recorded a moderate growth, while official reserves remained at a comfortable level, equivalent to 6.4 months of imports of goods and nonfactor services. The external debt of the Comoros remains unsustainable, and the government is endeavoring to expedite the implementation of the triggers in order to gain access to the completion point under the HIPC Initiative. The government is continuing to sign debt rescheduling agreements with its foreign creditors in conformity with the requirements of the HIPC process. Accordingly, the government is calling for the rapid restoration of the November 2009 debt rescheduling agreement with Paris Club members which was temporarily suspended as a result of delays in completing the third and fourth reviews under the ECF arrangement. To avoid penalties resulting from suspension, the government has engaged discussions with concerned creditors, while ensuring that its debt service is paid in strict accordance with agreed-upon timetables.

B. Program Implementation

6. **The implementation of the three-year ECF arrangement approved in September 2009 weakened significantly during the run-up to and aftermath of the December 2010 presidential** (Tables 1 and 2). Two performance criteria were not observed. Specifically, the end-December 2010 performance criterion on net reduction in domestic payments arrears was missed by 0.5 percent of GDP as the government faced with an unsustainable wage bill suspended all wage payments in a bid to renegotiate the salary increase granted in October 2010. Furthermore, the zero-ceiling on the accumulation of external debt service was overshot by 0.02 percent of GDP on account of weaknesses in external debt management. Almost all programmed structural reform measures were delayed. In particular, the implementation of the new civil service organizational frameworks for the civil service, initially planned for July 2011, was delayed; the census of civil service employees was not completed until December 2011, one year after the originally scheduled date; and the reform of public enterprises experienced delays. Consequently, Executive Board consideration of the third and fourth reviews, initially scheduled for 2011, was postponed.

III. Economic and Financial Policies for 2012

A. Macroeconomic Framework

7. **In 2012, real GDP is expected to grow by 2.5 percent with inflation declining on account of lower pressures on global food and oil prices.** Growth continues to benefit from the favorable performance of rain-fed subsistence agriculture, a slight strengthening of foreign direct investment, as well as a stepping up of technical and financial engagement of the country's main development partners. Against this backdrop, inflation will be held to 4.3 percent on a year-on-year basis. In the external sector, with exports remaining weak and the continuing high demand for imports, the external current account deficit is expected to exceed 10 percent of GDP.

B. Fiscal Policy

8. **In the medium term, government budget policy remains consistent with the objectives of the Fund-supported reform program under the ECF.** The government intends to pursue its efforts to achieve further gains in fiscal consolidation and improve the long-term profile of government indebtedness. In this perspective, the domestic primary budget deficit, which had fallen to the equivalent of 1.4 percent of GDP in 2011 (excluding exceptional revenues associated with the economic citizenship program), is projected to narrow further in 2012, reaching 1.1 percent of GDP. This reflects the effect of more rigorous revenue mobilization efforts in strengthening tax and customs administration, as well as closer scrutiny of expenditure, including wages. The government has made important changes in senior management personnel at the General Directorate of Taxes and Customs, a policy it intends to pursue in other areas of the finance administration. After cancelling the October 2010 wage increases, the government intends to implement the recommendations of the census of government employees and clean up the payroll list by end-June 2012. The government will then implement the new organizational frameworks for the civil service beginning in September 2012. All of these efforts are expected to help better control government wage costs. If the government receives external budget support in excess of programmed amounts, it will consult with the IMF on its use and will establish a new supplementary budget specifying how these resources will be allocated. In such a situation, the government will give priority to settling domestic payments arrears and to strengthening its deposits with the BCC.

9. **According to projections, domestic revenue is expected to amount to the equivalent of 14 percent of GDP in 2012.** To achieve this objective, the government is ensuring more rigorous management of the current taxpayer database of the Large Tax Payer Unit (*service de la fiscalité des enterprises, SFE),* which has doubled in size to reach 530 taxpayers over the last 12 months. The government has also strengthened the activities of the SFE offices in Anjouan and Mohéli. With technical assistance from the IMF and the AfDB, the government is expediting the establishment of the new General Administration of Taxes

and Government Property (*Direction Générale des Impôts et des Domaines*). The law establishing this agency is expected to be adopted by Parliament by end-June 2012. Pending the completion of this important reform and the comprehensive implementation of the law in question, in the first quarter of 2013, collaboration between the central government and island tax administrations has been strengthened. Further, the ad valorem taxation of imports will continue to be subject to closer monitoring by customs and, to that end, the operational resources of the central office responsible for monitoring the value, type, and origin of imported goods have been strengthened. In addition, the government has addressed the uncertainties affecting the Port of Moroni which is now being managed by an internationally reputable operator.

10. **In 2012, expenditure is expected to be contained to 24.7 percent of GDP.** In this context, the wage bill will decline to 8 percent of GDP, compared to 8.5 percent of GDP in 2011. To ensure the satisfactory implementation of its budget program and facilitate attainment of the completion point under the HIPC Initiative, the government is exercising close supervision over the wage bill––including through rigorous adherence to the new integrated wage payment system (GISE) across the country. Cumulative from January 1, 2012, the government has set ceilings on wage outlays at CF 9,144 million for June 30, 2012, CF 13,716 million for September 30, 2012, and CF 18,288 million for December 31, 2012. The government intends to raise investment outlays to 1.7 percent of GDP (0.7 percent of GDP in 2011). Social expenditures in education and health are expected to increase to CF 13,034 million (5.7 percent of GDP). More generally, the government is closely adhering to the spending limits agreed to under the 2012 budget, including one-off loan of CF 350 million (0.2 percent of GDP) to the electricity company in support of an emergency rehabilitation program for that company, prepared with technical assistance from the World Bank. After settling all wage arrears accumulated in 2011, the government has strengthened cash flow management in an effort to forestall any further accumulation of new domestic payments arrears. It is now ensuring the regular and timely payment of monthly wages to government employees.

11. **The overall fiscal balance (cash basis, including grants) should be virtually in equilibrium in 2012.** The net financing requirements of the government are fully met by financial assistance from Gulf region partners, the IMF, the AfDB, the World Bank, and France. In the event of shortfalls in revenue or grants, the government intends to adopt appropriate compensatory measures, including slower increases in goods and services and investment expenditures, as well as more vigorous collection of tax arrears.

C. Money, Credit, and the Financial System

12. **Following a considerable expansion over the last three years, broad money is expected to virtually stagnate in 2012.** Government borrowing from the banking system remains prudent so as to allow for adequate expansion of credit to the private sector. The reserve requirement ratio continues to be the main instrument for liquidity management. In

2011, it was brought back to 25 percent (from 35 percent) in response to a gradual decline in the demand for credit against a backdrop of persistent excess liquidity within the banking system. Subsequent changes in the ratio will continue to be dictated by the overarching objectives of maintaining price and macroeconomic stability, as well as provisioning the economy with adequate liquidity. The BCC is implementing the recommendations of the 2012 safeguards assessment, including producing financial statements in conformity with international standards and submitting the monetary data reported to Fund to prior review by the financial controller of the Bank.. Finally, in 2012 the BCC is completing its efforts aimed at further strengthening banking supervision with technical and financial assistance from the IMF, Banque de France, and the UNDP-FENU in the context of the Comoros Inclusive Finance Program (PAFIC).

13. **Overall, the soundness of the Comorian banking system continues to be satisfactory.** Despite a slight increase of NPLs in 2011, most financial institutions saw their profitability improve. Moreover, the banking system exhibits healthy ratios with respect to liquidity, gross solvency, and coverage of obligations to third parties. Pending finalization of a medium-term reform program, the government has pursued the execution of short-term measures designed to improve the financial situation of the National Postal and Financial Services Company (SNPSF). In this respect, important progress has been made, particularly with respect to the replenishment of cash flow, compliance with reserves requirements, and the improvement of the credit portfolio. As a result, the BCC has terminated the provisional administration of the institution. However, the SNPSF's overall situation remains fragile. The finalization and rapid implementation of a credible medium-term rehabilitation plan remain one of the priorities for the institution. The government has granted the BCC considerable leeway in the conduct of these important reforms with technical support from development partners.

D. Balance of Payments and External Debt

14. **The external current account deficit, inclusive of private and official transfers and grants, is expected to reach 10.4 percent in GDP in 2012 (9.5 percent of GDP in 2011).** It should decline below 10 percent of GDP in 2013. In the face of rising food and oil prices, the weak external position in 2011 and 2012 reflects the low level of exports and the return of official grants to normal levels, following the strong expansion observed in 2010. Confronted with a heavy external debt burden, the government intends to pursue a cautious indebtedness policy.

15. **Any external borrowing contracted or guaranteed by the government is subject to prior approval by the Minister of Finance of the Union, and the executive governments of the islands do not have the authority to contract or guarantee external borrowing**. As in the past, the government will neither contract nor guarantee any short-term or nonconcessional external debt as defined in the Technical Memorandum of Understanding

(TMU). The authorities will continue to consult the IMF before contracting or guaranteeing any concessional external debt in excess of US$20 million.

16. Having accumulated external payments arrears in 2010, the government has made efforts to improve debt management to prevent further difficulties in this area. External debt service payments arrears (on rescheduled debt obligations under the HIPC Initiative) were accumulated vis-a-vis the International Fund for Agricultural Development (IFAD) in 2010 and early 2011. They have since been settled in full. With support from the African Development Bank, the Public Debt Directorate is being provided with an effective debt management software and training for staff. Also, the World Bank has recently provided the government with technical assistance to assess their debt management capacity. On that basis, the authorities are developing an effective program for enhancing its expertise in this area. Inter-departmental monitoring of debt service maturities and payments (between the Debt Directorate, the Treasury, and the Central Bank) has been intensified. In this context, meetings among decision-makers from the relevant departments are being held on a regular basis.

E. Structural Policies

17. **The government is determined to accelerate its divestiture of Comores Télécom.** It is benefiting from technical and financial assistance from the World Bank group. In April, the government signed a partnership contract with the IFC to receive technical support in implementing the Comores Telecom divestiture transaction. A call for expressions of interest among potential strategic partners will be launched by end-December 2012.

18. **Faced with the steady deterioration in the country's energy situation, the government is reaffirming its commitment to in-depth reform of the energy sector.** To ensure the success of this reform, the government has requested technical assistance from the World Bank, the European Union, and the AfDB. The AfDB will be implementing a project to provide support to the energy sector in the amount of US$20 million during 2012. Various studies should be completed by end-September 2012, in particular: (i) an EU-funded study on the long-term energy strategy for the Comoros; (ii) an organizational and strategic audit of the electricity and water company (MA-MWE) supported by the AfDB; and (iii) a diagnostic study of the sector as well as a sectoral strategy proposed by the World Bank. These studies will help clarify the institutional and regulatory environment for the energy sector and facilitate agreement on arrangements for restructuring MA-MWE and the Société Comorienne des Hydrocarbures (SCH) in the context of performance contracts entrusted to providers specializing in energy management. Preliminary contracts have been established with a Saudi group (Al-Sharif Group) with a view to entering into a possible partnership in the production and distribution of electric energy, in the context of a far-reaching restructuring of the electricity and Water Company.

19. **In the immediate future, the government is focused on finalizing an emergency rehabilitation program for MA-MWE with technical assistance from the World Bank.** The financial cost of the emergency maintenance operations, estimated at CF 350 million, is fully reflected in government's financial operations for the second quarter of 2012. The execution of the emergency program is being overseen by World Bank staff.

20. **In the area of public financial management, the government's objective is to improve budget management.** Supported by the AfDB, the authorities have implemented a new General Tax Code; by end-March 2013 they are expected to complete the establishment of a new General Tax and Government Property Administration (AGID) and its board of directors. This reform is designed to strengthen overall cohesion and collaborative relationships between the offices of the central tax authorities of the Union and the tax offices of the island entities, and to enhance the efficiency of tax administration throughout the tax revenue chain (assessment, supervision, and collection) while strengthening the efforts towards a unified budget framework. With assistance from the World Bank, the government conducted a comprehensive census of government employees and civil servants. The government is preparing by end-June 2012 a new list of government employees for payroll settlement purposes under the GISE system. Current staffing levels broken down by grade and ministry will be reported to Fund staff by end-July 2012. With assistance from the World Bank, the government has also developed a list of priority sector expenditures which will be rigorously monitored by the inter-unit committee responsible for monitoring PRSP implementation. These efforts will help to ensure that the savings generated through the debt service reduction under the HIPC Initiative are actually used to finance the priority sectors in the poverty reduction and growth strategy. Furthermore, by end-2012 the government will finalize the terms of reference for a study aimed at introducing a budgetary framework and medium-term expenditure frameworks (MTEF) beginning in FY 2016.

21. **Civil service reforms should contribute to strengthening the medium-term viability of the budget.** In this context, the government has secured the adoption by Parliament of the law establishing organizational frameworks for the civil service; implementation is expected in September 2012. This reform is expected to generate further efficiency gains in payroll management resulting from the civil service census and a rigorous implementation of the GISE, making it possible to beef up average wages while keeping the overall wage envelope within limits compatible with the financial resources of the State. In this context, the government is continuing to seek technical and financial assistance from its development partners in preparing and implementing a program to support civil servants removed from the government's personnel lists.

F. Poverty Reduction Strategy Paper (PRSP) and Improvement of Economic and Social Statistics

22. **The government has finalized its first annual status report on implementation of the PRSP**. The report assesses limited but encouraging progress in several areas, including a

modest recovery in economic growth, improvements in political governance and school enrollment for girls, as well as some reduction of maternal and infant mortality. However, the progress remains modest in comparison with the ambitious objectives set out in the initial document. The main constraints consist in insufficient coordination of actions as well as limited absorption capacity relative to the announced amounts of financial resources. The government is drawing upon the conclusions and recommendations of this report to take steps to enhance the effectiveness of its poverty reduction strategy. Furthermore, to make the strategy more operational and realistic, the government has finalized with AfDB support a refocused action plan for the PRSP. The authorities intend to implement it rigorously with technical and financial support from its development partners.

23. **The government is resolved to continue its efforts to improve the socio-demographic and macroeconomic database needed for the design and monitoring of its development policy.** In this connection it is receiving significant technical assistance from the AfDB, particularly in respect of the preparation of the national accounts and the consumer price index. The program to improve the quality of national accounts and consumer price index statistics is expected to be completed in 2013. With support from the EU, the government has embarked upon a capacity-building program for the Economic and Financial Reform Monitoring Committee (CREF) in the areas of the collecting, compiling, verifying, processing, and consolidating economic and financial data, as well as preparing and monitoring the government's table of financial operations (TOFE).

IV. Program Monitoring and Extension, And Rephasing of Disbursements

24. **The program will be monitored on the basis of quarterly targets with performance criteria established on a semiannual basis** (Tables 1 and 2). Since the third ECF review has been substantially delayed, the government requests rephasing of related and subsequent disbursements and extension of the program to end-2013. This will provide adequate time for implementation delayed program reforms and concluding all outstanding reviews. In 2010, persistent shortcomings in wage bill management jeopardized program implementation, causing recurrent slippages in the budget program and calling the integrity of the program into question. The government intends to ensure that there is no recurrence of such incidents. Accordingly, quarterly wage ceilings as set in paragraph 10 above will be strictly adhered to. The government will provide the IMF with such information as needed to monitor the program, in accordance with the Technical Memorandum of Understanding. During the program period, the authorities will not introduce or intensify restrictions on payments and transfers for current international transactions, and will not introduce or modify any multiple currency practices, conclude any bilateral payments agreements that are inconsistent with Article VIII of the IMF's Articles of Agreement, or impose any restrictions on imports for balance of payments purposes.

25. **The fourth review of the ECF arrangement will be held in December 2012.** In the area of structural reforms, the review will focus primarily on measures aimed at

strengthening control of the wage bill and execution of public enterprise reform, in particular: (i) observance of the fiscal targets pertaining to the wage bill; (ii) cleanup of the payroll database in order to act upon the recommendations of the survey of government employees and civil servants; (iii) introduction of the organizational frameworks for the civil service; and (iv) implementation of the roadmap for Comores Télécom.

26. **The government requests that the ECF-supported program be extended for 15 months through end-December 2013.** This will make it possible to have more time after September 2012—the initial expiry date of the arrangement under the ECF—to complete the six program reviews and to make disbursements of the related financial assistance.

Table 1. Comoros: Quantitative Performance Criteria and Indicative Targets under the ECF-supported Program [1]
(in millions of Comorian francs, cumulative since the start of the fiscal year, unless otherwise specified)

	2010			2012			
	Dec.			Mar.	Jun.	Sept.	Dec.
	PC	Adj. PC	Actual	Est.	PC	Indicative Target	PC
Performance criteria							
1. Ceiling on net credit to government (NCG)	156		-719 met	1,816	508	2,026	2,214
2. Ceiling on the accumulation of net domestic payments arrears [2]	-10,784	-12,264	-11,184 not met				
3. Ceiling on the accumulation of new domestic payments arrears [3]				0	0	0	0
4. Ceiling on new nonconcessional external debt contracted or guaranteed by the government [4, 5]	0		0 met	0	0	0	0
5. Ceiling on new short-term external debt contracted or guaranteed by the government [4, 5]	0		0 met	0	0	0	0
6. Ceiling on accumulation of external debt service arrears [5]	0		44 not met [6]	0	0	0	0
Indicative targets							
7. Floor on the domestic primary balance	-3,141		-3,271 not met	63	-460	-1,821	-2,621
8. Floor on total domestic revenues	28,848		28,875 met	8,614	16,052	24,029	31,847
9. Ceiling on expenditures by cash advances	150		120 met	150	150	150	150
10. Floor on domestically financed social spending	11,870		11,941 met				13,034
11. Floor on gross reduction of domestic payment arrears				-684	-750	-864	-1,152

[1] Definitions of targets and adjusters are provided in the Technical Memorandum of Understanding (TMU).
[2] Targets and realizations adjusted as specified in the TMU. The target on the accumulation of domestic arrears is set on a net basis until December 31, 2010.
[3] Targets and realizations adjusted as specified in the TMU. The target on the accumulation of new domestic arrears is set from January 2012 onward.
[4] Excluding trade credits.
[5] Monitored on a continuous basis.
[6] Waiver for missed PC granted by the IMF Board in February 2012 under the related misreporting case (EBS/12/11).

Table 2. Comoros: Proposed Structural Benchmarks for the Arrangement Under the ECF, 2010–13

Measures	Macroeconomic Justification	Date	Status
Structural benchmarks			
Public finance management			
Completion of the civil service census	Improve control of the wage bill and public expenditure	December 31, 2010	Observed with delay in December 2011
Establish the post-census payroll list	Improve control of the wage bill and public expenditure	June 2012	New
Establish the offices of the large taxpayer unit in Anjouan and Mohéli	Enhanced effectiveness of tax administration	March 31, 2011	Not observed on time, but fully implemented in September 2011
Adopt legislation on new General Administration of Taxes (formerly the General Tax Directorate)	Enhanced effectiveness of tax administration	June 2012	New
Appoint the board of directors of the new general tax administration	Enhanced effectiveness of tax administration	March 31, 2011	Not observed; new date set for end-March 2013
Adopt TORs for study on the budget framework and MTEFs	Enhanced effectiveness of budget and expenditure management	March 31, 2011	Not observed; new date set for end-December 2012
Implementation of the new organizational frameworks for the administrations of the Union and the islands	Rightsizing the civil service to ensure medium-term budget sustainability	June 30, 2011	Not observed; new date set for September 2012
Adopt indicative targets for social spending and other priority outlays	Improve monitoring of the use of HIPC resources	June 30, 2011	Not observed on time, but completed in October 2011

Measures	Macroeconomic Justification	Date	Status
Complete a census of large taxpayers and thereby update the list of large taxpayers	Enhanced effectiveness of the collection activities of the large taxpayer unit	September 30, 2011	Observed
Adopt the terms of reference for a feasibility study for a comprehensive computerized public financial management system, including an estimate of the cost and a timetable for the installation of the proposed system	Improve monitoring of expenditures and overall budget execution; facilitate progress toward HIPC completion point	September 2012	New
Public enterprise reform			
Maintaining the flexible petroleum product price-setting mechanism	Permit a reliable supply of petroleum products and limit the pressures for subsidies on the budget	Ongoing	Ongoing
Adoption of the reform strategy for MAM-WE	Permit a reliable supply of electrical energy and limit the pressures for subsidies on the budget	March 31, 2011	Redefined as feasibility study for the new privatized MAM-WE, September 2012
Call for expressions of interest from potential strategic partners for Comores Télécom and SCH	Permit a reliable supply of telecommunications services and limit the pressures for subsidies on the budget	March 31, 2011	Delayed for Comores Télécom to end-December 2012 SCH: to be redetermined
Call for expressions of interest from potential strategic partners for MAM-WE	Permit a reliable supply of electrical energy and limit the pressures for subsidies on the budget	June 30, 2011	Redetermined: partnership agreement signed in January 2012 with Al-Sharif group to achieve the same objective

ATTACHMENT 2

TECHNICAL MEMORANDUM OF UNDERSTANDING

Moroni, June 2012

1. This technical memorandum of understanding (TMU) defines the quantitative performance criteria, indicative targets and structural benchmarks to monitor the implementation of the program supported by the three-year arrangement under the Extended Credit Facility. It also describes the data to be reported for program monitoring purposes.

I. Definition

2. Unless otherwise specified below, "the government" is meant to include the government of the Union of the Comoros and the autonomous island governments. Local governments, the central bank, or any government-owned entity with separate legal personality are excluded from the definition of government. The units covered under this definition of government are consolidated for the needs of the program.

II. Quantitative Performance Criteria

3. Quantitative performance criteria are proposed for June 30 and December 31, 2012 with respect to changes in net domestic credit to the government and zero-ceiling on new domestic payments arrears; with indicative targets for September 30, 2012. The following performance criteria are proposed for monitoring on a continuous basis: (i) the external payments arrears of the government; (ii) the contracting or guaranteeing of new nonconcessional external debt by the government; and (iii) the contracting or guaranteeing of new short-term external debt by the government.

A. Change in Net Domestic Credit to the Government

Definitions

4. Net domestic credit to the government is defined as overall net credit extended to the government from domestic bank and nonbank sources. Net bank credit to the government reflects the net debt position of the government vis-à-vis the central bank, commercial banks, and the National Postal and Financial Services Company (SNPSF), as well as microfinance institutions. It is the difference between the government's gross indebtedness to the banking system and its claims on the banking system. These government claims include all deposits at the central bank and commercial banks, as well as Treasury cash holdings. The government's debt to the banking system includes central bank credit (statutory advances as well as any

long-term credit and IMF net credit) and commercial bank credit, as well as net deposits at the SNPSF. Domestic nonbank credit to the government includes changes in the stock of Treasury bills placed in the domestic market, privatization receipts, and any other domestic financial debt of the government held outside the banking sector, other than arrears.

5. The change in net domestic credit to the government as of the date for the performance criterion or indicative target is defined as the difference between the stock on the date indicated and the stock on December 31, 2011.

Performance criteria

6. The amounts set out in Table 1 of the MEFP on Net Credit to Government for June 30 and December 31, 2012 are ceilings and constitute performance criteria. The amount set out in the above table for September 30, 2012 is a ceiling and constitutes an indicative target.

Reporting requirements

7. The BCC will report the provisional data on net bank credit to the government to Fund staff on a monthly basis, with a lag of no more than 45 days after the end of each observation period. Final data will be reported with a maximum lag of two months. The Ministry of Finance will report monthly on any financing from nonbank sources.

B. New Domestic Payments Arrears

Definition

8. Domestic payments arrears of the government are defined as any of the following: (i) any invoice that a spending ministry has received from a supplier of goods and services, delivered and verified, and for which payment has not been made within 90 days after the date the payment order (*ordonnancement*) was cleared; (ii) in the case of specific contracts between the suppliers and the government, any invoice received and not paid on the due date stipulated in the contracts; (iii) tax credits confirmed by the proper authorities after review, and not paid within 60 days from the date when the payment order was issued; and (iv) wages and salaries and any payments to a government employee that were due to be paid in a given month but remained unpaid on the 15th day of the following month.

Performance criterion

9. Under the program, the government will not accumulate any new domestic payments arrears as from January 1, 2012. The zero-limits on new domestic payment arrears for June 30 and December 31, 2012 constitute performance criteria, and the zero-limit on new domestic arrears for September 30, 2012 constitutes an indicative target.

C. External Payments Arrears

Definition

10. External payments arrears are defined as the sum of payments due but unpaid on outstanding external debt (for a definition of external debt see paragraph 15) that has been contracted or guaranteed by the government, with the exception of external payments arrears arising from public debt being renegotiated with creditors, including Paris Club members.

Performance criterion

11. Under the program, the government will not accumulate any external payments arrears with respect to the public debt, except for payments related to renegotiations with creditors, including Paris Club members. This performance criterion will be monitored on a continuous basis.

Reporting requirements

12. The authorities will report to Fund staff any accumulation of external payments arrears as soon as the due date has been missed. They will provide each month, within a maximum lag of 15 days, a table showing external debt due (after rescheduling) and paid.

D. Ceiling on the Contracting or Guaranteeing of New Nonconcessional External Debt or Short-Term Debt by the Government

Definition

13. This performance criterion applies not only to debt as defined in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Executive Board Decision No. 6230-(79/140), last amended by Executive Board Decision No. 1441-(09/91), effective December 1, 2009), but also to commitments contracted or guaranteed by the government for which value has not been received.

14. Short-term debt refers to external debt with a contractual maturity of less than one year. External debt refers to debt owed to nonresidents.

15. The definition of debt, as specified in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, reads as follows: "(a) For the purposes of this guideline, the term '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. Debt can take a number of forms, including: (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 sometime 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. For the purpose of the guideline, 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; (b) Under the definition of debt set out in point 9(a), arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. 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."

16. Any external debt of which the present value, calculated with the reference interest rates mentioned hereafter, is superior to 50 percent of the nominal value (grant element of less than 50 percent) is considered nonconcessional, with the exception of IMF lending under the Extended Credit Facility, which is considered concessional even if it does not meet the 35 percent grant element threshold. For debt with a maturity of more than 15 years, the ten-year reference market interest rate, published by the OECD, is used to calculate the grant element. The six-month reference market rate is used for debt with shorter maturities.

17. For the purposes of this performance criterion, government is understood to include the government (as defined in paragraph 2 above), as well as local administrations, public institutions of an industrial and commercial nature (EPICs), public administrative institutions (EPAs), public enterprises, and government-owned or -controlled independent companies (i.e., public enterprises with financial autonomy of which the government holds at least 50 percent of the capital).

Performance criterion

18. The government as defined in paragraph 17 will not contract or guarantee nonconcessional or short-term external debt as defined above. This performance criterion will be monitored on a continuous basis. It does not apply to debt rescheduling and restructuring operations. In addition, import-related credit and pre-export financing secured on export contracts of less than one year maturity are excluded from this performance criterion on short-term debt.

Reporting requirements

19. The authorities will report any new external borrowing and its terms to Fund staff as soon as external debt is contracted or guaranteed by the government.

III. INDICATIVE TARGETS

A. Domestic Primary Balance

Definition

20. The consolidated domestic primary fiscal balance (payment order basis) is calculated as total government revenue (defined below), excluding foreign grants, less expenditure, excluding interest payments, and foreign-financed technical assistance and investment expenditure.

Indicative Targets

21. The targets for the floor on the domestic primary fiscal balance, cumulative from the beginning of the 2012 calendar year, are set at CF –460 million for June 30, 2012 CF –1,821 million for September 30, 2012, and CF –2,621 million for December 31, 2012.

Reporting requirements

22. During the program period, data on the domestic primary fiscal balance (payment order basis) will be forwarded to Fund staff monthly by the Ministry of Finance of the Union within 45 days following the end of each month.

B. Government Revenue

Definition

23. Government revenue is defined as reported in the consolidated government financial operations table (TOFE), and includes all tax and nontax receipts and excludes external grants.

Indicative Targets

24. The floor on government revenue, cumulative from the beginning of the 2012 calendar year, is set at CF 16,052 million for June 30, 2012, CF 24,029 million for September 30, 2012, and CF 31,847 million for December 31, 2012. These amounts are considered indicative targets under the program, for the respective dates.

Reporting requirements

25. The Ministry of Finance will report preliminary revenue data to Fund staff monthly, with a lag of no more than 45 days, on the basis of actual collections as recorded in Treasury accounts. Final data will be provided once the final Treasury accounts are available, but not later than two months after the reporting of preliminary data.

C. Expenditures Made by Cash Advances

Definition

26. Expenditures made by cash advances include all expenditures paid without prior commitment order.

Indicative Targets

27. Responsibility for achieving the ceiling on expenditures outside of normal procedures rests with both the Union government and the autonomous island governments. This ceiling, cumulative from January 1, 2012, is set at CF 150 million at June 30, 2012, September 30, 2012, and December 31, 2012**.**

Reporting requirements

28. Data on expenditures made outside of normal procedures will be forwarded to Fund staff monthly by the Ministry of Finance of the Union, within 30 days following the end of each month.

D. Domestically Financed Social Spending

Definition

29. Total domestically financed social spending (current and capital) is calculated, for each category of current expenditure (wages, goods and services, transfers and subsidies) and capital expenditure as: (1) expenditure executed by the Ministry of Health (under "health"), and (2) expenditure executed by the Ministry of Education (under "education"). Domestically financed social spending is classified according to the above categories (health and education) based on a classification of each project presented in the 2012 budget into health and education. Total domestically financed current and capital social spending includes social spending financed by domestic resources, including revenues, domestic financing, and general external budget support, and excludes all social spending financed by project-specific foreign grants and/or loans.

Indicative Targets

30. The floor on total domestically financed social spending for the period from January 1, 2012 to end-December 2012 is set at CF 13,034 million. This amount is an indicative target under the program.

Reporting deadlines

31. During the program period, data on domestically financed social spending will be forwarded to Fund staff by the Ministry of Finance within 45 days following the end of the period.

E. Gross Reduction of Domestic Payments Arrears

Definition

32. Domestic payments arrears of the government are defined as any of the following: (i) any invoice that a spending ministry has received from a supplier of goods and services, delivered and verified, and for which payment has not been made within 90 days after the date the payment order (*ordonnancement*) was cleared; (ii) in the case of specific contracts between the suppliers and the government, any invoice received and not paid on the due date stipulated in the contracts; (iii) tax credits confirmed by the proper authorities after review, and not paid within 60 days from the date when the payment order was issued; and (iv) wages and salaries and any payments to a government employee that were due to be paid in a given month but remained unpaid on the 15th day of the following month.

Indicative Targets

33. The floor on gross reduction of domestic payments, cumulative from the beginning of the 2012 calendar year, is set at CF 750 million for June 30, 2012, CF 864 million for September 30, 2012, and CF 1,152 million for December 31, 2012. These amounts are considered indicative targets under the program, for the respective dates.

Adjuster

34. If external budget support is less than expected, the floor on the gross quarterly reduction of domestic payments arrears adopted in the MEFP, fiscal Table 2C, will be lowered by the full amount of the shortfall. In the case of a surplus in the amount of external budget support, the floor on the net reduction of domestic arrears will be raised by the full amount of the surplus. Cumulative from January 1 of the year in question, the program assumes external budget support (IMF inclusive) of CF 3,375 million by end-June 2012, CF 5,481 million by end-September 2012, and CF 6,980 million by end-December 2012.

Reporting requirements

35. During the program period, data on gross reduction of domestic payments will be forwarded to Fund staff by the Ministry of Finance within 45 days following the end of the period.

IV. Additional Information for Program Monitoring

36. The authorities will report to Fund staff the following information and data according to the schedule provided, either directly (e-mail or facsimile) or by airmail. Barring any agreement to the contrary, the data will take the form mutually agreed by the authorities and the IMF. The fiscal data, monetary data, external debt data, the consumer price index, and any information on important legislative and/or other developments will be provided not later than 45 days after the date to which they pertain.

Monthly:

The monetary survey and the monthly balance sheets of the BCC and commercial banks;

Classification of commercial bank loans by economic sector;

Interest rates;

TOFE data on a cash and payment order basis, the related detailed tables on revenue, and a table showing the link between the payment order basis and cash basis for expenditures;

External public debt operations (debt contracted and guaranteed by the government, settlement of external payments arrears, and debt service paid, broken down between interest and principal);

Consumer price index; and

Imports and exports, production of electricity, tourist arrivals, and any other indicators of economic activity that may be available on a monthly basis.

Quarterly:

Production of major agricultural products (vanilla, cloves, ylang-ylang)

Annually:

National accounts data;

Balance of payments data.

Moreover, information on important measures adopted by the government in the economic and social areas that would have an impact on program developments, changes in legislation, and any other pertinent legislation, will be reported to Fund staff by the authorities on a timely basis.