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This action is funded by the European Union

ANNEX

of the Commission Decision amending Commission Decision C(2017)7585 of 13.11.2017 on the Annual Action Programme 2017 in favour of the Republic of Mozambique to be financed from the 11th European Development Fund

Action Document for PFM and DRM Support Programme 2 - Mozambique

1. Title/basic act/ CRIS number	PFM and DRM Support Programme 2 - Mozambique CRIS number: MZ/FED/039-696 financed under the 11th European Development Fund (EDF)	
2. Zone benefiting from the action/location	Republic of Mozambique The action shall be carried out at the following location: Republic of Mozambique.	
3. Programming document	National Indicative Programme (NIP) 2014-2020 for Mozambique	
4. Sustainable Development Goals (SDGs)	Main SDG Goal 16: promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels. Other SDGs: Goal 8: promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all. Goal 17: revitalise the global partnership for sustained development.	
5. Sector of intervention/ thematic area	Sector 1: Good Governance and Development	DEV. Assistance: YES[1]
6. Amounts concerned	Total estimated cost: EUR 27 000 000 Total amount of EDF contribution EUR 27 000 000	
7. Aid modality and implementation modalities	Project Modality **Direct management** through Grants **Indirect management** with the World Bank **Indirect management with** the Republic of Mozambique	
8 a) DAC code(s)	15111 - Public finance management – 61 % of financing 15114 - Tax policy and administration support – 33 % of financing 15112 – Local Government Administration - 6 % of financing	
b) Main Delivery Channel	Recipient Government - 12000 World Bank – 44001	

[1] Official Development Assistance is administered with the promotion of the economic development and welfare of developing countries as its main objective.

9. Markers (from CRIS DAC form)[2]	General policy objective	Not targeted	Significant objective	Principal objective
	Participation development/good governance	☐	☐	X
	Aid to environment	X	☐	☐
	Gender equality and Women's and Girl's Empowerment [3]	☐	X	☐
	Trade Development	X	☐	☐
	Reproductive, Maternal, New born and child health	X	☐	☐
	RIO Convention markers	**Not targeted**	**Significant objective**	**Principal objective**
	Biological diversity	☐	☐	☐
	Combat desertification	☐	☐	☐
	Climate change mitigation	☐	☐	☐
	Climate change adaptation	☐	☐	☐
10. Global Public Goods and Challenges (GPGC) thematic flagships	N/A			

SUMMARY

Public Finance Management (PFM) and Domestic Revenue Mobilisation (DRM) systems and practices in Mozambique are considered as relatively good, compared to peers, by most independent diagnostics but have demonstrated limited effectiveness on the inclusive and sustainable nature of the economic growth. Over the past years, the EU has played a leading role in supporting the PFM reforms and important improvements on transparency were obtained though this dialogue process. A financing agreement[4] was signed in April 2018 for a EUR 7 000 000 annual action programme (AAP 2017) covering mainly the strengthening of planning and budgeting, execution and external control processes. Transparency concerns and macro-economic slippages linked to the undisclosed debt issue triggered the discontinuation of the International Monetary Fund's (IMF) Policy Support Implementation (PSI) programme in 2016 and subsequently the EU's Good Governance and Development Contract[5] (EUR 200 000 000) in 2018. Through the reprogramming of the NIP funds, followed by the ad-hoc review of the 11th EDF NIP for Mozambique, which foresees the support of macroeconomic and financial stability, EUR 20 000 000 has been allocated for increasing support to PFM and DRM in order to further strengthen the ongoing reforms and related policy dialogue with the Government.

The additional funds allow for an EU engagement in highly relevant new areas such as DRM. Expected revenues from the extractive sector, in particular, the natural gas, could potentially

[2] When a marker is flagged as significant/principal objective, the action description should reflect an explicit intent to address the particular theme in the definition of objectives, results, activities and/or indicators (or of the performance / disbursement criteria, in the case of budget support).

[3] Please check the minimum recommended criteria for the gender marker and the Handbook on the Organisation for Economic Co-operation and Development - Development Assistance Committee (OECD-DAC) gender equality policy marker. If gender equality is not targeted, please provide explanation in section 4.5.Mainstreaming.

[4] Decision C (2017)7585.

[5] Financing Agreement No. MZ/FED/038-077.

add significant fiscal space while also raising new challenges such as more volatile revenues, a risk for a decrease in accountability to citizens and limited diversification of the economy. This action proposes contributing to the necessary reforms to enable Mozambique to maximise the impact of the future revenues and to strengthen revenue collection in the existing mining sector (e.g. by auditing cost declarations and by addressing tax avoidance and evasion).

Another new intervention area is the expenditure management and control. The country has recently build-up a significant stock of arrears to suppliers which reveals major bottlenecks in its treasury management and control system. This action proposes support to authorities to move towards modern treasury practices and systems.

The action also envisages scaling up on-going support to planning and budgeting, public investment management and the external control function. Priority will be the support to the Mozambique Electronic Financial Management System (designated as E-SISTAFE) which has been key for the progress to date. Contributing to the continuous improvements of this electronic system and ensuring more effective use at all levels will be a crucial element for the planned decentralisation foreseen in the recent Constitutional revision[6].

The undisclosed debt scandal has revealed critical major fiscal risks stemming from public investment processes and State Owned Enterprise (SOE) sector. An improved selection process of public investments and strengthened control on SOE´s can contribute to reducing the debt burden and increased fiscal space for social sectors.

This additional support to PFM and DRM is timely and relevant given that the EU recently assumed co-chairmanship of the partners PFM coordination platform (with the IMF). Increased financing for the governments public finance strategy combined with participation in a multi donor World Bank (WB) project, will provide the EU with a privileged position to ensure that evidence and main bottlenecks are fed into the policy dialogue with the authorities.

The emphasis on the natural resources good governance, transparency, accountability and the leverage that EU can have by using policy dialogue, jointly with other donors, will be conducive to contributing to the ultimate goal of inclusive and sustainable economic growth.

The **overall objective** is to contribute to transparency, efficiency and accountability of the DRM and PFM processes. The expected results are as follows:

(i) improved tax policy and management;

(ii) improved strategic allocation and more efficient spending of public funds at central and decentralised level;

(iii) improved performance of the Supreme Audit Institution.

[6] Mozambique's parliament approved in May 2018 constitutional changes with substantial decentralisation of powers. Provincial governors will be selected as from 2019 towards by the party that wins local elections rather than be appointed by the president.

1 CONTEXT ANALYSIS

1.1 Context Description

Mozambique ranks amongst the ten countries with the lowest Human Development Index (180th out of 189 countries in 2018) and the lowest annual GDP per capita (USD 1,136)[7]. In spite of significant progress in poverty reduction since the late 1990's, over 46 % of the population continue to live below the national poverty line[8], and the absolute number of poor has remained relatively constant (11.8 million people) as the population has been growing faster. Inequality and spatial differences have increased. There is a widening poverty gap between rural and urban zones (37.4 % urban poverty compared to 50.1 % in rural areas) and geographical regions (Provinces in the centre and north have poverty rates of nearly 40 points higher than the Province of Maputo). There are concerns that the revenues from the gas mega-projects, expected to come upstream as from 2030 onwards, could further increase inequality if not carefully managed. There is also an increasing feminisation of poverty (63 % of female headed households are poor compared to 52 % of male-headed households). The trends of the main social indicators are positive, but performance remains low compared to its peers; for instance adult literacy stands at 50.6 % and average life expectancy is 58.9 years. Mozambique is continuously facing multiple challenges such as high malnutrition and stunting rates; increasing HIV prevalence rates at 12.3 % (for adults) and wide-spread exposure to malaria.

Mozambique is slowly emerging from a period of elevated macroeconomic volatility two years after the disclosure of the USD 2 billion debt which triggered a significant economic downturn. The economic downturn causes included droughts and floods that hit agriculture production, lower commodity prices affecting mineral exports, and a contraction of Foreign Direct Investment (FDI) inflows as several mega-projects reached completion. These were aggravated by the discovery in 2016 of undisclosed state-guaranteed loans representing 10 % of GDP (approx. USD 1.4 billion) and the resulting breach of trust in the national systems. Stability has been partly re-established, the exchange rates have been stable since mid-2017 and assisted in reducing inflation to a single digit number. Nevertheless, the economic recovery is marked by a reduced growth capacity as GDP growth dropped to a projected 3.3 % for 2018 (much less than 8 % of the preceding decade). Recent trends point to more positive signs for growth in the sector of manufacturing, construction and services.

Major structural challenges persist as Mozambique's economic diversification remains weak. The economy is highly dependent on primary sectors such as mining, forestry, fisheries, natural energy. Manufacturing contributes minimally to GDP (8% in 2016), and the country´s exports consist of mainly unprocessed or semi-processed basic or raw products (mining, agriculture and fisheries). The main challenge lies in reverting the concentration towards the extractive sector (representing 50 % of exports by end 2017), traditionally known for its limited spill-over effect to the population. A recent WB report indicates that continuous weak performance in the non-megaproject economy could keep GDP growth at the 3 to 4 % range until the end of the decade.

The spending on social sectors such as education, health and infrastructure registered a continuous increase as a proportion of GDP over the last decade[9] (to a lesser extend over the

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7 GDP per capita , Purchasing Power Parity PPP (constant international USD), World Bank Data, 2017

8 Income poverty head count using PLEASe methodology. Adjusted foodbasket. Ministry of Economics and Finance. Directorate of Economic and Financial Studies. Poverty and well-being in Mozambique. October 2016.

9 WB PER 2014: since 2009 consistently more than 24 % of total spending was absorbed by the education and health sectors. Also recognising the fact that a considerable part of spending to the health

past 2 years). When comparing spending and development outcomes with peer countries, the Public Expenditure Review (PER) assessment suggests considerable room to improve outcomes given the relatively high spending levels. Specific suggestions for efficiency gains include the need for improved governance mechanisms at the service delivery unit (schools and hospitals), procurement practices, human resources policies, management and value-for money of resources.

The undisclosed USD 2 billion debt had a substantial negative impact not only on the economic development, but also on the trust of international partners and financial markets. The debt relates to non-concessional loans made to three Mozambique commercial companies with a sovereign guarantee. Their discovery, in 2016, lead to the IMF declaring their Policy Support Instrument (PSI) off-track and the filling of a misreporting case. The EU and the other General Budget Support (GBS) donors subsequently terminated their budget support operations (EU in 2018). Under pressure of the IMF and the development partners, the Attorney General commissioned in 2017 an international audit revealing breach of legislation, substantial overpricing, mismanagement and a major information gap. Limited actions were taken regarding accountability in 2018, until in December when the former Finance Minister M. Chang was detained in South Africa. The United States had issued an extradition demand based on accusations of his involvement in the undisclosed debts (as signatory of the guarantees). In early 2019 the Mozambican authorities arrested nine defendants linked to the case, of which eight currently remain in detention awaiting their trial. The current Deputy Minister of Finance, I. Lucas was also recently exonerated for her involvement in the scandal. In March 2019, the Attorney-General initiated judicial proceedings with the High Court of Justice of England against Credit Suisse, Privinvest and other international entities. Mozambique demands, among others, to declare the guarantees for two of the three loans (ProIndicus and MAM) invalid and illegal. The Constitutional Council ruled in June 2019, declaring the nullity of the acts inherent to the loan contracted by Ematum SA, and the respective sovereign guarantee granted by the government in 2013, with all legal consequences.

Regarding relations with IMF, the country remains under Article IV surveillance. An article IV IMF mission took place in March 2019. In April, the IMF approved a USD 118 200 000 Rapid Credit Facility as support in the wake of Cyclone Idai. The loan aims at addressing large budgetary and external financing gaps arising from reconstruction needs after the Cyclones, which caused significant loss of life and infrastructure damage. The mission encouraged the ongoing efforts, with IMF technical assistance, to prepare a diagnostic report[10] of governance and corruption challenges in areas most relevant for economic activity. The IMF also reported on good progress regarding negotiations for a potential Staff Monitored Programme (SMP) which will continue in 2020.

Mozambique remains in "debt distress" since it formally defaulted on the EURO bond beginning 2017 (IMF–World Bank debt sustainability framework). About 80 % of Mozambique's public debt is external (USD 8.7 out of total USD10.3 billion), turning the country extremely vulnerable to exchange rate fluctuations. With the 2016 sharp devaluation of the metical and disclosure of the USD 2 billion debt, the Debt/GDP ratio soared to about 120 %. The recent shift away from external financing and the stronger metical have reduced the public debt stock to approximately 110 % of GDP. Domestic debt poses another risk as it

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sector remains off-budget as this is externally funded. Including these off budget financing, more than 30 % have been consistently executed by both sectors since 2009.

[10] https://www.imf.org/en/News/Articles/2018/04/21/pr18142-imf-board-approves-new-framework-for-enhanced-engagement-on-governance

has increased exponentially and carries a higher cost for the state budget. Negotiations are currently on-going with the bondholders to re-structure the Eurobond (EMATUM). A principle agreement was reached in June 2019, however it still needs to be voted by the bondholders.

Looking ahead, challenges related to fiscal sustainability and macroeconomic risks remain considerable. Fiscal risks continue substantial as state owned enterprises continue to underperform, debts remains in distress and the wage bill, a typically rigid expense, continues to be a significant source of fiscal pressure. In addition, the ongoing electoral cycle and the emerging decentralisation arrangements could have significant budgetary implications conditioning fiscal adjustment in the medium-term.

An additional challenge in the long term is related to Mozambique's demographic trends. The working age population of about 11 million persons is projected to double by 2030. Almost 500 000 persons will enter the labour force per year over the next years, double the rate of the past decade. In addition , the high pace of population growth (3.5 % per year) which is above the economic growth rate (3.1 % in 2017) that is projected to bring the current population (28.9 million) to reach 40 million by 2030 will further challenge the Government provision of basic services (health and education) and infrastructure.

1.2 **Policy Framework (Global, EU)**

The Manila Consensus on PFM adopted in 2011 contributed to shaping PFM-related commitments in Busan. It called on partner countries to be ambitious in strengthening their PFM systems through credible reform programmes and urged development partners to increase the amount of external assistance flowing through a country's PFM system as part of efforts to improve implementation of public policy and its results for sustainable development. It sets out a number of commitments specifically focusing on PFM.

The proposed programme is in line with the Addis Ababa Action Agenda – Financing for development commitments (to strengthening financial systems and economic institutions) and the Paris and Busan Declarations (to stress reliance on country systems and on governance).

The present action will support several relevant EU and global policy frameworks. Above all the action will contribute to the New European Consensus on Development 'our world, our dignity, our future'[11]" which marks the pathway towards achieving the Sustainable Development Goals (SDG) agenda by 2030. The programme responds directly to chapter 4.1 of the New European Consensus on Development: "*Mobilising and making effective use of all means of implementation*" where the EU and its Member States commit to "*step up support to developing countries in their efforts to strengthen revenue mobilisation, debt and public expenditure management, develop tax systems, increase the efficiency and effectiveness of public expenditure and to phase out environmentally harmful fossil fuel subsidies*."

The action also supports the EU-Africa Alliance for Sustainable Development and Jobs[12] that sets up a renewed partnership focused on Africa's economic potential. The action builds on the "EU Growth and Jobs Compact" for Mozambique which identifies the development of public quality infrastructures, and ensuring a stable economic environment as conducive for economic sustainable growth.

[11] OJ C 210 of 30.6.2017.

[12] Communication from the Commission to the European Parliament, the European Council and the Council – Communication on a new Africa-Europe Alliance for Sustainable Investment and Jobs: Taking our partnership for investment and job to the next level. COM (2018) 643 final of 12.9.2018.

The EU Agenda for Change[13] promotes public-sector management for better service delivery, fair and transparent domestic tax systems and governance programmes that support advocacy, awareness-raising and reporting and increase the capacity of control and oversight bodies.

The proposed action is consistent with the 2013 Good Practice Note on Sequencing Public Finance Management (PFM) Reforms and with the EU Staff working document “Collect More/Spend better (CMSP)” as all four critical areas identified in the staff working document on revenue mobilisation and spending have been mainstreamed in the programme.

The initial 11th EDF National Indicative Programme (NIP) included an allocation for complementary support to Good Governance and Development Contract (GGDC) in the areas of PFM and governance for the first focal sector "good governance and development". A financing agreement for the PFM area was signed in April 2018 for EUR 7 000 000. The Budget Support Steering Committee decided in July 2018 to discontinue the GGDC contract. Through the subsequent reprogramming of the NIP funds followed by the ad-hoc review of the NIP, EUR 20 000 000 has been allocated for increasing support the PFM and DRM reforms. The EU has traditionally been supporting the PFM reform agenda and key results have been obtained. The increase in allocation will ensure that the EU remains a key partner for Mozambique. As part of the Financing Agreement signed in April 2018, following results were obtained: (i) hands-on training of about 80 Government officials in the Public expenditure and financial accountability (PEFA) methodology (including a tentative self-assessment); (ii) training of about 80 Government officials in public investment pipeline IT system; (iii) financing of the 2019 PEFA exercise; (iv) signing of two grants; one with the Centre for the Development of the Financial Information System (CEDSIF) and another with the Administrative Court; launching of several tenders under both grants.

The support provided through the additional financing will assist the Government in progressing towards establishing a conducive environment to a potential re-engagement on budget support.

1.3 Public Policy Analysis of the partner country

The Mozambique State is composed out of three types of institutions (i) the central Government; (ii) geographically deconcentrated government entities (provinces and districts); and (iii) autonomous municipalities which are fully independent. A constitutional revision took place in 2018 providing the basis for an advanced decentralisation process whereby the provinces and, in a subsequent phase, the districts would be considered as decentralised entities. The bulk of the legislative framework (but not all) to operationalise this decentralisation process was approved by Parliament in April 2019.

The PFM system is governed by the SISTAFE Law and the regulations (State Financial Management System), approved in 2002 and 2004 respectively. The legal framework has been rated by international assessments as adequate (Public Expenditure Review (PER), PEFA, Tax Administration Diagnostic Assessment Tool (TADAT), Methodology for Assessing Procurement Systems (MAPS) International Monetary Fundy (IMF) diagnostics, etc.). Overall legislation is assessed as adequate and consistent with international norms, however legislation remains marked by contradictions, vague statements and often lacks full implementation. Legislation for the external control was strengthened in 2013/4 promoting greater transparency and clarifying the scope and mandate of the Supreme Audit Institution.

[13] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Increasing the impact of EU Development Policy: an Agenda for Change. COM (2011) 637 final of 13.10.2011.

The procurement decree (05/2016) was adjusted in 2016, simplifying some procedures and limiting the scope for direct awards. In 2017 a decree (77/2017) was adopted for issuing and managing debt. Legislation on the public enterprise sector (03/2018) was approved in 2018, providing the legal basis for enhanced control and oversight of the state owned and participated enterprises.

The Government is implementing its "Five-Year Plan 2015–2019 (*Plano Quinquenal do Governo* - PQG)" which guides the country´s development priorities. This document is structured around five main objectives[14] and three pillars. PFM issues are mainstreamed in two supporting pillars, namely on “consolidating the democratic state, good governance and decentralisation” and “sound and sustainable macro-economic environment”.

A Public Finance Vision (PFV) 2025 was adopted in 2012, setting the long-term targets but lacking a clear prioritisation and sequencing of reforms. These gaps together with the rapidly changing public finance context (high debt and fiscal deficit ratios, stagnating tax ratios and rather limited effectiveness of spending), led the Government of Mozambique (GoM) to elaborate its first Public Finance Strategic Plan (PFSP) 2016-2019. The results of recent PFM diagnostics, mainly the PEFA[15] alimented the identification of priorities and development partners provided important inputs through the PFM Partner´s Coordination Group. The PFSP responds broadly to the need of widening the scope of reforms and identifies as priority reforms: (A) to stimulate savings and private investment, (B) to increase revenue collection, (C) to enhance cautious public resources allocation, (D) to ensure greater rigor in public spending, (E) to improve public assets management, (F) to guarantee sustainability of public debt and (G) to ensure the correct use of the public domain. The proposed action responds to five key objectives of the PFSP. However, a lack of progress reports on the PFSP affects its credibility and demonstrates the need for a strengthened leadership on PFM reforms. Some progress was noted as a Public Finance Committee (PFC) was constituted to coordinate financing of the strategy. This committee is led by the Permanent Secretary of the Ministry of Economy and Finance (MEF) and development partners participate in the bi-yearly meetings (since 2017).

1.4 Stakeholder analysis

The direct beneficiaries are the Ministry of Economy and Finance and the Administrative Court (AC). In the current development context, most of the line Ministries and deconcentrated budget holders (provinces and districts services) will participate in the capacity development efforts foreseen in the action. The line ministries and provincial departments (such as education and health) will be targeted for trainings, seminars, consultations, etc.) and gain from improved “core” PFM and DRM systems. Secondary beneficiaries are the “demand-side” actors of government´s financial and performance information such as Parliament and civil society organisations (CSOs).

The MEF has the leading role for coordinating the implementation of the PFM reforms and in cooperation with the Revenue Authority (AT) coordinates DRM reforms. MEF is the main implementing partner of this programme. The MEF was constituted in 2015 as a result of the merger of two ministries (the Ministry of Planning and Development and the Ministry of

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[14] The five objectives are (i) consolidation of the national unity, peace and sovereignty; (ii) development of human and social capital; (iii) employment and productivity promotion; (iv) development of social and economic infrastructure and (v) sustainable and transparent management of the natural resources.

[15] Namely the IMF Fiscal Transparency Assessment (FTA), IMF PIMA, IMF PFM diagnostics, TADAT, SAI PMF and a repeat PEFA assessment using both the previous (2011) and the new (2016) methodology.

Finance). In addition, the proposed action will have a specific focus on strengthening the Centre for the Development of the Financial Information System (CEDSIF). CEDSIF was a beneficiary of the 10th EDF PFM programme, is an autonomous institution subordinated to the MEF and assigned to orient and coordinate the Public Finance reforms. Following services are CEDSIF´s mandate: implementation and maintenance, promote change management and reforms for the *SISTAFE – Sistema de Administração Financeira do Estado*; support other state organs and institutions in elaborating complementary IT-solutions; training and certification for the Integrated Financial Management Systems (IFMIS) users.

The Administrative Court functions as a Supreme Audit Institution (SAI). The Court is a key stakeholder for accountability and was also a beneficiary of the 10th EDF PFM programme. It has jurisdiction for prior approvals (ex-ante) and to audit all public accounts (also SOE´s). In addition, the Administrative Court also has judicial responsibility to decide on legal implications, to impose fines and/or initiate relevant investigations. The court is implementing its third generation strategic plan - *Plano Estratégico Do Tribunal Administrativo* (PLACOR 2017-2019) - and underwent a quality review system recommended by International Organisation of Supreme Audit Institutions INTOSAI (SAI-PMF), however the review document was not published. Several institutions, such as the IMF and the World Bank refer to the work of the Administrative Court as advanced compared to its peers.

Other key actors in support to PFM and DRM reforms, in particular in strengthening accountability are CSOs. The gender profile for Mozambique published in February 2016 concludes that there are sociocultural factors that discriminate and exclude women from social, political and economic opportunities, particularly aggravated by living in rural areas and illiteracy. The CSO Mapping carried out by the EU Delegation indicates that the level of influence of CSOs, in particular in the elaboration and oversight of the state budget, has increased over the last years. The *Forum de Monitoria do Orçamento* (*FMO*) has played a key role as CSO platform provide analytical documents and conducing high level advocacy for PFM and DRM issues (including tax evasion). CSOs will not directly be involved in the implementation of this action, as their support will be covered under a specific CSO programme (see chapter 3.2).

1.5 **Problem analysis/priority areas for support**

In 2016, Mozambique finalised its 4th national PEFA assessment. The assessment indicated that Mozambique has succeeded in consolidating the major improvements in the PFM system, with improved performance in the areas of budget execution, accounting, reporting and internal audit. The assessment points at a performance deterioration in two areas of PFM and DRM, respectively: the comprehensiveness of budget documentation and the effectiveness of tax arrears collection. Core PFM areas where performance remains below standards are procurement, the quality of medium term planning and budgeting, and external scrutiny and audit. This report also includes a baseline for the new 2016 PEFA framework with analysis on three relevant areas: Public Asset Management (PAM), Public Investment Management (PIM) and a credible fiscal strategy for which the later two register a weak performance.

The country has embarked over the past decade on high risk public investments with questionable link to public policy priorities and value for money. A series of PIM reforms were initiated in 2013, with support of the World Bank, and led to the adoption of tools[16] and enhanced capacity in the MEF. However many bottlenecks remain as WB recently reported that in 2018 around 115 projects were received, out of which only 19 projects met the

16 Such as public investment evaluation and selection procedures; a selection committee, etc.

standards. Limited institutional and human capacities and a lack of legal enforcement continue to hamper effective implementation of this reform.

The path towards more sustainable debt remains challenging. A "Debt Management Performance Assessment" was conducted by the World Bank in 2018 and resulted in a "debt management action plan". A decree on contracting public debt and issuing guarantees was adopted in 2017. This decree requires a firmer debt contracting process (ratification by the Council of Ministers) and reinforces transparency by reporting requirements. Some progress is noted on transparency as basic reporting on debt seems to be re-established in 2019. Furthermore, in April 2018 a new law on State participated companies was adopted by Parliament. This law required majority (>50 %) state owned enterprises to adopt rules on management, governance and transparency which are in line with OECD good practices. This law is applicable since August 2018 and some initial steps have been noted such as transparent board nomination procedures for *Electricidade de Moçambique* and the publication of a Fiscal risk statement in 2019. It remains, however, unclear which entity will lead on these reforms and how implementation will be enforced. Support to and fast tracking of the implementation of these new legal instruments should be a priority in the coming months.

More recently a liquidity crisis, triggered by weak cash management has affected sound public financial management practices. The liquidity crisis caused the build-up of large arrears, both to creditors and to local suppliers. Government estimates place the stock of domestic arrears to suppliers at 3.8 % of GDP at end 2016, equivalent to the budget allocated to health spending for 2018. The authorities, with technical support from the IMF, elaborated an action plan to address and prevent arrears in 2018. As a first step an audit on existing arrears was conducted resulting in about 60 % of the suppliers invoices certified as eligible. The high level of arrears has affected supplier´s confidence to provide goods and services and has reduced access to cash in the economy. Urgent reforms are needed to move away from cash rationing to modern treasury management practices. IMF is providing technical assistance on the subject and the WB project will support capacity building and development of modern tools and practices.

Most analytical documents on the country´s economic framework point to the risk of the country becoming trapped in the "resource curse" given the weak capacity and institutions for managing the expected revenue from the extractive industry. Mozambique has experienced rapid development of its petroleum sectors, with vast offshore discoveries of natural gas, placing the country as the third-largest proved natural gas reserve holder in Africa, after Nigeria and Algeria. The start of gas production is expected around 2024. A strong reform drive is needed to ensure Mozambique is able to maximise the benefits as considerable gaps in the policy environment and administration remain. Political willingness to create inclusive growth is also important. In this context, policy dialogue could play an important role in view of good governance in the natural resources management. The country needs to develop: 1) a macro-fiscal framework integrating natural resource revenue flows, 2) a framework to efficiently and transparently manage savings, 3) capacity for an expected ramp up in public investment, 4) a tax policy framework for the mid- and downstream gas sector and 5) a macroeconomic policy framework including monetary and exchange rate policy that is adjusted to the new environment.[17]

Finally, a gradual process for the recently adopted decentralisation legislation will be important to avoid service delivery issues and additional pressure on the limited fiscal space.

[17] Managing Natural Resource Wealth Thematic Fund, fiscal year 2019, mid-year report, IMF.

Significant efforts and resources are require to draft and implement the necessary legislation, new intergovernmental fiscal arrangements, and institutional and PFM capacity building to help these subnational governmental entities fulfil their new mandates.

2 RISKS AND ASSUMPTIONS

Risks	Risk level (H/M/L[18])	Mitigating measures
Political risk: • political instability related to the elections, • limited political leadership for PFM and DRM reforms.	**M**	• Ensure sufficient time for project implementation so that eventual delays due to limited mobility can be mitigated, • continue advocacy for PFM and DRM reforms throughout policy dialogues (both through the PFM as through the GBS platforms).
Macro-economic risk: • volatility of the national currency (MZN)/difficulty budgeting and execution processes, • high inflation**.**	**M**	• Procurement processes should provide for clauses to limit the impact of the volatility of the national currency and high inflation.
Developmental risk: • need for improved strategic leadership for the PFM and DRM reforms (among the different reformers), • human resources capacity issues (high turn/over, lack of career management, etc.), • limited effectiveness of trainings given high rotation of staff, • poor coordination support both within Government and between donors lead to ineffective interventions.	**H**	• Increased involvement and coordination by the National Authorising Officer (NAO) for the Financing Agreement implementation, • ensure linkage with the Public Finance Committee (PFC) and actively contribute to the coordination with other development partners (see 3.2), • advocate for improved training strategies to reduce the impact of the high turn/over, • support efforts to advance on career management, • use existing donor working groups at high level as instruments to ensure effective buy in and coordination of reform interventions, • the proposed programme arrangements (steering committee will ensure effective coordination between key GoM players on the programme).

[18] High (H), medium (M), low (L).

Corruption risk: Risk of financial losses due to misappropriation or fraud and electoral cycle pressures.	**H**	• To include requirement on expenditure verification reports for each pre-financing for grants managed by public entities; grants ensure that spending is only eligible for agreed and earmarked activities, • implementation of EU programme: Support to fight corruption in MZ/FED/039-688.

Assumptions
• Macro-Economic stability, • political stability during elections in 2018 and 2019, • political support from GoM to tackle the procurement issue, • improved Public Finance Strategic Plan 2020-2024 with yearly progress reports, • the authorities continue and beef up their set-up for PFM and DRM governance, • strong EU and international community engagement to support a national dialogue on economic governance and on inclusive growth, • stronger coordination among donors to support government plans, • stronger collaboration between various departments in the Ministry of Economy and Finance and with the Revenue Authority that lead to more informed policy making, • more evidence and research feeds into policy and planning.

3 LESSONS LEARNT AND COMPLEMENTARITY

3.1 Lessons learnt

From the PFM reform programme under the 10th EDF, following lessons were learned:

- The impact of trainings for budget holders remains hampered by a high staff turnover rate (mainly at provincial and district level). Consequently the professionalisation of the IFMIS users should be priority for the coming years (monitoring mission finding);
- Extensive diagnostics are not always cost efficient and risk to deviate the attention from implementing solutions and cause implementation delays (ROM finding);
- Alignment of the EU actions to national systems and instruments was appreciated, however, could be further encouraged in a next phase (Steering Committee feedback);
- Technical assistance (TA) can provide added value but is best formulated around specific deliverables instead of long term resident TA (Steering Committee);
- Close coordination with other partners active in PFM contributed to increased effectiveness of the policy dialogue;
- There is scope to improve the NAO´s involvement.

The independent BS evaluation carried out in 2015 recommends consolidating and deepening the progress achieved in macroeconomic management, in PFM reform and in the improvement of transparency and accountability. For macroeconomic management, the evaluators pointed to the need for on greater attention to the framework for investment selection and to reinforce the institutional arrangements for the coordination and leadership of the PFM reforms.

The European Court of Auditors (ECA) issues in 2016 a special report[19] on the use of budget support to improve domestic revenue mobilisation in sub-Saharan Africa and Mozambique was one of the case studies. One of its main recommendations is to increase the EU´s engagement on DRM as its critical the EU´s objectives.

3.2 **Complementarity, synergy and donor coordination**

Complementarity is ensured with following EU programmes/initiatives:

- The "fight corruption in Mozambique" programme of the 11th EDF which will (i) support the strengthening of judicial institutions to prevent and fight corruption and bring corruption cases to justice and (ii) Supporting justice professional associations, civil society and involve media; (MZ/FED/039-688).
- The "Support to consolidation of Democracy" which will provide support to electoral processes and capacity-building for new elected and their institutions/bodies which is important for the oversight and accountability aspect of the public finances. (MZ/FED/040-700).
- The "Support to the Consolidation of Peace in Mozambique" will provide support the consolidation of the ongoing peace process, through a comprehensive framework of interventions which will be split in different financing agreements: (1) support to livelihoods in conflict-affected areas (rehabilitation) – AAP 2019 (MZ/FED/041-899); (2) decentralisation; (3) reconciliation and (4) disarmament, demobilisation and reintegration (DDR). Only the first component will be part of AAP 2019, the later will be decided in 2020.
- Regional programmes such as the EU PALOP-TL[20] which focuses on peer learning and exchange of best practices for the Ministry of Economy and Finance, Supreme Audit Institution (SAI), Parliament and Civil Society (MZ/FED/039-765).
- Complementary support to CSOs is provided through the Support Programme to Non State Actors in Mozambique: participation for inclusive growth (*Programa de Apoio aos Actores Não Estatais* PAANE II). The CSO Platform for Budget monitoring (FMO) receives a direct grant to enhance their capacity on budget dialogue and monitoring as part of this programme (MZ/FED/039-385).
- Funding is provided to the IMF through the AFRITAC South (Regional Technical Assistance Centre in Southern Africa) and the Natural Resource Wealth Thematic Fund (MNRW). Coordination with the IMF´s is ensured through regular briefings organised in country.
- WB has two other projects that are complementary to this project, a Decentralisation project and Economic Management for Inclusive Development project (supporting the public investment reform, among others).

The 2018 PFM/ DRM partner´s mapping reveals that about 11 agencies (including the IMF and the United Nations (UN)) provide support accounting for an estimated USD 44 000 000 during the period 2017-2020. The support is operationalised through a variety of modalities (basket funds, projects, TA, thematic funds, etc.) and covers the entire budget cycle. Majority of the funds are directed to the statistics and tax area. Budget and planning has been rather

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[19] ECA, 35/2016 Special Report: "The use of budget support to improve domestic revenue mobilisation in sub-Saharan Africa", https://www.eca.europa.eu/Lists/ECADocuments/SR16_35/SR_REVENUE_IN_AFRICA_EN.pdf

[20] *Países Africanos de Língua Oficial Portuguesa e Timor-Leste.* PALOP is the group of Portuguese-speaking African countries, comprising Angola, Cape Verde, Guinea Bissau, Mozambique and São Tomé and Príncipe, and Timor Leste since 2005. PALOP integrated the African Caribbean and Pacific (ACP) Group in 1985.

marginal in receiving external funds, as well as budget execution. This overview does not take into account yet the planned WB Public Revenue, Expenditure, and Fiscal Decentralisation Enhancement and Reform (PREFER) project as it is still in design phase.

Complementarity with other development partners is ensured through the different working groups. The overarching coordination is through the PFM Coordination Group to which 11 agencies participate and where strategic issues are discussed as well as dialogue with authorities is ensured. The EU assumed co-chairmanship of this group in 2019, together with the IMF. There are various subgroups reporting to the PFM Coordination Group. By joining forces with other partners, EU´s impact on the policy dialogue will also be enhanced. For instance by contributing to the WB PREFER project, the EU will be in a privileged position to ensure that evidence generated within the programme and main bottlenecks are fed into the policy dialogue.

The support to the Tax Authority is coordinated by the tax working group. Financing is channelled through a basket fund managed by the tax authority (with Switzerland and Norway contributing). Separate technical assistance is provided by Department for International Development (DFID), IMF and Spain. All donors are represented in the working group.

The support to the SISTAFE reform is coordinated by the CEDSIF working group. Financing is channelled through a basket fund managed by CEDSIF (with Italy and Denmark contributing).

Partner´s support to the external audit area is coordinated by the audit working group and is based on the strategic plans of the Administrative Court (the strategic plan is designated "PLACOR"). Majority of funds are channelled through a basket fund implemented by the Court and coordinated by Sweden (with contributions from Ireland). The EU, WB, France and the German development agency *Deutsche Gesellschaft für Internationale Zusammenarbeit* (GiZ) support earmarked activities of the strategic plan. GiZ´s programmes provide valuable financial support as well as technical assistance. GiZ is also a strategic partner to the proposed PFM/DRM programme.

Budgetary policy analysis is ensured mainly through the Budget Analysis Group (BAG) to which the EU actively participates.

4 DESCRIPTION OF THE ACTION

4.1 Overall objective, specific objective(s), expected outputs and indicative activities

Overall objective: is to contribute to transparency, efficiency and accountability of the DRM and PFM processes.

Specific objective 1: Improved tax policy and administration. This objective addresses the Public Finance Strategic Plan objective B: "*Aumentar a arrecadação das receitas do Estado*" (to increase revenue collection);

Specific objective 2: Improved strategic allocation of public funds and a more efficient spending at central and decentralised level. This objective addresses the Public Finance Strategic Plan objectives C: "*Assegurar a afetação criteriosa dos recursos*" (ensure the careful reallocation of resources) and D: "*Garantir maior eficiência na execução da despesa pública*" (to ensure better efficiency in the implementation of the public expenditure).

Specific objective 3: Improved performance of the Supreme Audit Institution. This objective addresses the Public Finance Strategic Plan objective G: "*Assegurar a correcta utilização da coisa pública*" (to ensure the correct use of the public good).

For Specific Objective 1, the expected outputs are:

1.1 Enhanced capacity for tax policy formulation: to engage in revenue forecasting, impact assessments of policy measures, to formulate coherent, transparent, and participatory tax policies;

1.2 Improved procedures and capacity for tax administration, in particular on tax audits. (focussing on a risk based approach and the extractive industries sector);

1.3 Automated tax systems: E-taxation system fully operational and rolled out with improved business process.

For Specific Objective 2, the expected outputs are:

2.1 Developed and rolled-out IT Systems for Planning and Budgeting Module (MPO), and the State Management Human Resources (SNGRHE);

2.2 Enhanced information on budget documents (improved formats) and public investment projects;

2.3 Control processes for the different phases of expenditure chain re-established: Improved cash flow forecasting and procurement processes;

2.4 Improved intergovernmental fiscal transfer modalities (for the repartition of State transfers to subnational entities reformed).

For Specific Objective 3, the main expected outputs are:

3.1 Increased capacity to produce audit reports and publish citizen briefs (based on PEFA PI - 30 indicator);

3.2 Improved capacity to ensure a risk based audit report on the state accounts (focus on Public Investment, State Owned Enterprises, extractive industry and Public Private Partnerships PPPs);

3.3 Improved managerial capacity of the TA.

Indicative Activities:

This programme will ensure an adequate mix of instruments such as the provision of capacity building, technical assistance, financial support for the acquisition of equipment and software's (through grants), and a results based financing tool. The results based financing aims at enhancing a performance based culture.

(i) *Results Based Financing:* A component under the WB Public Revenue, Expenditure, and Fiscal Decentralisation Enhancement and Reform (PREFER) project. Through results-based financing, the programme aims at addressing bottlenecks, creating incentives for inter-ministerial collaboration, and rewarding successful reforms within MEF directorates, AT and other relevant PFM/ DRM institutions. About 60 % of the funds of the WB will be disbursed through the Disbursement Linked Indicators (DLI). This mechanism will allow for necessary capital and recurrent investments of GoM necessary to continue with the initiated reforms. Increased funding will be made available to incentivise government agencies for improving public sector performance, based on externally verified compliance with DLI annual targets. A set of specific DLIs within these areas will be formulated and eligible expenditures identified with the Government and participating development partners during pre-appraisal. The selected DLIs will be mainly output indicators such as implementation of PFM and DRM systems, adherence to guidelines and policies, and adoption of laws and regulations.

An independent verification agency will be contracted on a yearly basis to conduct verification for all project DLIs prior to submission to the WB. The WB, with the advice of the WB PREFER project contributing development partners, will retain the right to make the final decision as to whether a DLI has been achieved according to the criteria established within the Project Appraisal Document (PAD) or not.

(ii) *Capacity building/technical Assistance*: An important part of the activities will relate to policy reviews, reform guidance, developing and providing training on manuals, templates, and standards. Comprehensive capacity building will be ensured through coaching, orientation, and peer learning and conducting analytical work to inform ongoing reforms. This technical assistance can also potentially provide support for the functioning of the PFM Working Group. Specific capacity building activities by objective can include:

Objective 1- improved tax policy and management: This component will finance technical assistance (WB PREFER project) to the Tax Authority and MEF Directorate for Economic and Financial Studies (DEEF) around:

- Short-, medium-, and long-term revenue forecasting;
- Tax impact analysis; among others on tax exemption and profit sharing and profit shifting to low-tax jurisdictions;
- Strengthening the capacity of the (recently created) extractive industries unit at the Tax Authority to improve among others tax audits (focussing on a risk based approach and the extractive industries sector);
- harmonisation of tax legislation;
- support to strengthening of core functions of tax administration—registration, filing and payment, arrears management, auditing, and appeals and citizen services;
- Greater integration of IT solutions (i.e., *e-Tributação*, e-filing, *Portal dos Contribuintes*, JUE, etc.);
- Strengthening national and subnational level capacity, through professional training, peer learning, and change management.

Objective 2- improved strategic allocation and more efficient and effective spending of public funds at central and decentralised level. This component will finance technical assistance to support MEF directorates, the procurement authority (UFSA), and budget holders (including subnational entities) on:

- development of tools for financial programming;
- improving tools/processes for commitment control;
- providing capacity building to sector ministries on the changes in the budget execution process (procedures, processes, etc.) and associated e-SISTAFE controls, and conducting change management related activities;
- strengthening IT (revision of the procurement business process and connection to budget execution system);
- improving the transparency of official procurement data (online portal);
- establishing a coherent intergovernmental fiscal transfers system;
- revising and strengthening procedures for the execution and monitoring of local budgets to increase the effectiveness of public expenditures at the local level;
- contributing with other development partners to the updating of relevant diagnostics (e.g., subnational PEFAs or Public Expenditure Reviews).

Objective 3- Improved performance of the Supreme Audit Institution will be implemented through financing of a grant. Activities will concentrate on:

- capacity building for auditors on topics of extractive industries, on PPPs and on conducting risk based audits;

- capacity building for auditors to ensure access to and participation in the international certification process;

- contracting of consultants to increase the number of auditors;
- acquisition of equipment for auditors;
- acquisition of complementary IT functionalities for previously EU financed software's.

(iii) A horizontal Capacity Development Facility (CDF) has been set up to support the implementation of this action (under the existing Financing Agreement). This CDF is a flexible tool to mobilise resources to ensure added value to the PFM policy dialogue. In 2018 and 2019 this facility financed training on the PEFA and Public Investment Management (main diagnostic tool for PFM) as well as the 2019 PEFA assessment (expected to start in July 2019). This facility will be crucial to provide flexible means to implement PEFA recommendations or any PFM reforms for which no support is foreseen under the other implementation modalities.

The beneficiaries, MEF (including subordinated institutions), the Administrative Court and civil society organisations can access this facility to mobilise in an efficient and effective manner high level technical expertise for specific deliverables. The Technical Committee established the modus operandi of this fund in 2018. The request for support is to be sent to the NAO that, together with the EU, ensures a screening of the relevance, added value and implementation options.

4.2 **Intervention Logic**

The hypothesis of the programme is that improved PFM/ DRM performance, including better cash flows, less arrears, more efficient procurement, as well as a better oversight and scrutiny of the budget will lead to better fiscal discipline, increased revenues and enhanced efficiency of planning, allocating and spending the budget. These achievements will be possible, if the core assumptions as indicated in the risk matrix are maintained. The above improvements may also contribute to the reduced debt accumulation, improved fiscal space for viable and sustainable investment projects, which can steer towards a more inclusive and sustainable economic growth.

The intervention logic has three objectives: i) it aims at increasing the revenue mobilisation ("Collect More"); ii) it will strengthen the strategic resource allocation, as well as tackling specific bottlenecks for a more efficient spending ("Spend Better"); and iii) it will enhance the scrutiny on public finance by a more risk-based and transparent external control function.

Two cross cutting aspects are mainstreamed throughout the three objectives, namely (i) transparency and (ii) a focus on the extractive industry.

- Budget transparency gives opportunity to the citizens to access information on government revenues, allocations and expenditures. This provides evidence to advocate more effectively for equitable resource allocations and fulfil COS´s role as watchdog. Transparency on tax policy and management can increase the social pressure on non-compliant companies, excessive tax exemption and raise awareness on the tax gap. Transparency on the external audit function can increase the pressure for compliance.

- Secondly, Mozambique is presented with an opportunity to accelerate its sustainable development process given the expected stream of extractive sector revenue (as from 2023 onwards). The increased revenues will only translate into development if appropriate processes and systems are in place. The programme aims at strengthening tax policy and administration for extractive industry, improving the appraisal process of public investments, contributing to transparent and fair procurement processes and finally the external control function´s capacity to audit high risk transactions (i.e. the extractive sector, revenue and spending side).

Finally, the emphasis on the resources management of the extractive industry and the EU´s leverage with policy dialogue, jointly with other donors, will be conducive to contributing to the ultimate goal of inclusive and sustainable economic growth.

4.3 Mainstreaming

Mozambique adopted commitments to address gender issues and to promote gender equality. The country registered improvements in women’s position, especially at central level (with 36 % of female Parliament Members), however progress at local level seems less prominent. The Report on "*Beijing+20"* highlights many remaining gender gaps such as female poverty, secondary education (early marriages), female health issues, etc.

Environment and climate change is one of the five priorities identified in the PQG (2015-2019), "*to ensure sustainable management of natural resources and the environment*". This environmental boost in Government's plan is expected to ease the way for enhanced consideration of environmental aspects related to public investment management decisions and the extractive industry (related to environmental sustainability).

Both gender and environment will benefit from improved planning and budgeting systems as well as improved credibility of the budget (which is one of the main PFM reform objectives). By strengthening the programmatic budgeting process more consistent and credible budget information will be publicly available. This will contributed to improved tracking and analysis of cross/cutting issues which can feed back into improved policy definition in these areas (as well as others).

Human rights are indirectly supported by mainstreaming transparency in the three specific objectives of the programme. Enhanced transparency of public funds will increase access to information for human rights angle.

Gender, resilience and conflict sensitivity, environment and climate change and human rights are not main targets of the intervention. However, they will be promoted by improving the budget and planning systems, by encouraging female participation to trainings and by increased use of information and communication technologies (and consequently reduce the use of paper) for the different budgetary processes. This process will be enhanced by ensuring a yearly dissemination/consultation session with the CSO Budget Monitoring Platform (FMO) on the progress of the programme. A specific meeting will be organised with a representative of this CSO platform to present progress and consult CSOs on future priorities for PFM and DRM reforms (this ideally should be done through the PFSP processes). Coordination will be ensured with the recently approved Support Programme to Non State Actors in Mozambique: "participation for inclusive growth" (PAANE II).

4. 4 Contribution to SDGs

This intervention is relevant for the 2030 Agenda for sustainable development. It contributes primarily to the progressive achievement of SDG(s) Goal 16 target "*Develop effective, accountable and transparent institutions at all levels*", but also promotes progress towards Goal 8 " *Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all*" and SDG Goal 17: "*Revitalise the global partnership for sustainable development*".

5 IMPLEMENTATION

5.1 Financing agreement

In order to implement this action, it is foreseen to conclude a financing agreement with the partner country.

5.2 Indicative implementation period

The indicative operational implementation period of this action, during which the activities described in section 4 will be carried out and the corresponding contracts and agreements implemented, is 84 months from the date of entry into force of the financing agreement.

Extensions of the implementation period may be agreed by the Commission's responsible authorising officer by amending this Decision and the relevant contracts and agreements.

5.3 Implementation of the budget support component

N/A

5.4 Implementation modalities

The Commission will ensure that the EU appropriate rules and procedures for providing financing to third parties are respected, including review procedures, where appropriate, and compliance of the action with EU restrictive measures[21].

5.4.1 *Grants: (direct management)*

(a) Purpose of the grant(s)

The grant´s purpose is to achieve the **Specific Objective 3** "enhanced accountability". The fields of intervention, the expected results and related activities are listed in section 4.1 and 4.2. will be to provide capacity building and technical assistance for the internal control and IT systems and to improve the audit capacity for extractive industries, PPPs and SOE´s. Procurement of some minor IT elements (hardware and software) and other equipment is also foreseen.

(b) Type of applicants targeted

The types of applicants targeted are: the Administrative Court which is part of the Judiciary power. In agreement with the NAO this grant is managed directly as it's an independent institution.

(c) Justification of a direct grant

Under the responsibility of the Commission's authorising officer responsible, the grant may be awarded without a call for proposals to the Administrative Court (designated as the "*Tribunal Administrativo*"). Under the responsibility of the Commission's authorising officer responsible, the recourse to award of a grant without a call for proposals is justified because the beneficiary is in a de jure monopoly situation as the Administrative Court was created by the Constitution of Mozambique to act as the Supreme Audit Institution. This role cannot be performed by any other public or private entity. The Administrative Court is the only potential candidate for the action.

[21] www.sanctionsmap.eu Please note that the sanctions map is an IT tool for identifying the sanctions regimes. The source of the sanctions stems from legal acts published in the Official Journal (OJ). In case of discrepancy between the published legal acts and the updates on the website it is the OJ version that prevails.

5.4.2 *Indirect management with an international organisation*

A part of this action may be implemented in indirect management with the International Development Association (IDA) World Bank Organisation. The implementation by this entity entails support to the WB Public Revenue, Expenditure, and Fiscal Decentralisation Enhancement and Reform (PREFER) project on PFM/ DRM that will be established by end 2019. Support to this PREFER project will ensure the partly achievement of the **Specific Objective 1**: "**improved tax policy and management"**, in particular outputs 1.1 and 1.2 (see chapter 4). Financing through this entity will also partly contribute to achieving **Specific Objective 2 "budgeting and spending",** in particular outputs 2.3 and 2.4 **(**see chapter 4). Both objectives will be operationalised through the provision of technical assistance, supply of tools, capacity building and Results-Based Financing. The envisaged entity has been selected using the following criteria: experience related to the indicated areas, value added, mixture of tools (technical assistance and results based financing).

If negotiations with the above-mentioned entrusted entity fail, the part of this action may be implemented in indirect management with an entrusted entity.

5.4.3 *Indirect management with the partner country*

A part of this action with the **Specific Objective 1**: "**improved tax policy and management**" in particular output 1.3 and **Specific Objective 2**: "**"budgeting and spending", in particular** outputs 2.1 and 2.2 (see chapter 4)**,** may be implemented in indirect management with the Republic of Mozambique according to the following modalities:

The partner country will act as the contracting authority for the procurement and grant procedures. The Commission will control ex- ante all the procurement and grant procedures. Payments are executed by the Commission.

The partner country shall apply the Commission’s rules on procurement and grants. These rules will be laid down in the financing agreement to be concluded with the partner country.

5.5 **Scope of geographical eligibility for procurement and grants**

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply, subject to the following provisions.

The Commission’s authorising officer responsible may extend the geographical eligibility on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realisation of this action impossible or exceedingly difficult.

5.6 Indicative budget

Budget line	**EU Total contribution (in EUR)**
5.4.2 Indirect Management with WB	9 500 000
5.4.3 Indirect Management with the partner county	11 000 000
5.4.1 Grants (direct management)	3 300 000
5.9 Evaluation 5.10 – Audit	400 000
5.11 Communication and visibility	500 000
Contingencies[22]	2 300 000
Total	**27 000 000**

5.7 Organisational set-up and responsibilities

A Steering Committee meets once a year to decide the overall direction of the project, to monitoring the indicators and to supervise the overall implementation of the programme. Additional meetings can be arranged ad hoc at the request of the Delegation or any of the other members. The committee is chaired by the National Authorising Officer (NAO) with the participation of all implementing partners (MEF, CEDSIF, Administrative Court and the World Bank). A separate meeting will be organised with a representative of a CSO platform on PFM and DRM issues to present progress and consult CSOs. Coordination will be ensured with the Support Programme to Non State Actors: PAANE II.

The Delegation and the Steering Committee will be supported in their work by technical committees for each of the three main components of the programme.

- Objective 1 and 2: The Technical Committee for the support to SISTAFE reform programme will be the Partnership Committee set up to provide oversight of the SISTAFE Reform joint financing mechanism. The functioning of this Partnership Committee (PC) is outlined in the Memorandum of Understanding between the supporting development partners and CEDSIF. The EU Delegation participates as observer to this PC and the IMF is an ex officio member. The PC meets at least twice a year and assesses the progress and financial reports, discusses the audit report, and approves the annual plan and budget for the overall SISTAFE Reform Programme. To ensure coherence and consistency, the PC will be informed of the work plan and progress reports produced in relation to the grant for the benefit of the NAO and the Commission.
- Objective 3: The Technical Committee for the support to the Administrative Court will be the Partnership Committee (PC) set up to provide oversight of the TA's Joint financing mechanism. The functioning of this PC is outlined in the Memorandum of Understanding between the supporting development partners and the Administrative Court. The EU Delegation participates as observer to the PC. The PC meets at least twice a year and assesses the progress and financial reports, discusses the audit report, and approves the annual plan and budget. To ensure coherence and consistency, the PC will be informed of

[22] Consider that contracts where no financing agreement is concluded, contingencies have to be covered by individual and legal commitments by 31 December of N+1.

the work plan and progress reports produced in relation to the grant for the benefit of the NAO and the Commission.

- Transversal component 3: A Capacity Development Facility Technical Committee has been established to support the NAO in the planning and the supervision of its implementation. The Technical Committee includes a representative of the NAO and the EU Delegation; CEDSIF, TA, MEF are invited as observers. It meets on a semestral basis and has approved Terms of Reference, the appraisal criteria, and a format for submission of requests.
- The World Bank is preparing a Public Revenue, Expenditure, and Fiscal Decentralisation Enhancement and Reform (PREFER) Project to support two critical objectives within Government of Mozambique's (GoM) Strategic Plan for Public Finances (PEFP, 2016-2019): increasing revenue collection (Objective B) and guaranteeing greater efficiency in the execution of public expenditure (Objective D). The PREFER entails an investment policy financing (IPF) instrument with Disbursement Linked Indicators (DLIs) and the provision of technical assistance. A governance structure for the project will be designed during project appraisal and established prior to project effectiveness. These arrangements will involve a Steering Committee, to ensure political leadership, as well as a Technical Committee, to facilitate and support cross-institutional coordination and collaboration. The specifics of both committees will be elaborating within the Project Appraisal Document (PAD).

5.8 **Performance and Results monitoring and reporting**

The day-to-day technical and financial monitoring of the implementation of this action will be a continuous process, and part of the implementing partner's responsibilities. To this aim, the implementing partner shall establish a permanent internal, technical and financial monitoring system for the action and elaborate regular progress reports (not less than annual) and final reports. Every report shall provide an accurate account of implementation of the action, difficulties encountered, changes introduced, as well as the degree of achievement of its results (outputs and direct outcomes) as measured by corresponding indicators, using as reference the Logframe matrix (for project modality).
Reports shall be laid out in such a way as to allow monitoring of the means envisaged and employed and of the budget details for the action. The final report, narrative and financial, will cover the entire period of the action implementation.
The Commission may undertake additional project monitoring visits both through its own staff and through independent consultants recruited directly by the Commission for independent monitoring reviews (or recruited by the responsible agent contracted by the Commission for implementing such reviews).

5.9 **Evaluation**

Having regard to the importance of the action, mid-term and final evaluations will be carried out for this action or its components via independent consultants contracted by the Commission.

The mid-term evaluation will be carried out for problem solving and learning purposes, in particular with respect to adequate actions for mobilising the contingency allocation and assessing the effectiveness of the results based financing component of the WB PREFER project.

The final evaluation will be carried out for accountability and learning purposes at various levels (including for policy revision), taking into account in particular the fact that an innovative component was applied, namely the results based financing of the WB PREFER project.

The Commission shall inform the implementing partner at least 2 months in advance of the dates foreseen for the evaluation missions. The implementing partner shall collaborate efficiently and effectively with the evaluation experts, and inter alia provide them with all necessary information and documentation, as well as access to the project premises and activities.

The evaluation reports shall be shared with the partner country and other key stakeholders. The implementing partner and the Commission shall analyse the conclusions and recommendations of the evaluations and, where appropriate, in agreement with the partner country, jointly decide on the follow-up actions to be taken and any adjustments necessary, including, if indicated, the reorientation of the project.

Evaluation services may be contracted under a framework contract.

5.10 Audit

Without prejudice to the obligations applicable to contracts concluded for the implementation of this action, the Commission may, on the basis of a risk assessment, contract independent audits or expenditure verification assignments for one or several contracts or agreements.

It is foreseen that audit services may be contracted under a framework contract.

5.11 Communication and visibility

Communication and visibility of the EU is a legal obligation for all external actions funded by the EU.

This action shall contain communication and visibility measures which shall be based on a specific Communication and Visibility Plan of the Action, to be elaborated at the start of implementation.

In terms of legal obligations on communication and visibility, the measures shall be implemented by the Commission, the partner country, contractors, grant beneficiaries and/or entrusted entities. Appropriate contractual obligations shall be included in, respectively, the financing agreement, procurement and grant contracts, and delegation agreements.

The Communication and Visibility Requirements for European Union External Action (or any succeeding document) shall be used to establish the Communication and Visibility Plan of the Action and the appropriate contractual obligations.

It is foreseen that a contract for communication and visibility may be contracted under a framework contract.

6 PRE-CONDITIONS

N/A

APPENDIX - INDICATIVE LOGFRAME MATRIX (FOR PROJECT MODALITY) [23]

	Results chain: Main expected results (maximum 10)	Indicators (at least one indicator per expected result)	Sources of data	Assumptions
Impact (Overall Objective)	Improved transparency, effectiveness and efficiency of the revenue collection and public resources management by strengthened systems and processes.	OO1. Revenue/Gross Domestic Product (also adjusted); OO2. Aggregate expenditure Out-turn compared to original approved budget (PEFA PI-1) * OO3. Composition of expenditure Out-turn compared to original approved budget (PEFA PI-2)* OO4. PEFA: PI-15 Revenue Budgeting* OO5. Open Budget Index (OBI) *	OO1. Balanço do Plano Economico Social (BdPES), State Accounts; OO2-4. PEFA reports; OO5. OBI reports.	*Not applicable*
Outcome(s) -Specific Objective 1	SO1: improved tax policy and revenue administration.	SO 1.1. PEFA: PI 19 Revenue Administration compliance*/ (** EU RF 2.30) SO 1.2. % of taxpayers registered/paying through the portal and E-taxation	SO1.1 - 1.2 PFSP implementation reports; BdPES/State Accounts/Budget; PEFA reports, AT implementation reports.	Authorities maintain the PFM dialogue; the training centres handle the project's deliverables for longer-term capacity programmes; Governments respect the PFSP monitoring processes and remain committed to PFM reforms; prudent macroeconomic and monetary policies.

[23] Mark indicators aligned with the relevant programming document mark with '*' and indicators aligned to the EU Results Framework with '**'.

Outcome(s) -Specific Objective 2	SO2: Improved strategic allocation and more efficient spending of public funds at central and decentralised level.	SO 2.1 PEFA: PI-4: classification of the Budget;* SO 2.2 PEFA: PI-9: Public access to key Fiscal information* SO 2.3 Discrepancy between State Budget and MTEF limits SO 2.4 PEFA PI-24 Transparency, competition and complaint mechanisms in procurement;* SO 2.5 PEFA PI-11 – Public Investment management; nr of the largest investment projects approved and selected based upon the criteria of the manual on selection of projects;* (SO2.1. – SO2.5. ** EU RF 2.30)	SO 2.1-2.5: PFSP implementation reports; BdPES/State Accounts/Budget Execution Reports; PEFA reports; CEDSIF implementation reports; WB implementation reports.	The training centres handle the project's deliverables for longer-term programmes; Governments respect the PFSP monitoring processes and remain committed to PFM reforms; prudent macroecon omic and monetary policies.
Outcome(s) -Specific Objective 3	SO3: Improved performance of the Supreme Audit Institution.	SO 3.1 PEFA: PI-29 SAI independence and external audit of the Government´s annual financial reports;* SO 3.2 % recommendations of audits emitted by the External Control that are implemented;* (PLACOR 3.1.A) SO 3.3 Nr. and % of the audit judgements that are published on-line (as required by law) (PLACOR 1.1.B – in process of reformulation) * SO 3.4 % of Public spending covered by external audit (PLACOR 1.1.A)* (All above ** EU RF 2.30)	SO 3.1 PEFA SO 3.2 PLACOR Implementation reports (extract from the recommendations system); PARECER of State Accounts SO 3.3 Website SO 3.4 PLACOR Implementation reports.	TA respects the PLACOR Monitoring processes.
Outputs	Output 1.1: Enhanced capacity for Tax Policy formulation. Output 1.2: Improved procedures and capacity for tax administration, in particular on tax audits. Output 1.3: Automated tax systems.	OI 1.1 WB DLI – Number of fiscal implications and impact on the economy analysis produced; among others on tax exemption and profit sharing (to be adjusted to WB DLI in case of changes). OI 1.2 WB DLI - a risk based audit approach for large contributors (especially the extractive industries sector) developed (to be adjusted to WB DLI in case of changes). OI 1.3 All *e-Tributação* modules developed, tested, piloted and interfaced with *Portal do Contribuinte*; (CEDSIF grant and WB project) - (to be adjusted to WB DLI in case of changes).	OI 1.1/OI 1.2 WB project implementation reports, DLI verification audits. OI 1.3 CEDSIF/MEF implementation reports and reports from *e-Tributação and Portal do Contribuinte*.	Authorities maintain the PFM dialogue; the training centres handle the project's deliverables for longer-term capacity programmes; Governments respect the PFSP monitoring processes and

				remain committed to PFM reforms; prudent macroeconomic and monetary policies.
	Output 2.1 Developed and rolled-out IT Systems for Planning and Budgeting Module (MPO), and the State Management Human Resources. Output 2.2 Enhanced information on budget documents (improved formats) and public investment projects. Output 2.3 Control processes for the different phases of expenditure chain re-established. Output 2.4 Improved intergovernmental fiscal transfer modalities.	OI 2.1.1 Status of salaries paid "*via directa*" (through the Central Bank accounts) (PFSP-D4). OI 2.1.2 Status of civil servants life cycle managed through *Sistema Nacional de Gestão dos Recursos Humanos*. OI 2.1.3 Status of certification of the users and their access to e-SISTAFE users that are certified (PFSP-D4). OI 2.1.4. Status of alignment of draft budgetary documents with the programmatic approach (SPO) (PFSP -C1). OI 2.2.1 aligned and improved format of the state budget and plan (PFSP - D4). OI 2.2.2 proportion of public investment projects included in the budget introduced in the e-SNIP module (currently already operational) as per regulations. OI 2.3.1 WB DLI - Status of tools and procedures for a quarterly treasury system (to be adjusted to WB DLI in case of changes). OI 2.3.2 WB DLI – Status of access to and usage by the Ministries the upgraded MPE system for full fiscal year and procurement data disclosed in online Procurement Portal (to be adjusted to WB DLI in case of changes). OI 2.3.3 WB DLI – Number of financial reports including accumulated arrears (to be adjusted to WB DLI in case of changes). OI 2.4.1 WB DLI – Number of budget documents and financial reports with intergovernmental transfer system (formula and amounts) to subnational entities published (to be adjusted to WB DLI in case of changes).	OI 2.1 CEDSIF Implementation reports, State Budgets, State Accounts, PFSP implementation reports. OI 2.2 State Budgets, State Accounts, PFSP implementation reports, MEF reports. OI 2.3 State Budgets, State Accounts, PFSP implementation reports, MEF reports, WB progress reports, DLI verification audits. OI 2.4 State Budgets, State Accounts, PFSP implementation reports, MEF reports, WB progress reports, DLI verification audits.	Authorities maintain the PFM dialogue; the training centres handle the project's deliverables for longer-term capacity programmes; Governments respect the PFSP monitoring processes and remain committed to PFM reforms; prudent macroeconomic and monetary policies.

	Output 3.1 Increased capacity to produce audit reports and publish citizen briefs. Output 3.2 Improved capacity to ensure a risk based audit report on the state accounts (focus on public investment, State owned enterprises, extractive industry and PPPs). Output 3.3 Improved managerial capacity of the TA.	OI 3.1.1 Status of timely and quality publication of the simplified version of the Report and "*Parecer*" of the State Account realised until March n+2 (PLACOR 1.3.A). OI 3.2.1. % (or number) of audits realised–compared to those planned related to extractive industries (PLACOR 1.2.A). OI 3.2.2.% (or number) of audits realised –compared to those planned related to PPPs (PLACOR 1.2.A). OI 3.2.3 Improved chapter on extractive Industries included in the report and PARECER of the State Accounts (PLACOR 1.2.A). OI 3.2.4 % (or number) of auditors trained and with access to international testing for internationally certified auditors. OI 3.3.1 The status of implementation of the "Plano Director de Sistemas de Informação" (PLACOR 4.2.A). OI 3.3.2 Status of the different procedure manuals (PLACOR 3.1.A). OI 3.3.3 % of recommendations of the External evaluation on the effectiveness of the internal control (COSO methodology) implemented.	OI 3.11: Trib. Admin website. OI 3.2.1-3.2.4 Trib Amdin website; PLACOR Implementation reports; PARECER of State Accounts TA´s Website. OI 3.3.1-3.3.3 Trib Amdin website; PLACOR Implementation reports; PARECER of State Accounts TA´s Website.	State –Budget allocation to the Administrative court maintained or increased.