September 2012

Preparing a Government Debt Management Reform Plan

THE WORLD BANK

Economic Policy and Debt Department (PRMED)
Poverty Reduction and Economic Management Network (PREM)
Financial Advisory and Banking Department, Government Debt and Risk Management (FABDM)
Treasury (TRE)

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Introduction

The World Bank supports the strengthening of government debt management in developing countries largely through a three-step programmatic approach and on a demand-driven basis. This work program includes assistance through: 1) assessing and benchmarking debt management capacity via application of the Debt Management Performance Assessment (DeMPA) tool; 2) assisting the development of government reform plans to improve management of public debt (Reform Plans); and 3) supporting the implementation of government reform efforts through advice and targeted technical assistance, including help in developing and carrying out a medium term debt management strategy (MTDS).

This note relates to the second step above, and aims to guide World Bank teams assisting governments develop Reform Plans. While Reform Plans are country-specific and vary considerably depending on the prevailing circumstances of the country, these guidelines aim to foster a consistent approach and set of process steps for working with client countries. This note is based on lessons learned from a 12-country pilot program between 2002 and 2004, subsequent work with around a further 30 countries led by the Treasury,[1] and another 20 developing countries on designing their Reform Plans under the umbrella of the Debt Management Facility (DMF) from 2008 and ongoing work led by the PRMED.[2]

2. What Is A Debt Management Reform Plan?

When initiating the preparation of a Reform Plan in the area of government debt management, it is helpful to think about the desired long term reform goal. Based on practical experience, the World Bank has concluded that the ultimate expected result of government debt management reforms can be described as follows:

The country has in place sustainable governance arrangements, internal processes, resources, and staff capacity to develop and efficiently execute a government debt management strategy based on a sound analysis of cost and risk, and taking account of macroeconomic and market constraints.[3]

With the above goal of debt management reform in mind, a Reform Plan should include the following features:

- A **specific timeframe** for achieving steps toward effective debt management. While improvement of debt management capacity will be a gradual process the period of the plan should ideally not exceed the medium term of 3-5 years, in order to maintain momentum and focus. Reform actions should be recommended sequentially starting

[1] The lessons learned from this pilot program are discussed in more detail in the World Bank (2007) *Managing Public Debt – From Diagnostics to Reform Implementation.*
[2] For a detailed list, see http://debtext.worldbank.org/ReformMission.asp
[3] See World Bank (2007) *Managing Public Debt – From Diagnostics to Reform Implementation*, p. 2 and 3.

realistically from 3 months onwards to the date of the end-point chosen in consultation with the authorities.

- The **identification of the key constraints** in government debt management institutions, functions and operations, informed by a recent and comprehensive assessment. The scope of the Reform Plan can cover all government debt management activities, loan guarantees, lending, and cash balance management, or can be limited to focus on country specific priorities as discussed and agreed to with the authorities. Nevertheless, if the scope is narrow the plan should be consistent with the broader institutional setting, in order to avoid a piecemeal approach. (For example, in most cases it is not enough to only have a sophisticated debt management system installed, or only train the staff in debt management strategy development. Instead, all the pieces must fit together to achieve the result as defined above.)

- A **prioritized and sequenced action plan** to address areas requiring improvement. The plan should be project-related and contain details on the expected outputs and outcomes, actions, sequencing and milestones (see section 6 for definitions). It also provides an estimate of the resources, budget and time required to implement the plan. Activities and outputs in the first year may be specified in more detail than those in later years, which will depend on earlier achievements and evolving circumstances.

- A **country-specific approach** to reflect the willingness of the authorities to undertake institutional and structural reforms, and realistically set the pace at which they can be implemented. Government officials will be accountable for implementing the plan, so it is imperative that it is practical and tailored to their circumstances. It is thus essential that they participate fully and actively in the drafting of the plan.

These features are discussed in more detail in the subsequent sections.

3. An Approach to Reform Plan Design Assistance

To ensure the recommended features of a Reform Plan discussed in the previous section are considered, a sequenced approach to helping design the reform Plan is suggested. The starting point in developing a government Reform Plan is an analysis and understanding of the current state of debt management operations through a needs assessment, e.g. by application of the DeMPA tool.

The next stage involves working with the authorities to identify the medium term priorities that are most important for achieving the long term goal of effective debt management.[4] This should include an evaluation of any organizational shortcomings, consideration of any recently completed reform efforts, with attention to lessons learned, a candid examination of the appropriate scope for reforms taking into account existing capacity, the willingness to undertake institutional reforms, available funding, etc., and discussion of the possible sequencing of reforms.

[4] Reference to the overall goal in the previous section can be helpful for debt managers to ground priorities to the long term goal.

With a clear understanding of the priorities for reform, the bulk of the World Bank support can be spent helping the authorities to concretely put together a plan for implementing actions. Along with the identification of specific actions in each pillar (or project component) to ensure that the outputs are achieved, it is important to consider the sequencing of the suggested actions for each pillar and their consistency across the pillars to avoid gaps and overlaps.

Depending on the implementation of activities by the authorities, a follow-up mission to refine the Reform Plan can be considered on a case-by-case basis. Follow-up missions may be needed to further calibrate action steps and sequencing.

4. Design Factors for Success in Implementation

Political commitment. The often complex policy and institutional reforms associated with improving performance in public debt management can only be adopted and implemented if there is sufficient political support within the relevant parts of the government. To ensure this support, it is essential that the Reform Plan is developed in close coordination with country authorities, preferably with country officials wholly responsible for drafting the plan, and World Bank staff acting as a sounding board, providing examples of country experience with Reform Plans and lessons learned that make a good fit with the country context.

Political commitment is critical, especially for institutional reform. Regardless of the institutional arrangements for government debt management, building capacity is a long-term endeavor, and requires leadership and management skills for successful reform. Existing organizational arrangements, with government debt management functions perhaps spread among departments or located in the central bank, may have been in place for decades. Strong leadership is needed to overcome possible resistance to proposals to reformulate debt management responsibilities.

Realism in resourcing and timeframes. The main stages of the implementation process must be clearly understood, and realistic timeframes and budgets have to be established. A common mistake is to underestimate the magnitude of the resources needed for successful capacity building, the time required, and the budgetary costs involved, especially in acquiring or developing skilled staff and installing satisfactory management information systems. Programs aimed at developing a sound government debt management capability can take many years. Programs substantially upgrading the quality of debt management in many OECD countries during the late 1980s and early 1990s often took five years or longer, given the challenges of recruiting and training staff, developing a risk management strategy, and supporting it with appropriate management information systems and documentation on policies and procedures. Comprehensive reform and staff development can even take longer if the initial conditions are much less supportive than those prevailing in many OECD countries at the start of their programs (Wheeler, G. 2004).[5]

[5] See Wheeler, Graeme (2004) *Sound Practice in Government Debt Management* p. 162.

However carefully the Reform Plan has been designed, expect delays in implementation and that circumstances will change. It is common to have recommended actions less specified after the first year, and to revise the plan annually, or even earlier if needed.

Country specificity and appropriateness. Reform Plans that reflected country specific priorities, the prevailing political climate, technical difficulty, and capacity constraints have seen greater incremental progress than those that laid out the first best solutions which might have been impractical to implement. These reform experiences are best characterized as "good fit" rather than "best practice." In addition, plans that incorporate medium-term capacity building while taking into account immediate constraints have helped keep in sight the bigger picture. This has helped governments identify opportunities to implement more ambitious reforms.[6]

Reform champion. In line with the above, it is essential to have a committed project manager in the country, a local champion who can drive the process forward. In the area of debt management, an ideal champion is the head (or the deputy head) of the principal debt management unit and if there are several debt entities then the head of the middle-office (if existing). For a successful outcome it is important that the project and the local champion receive political support. In a debt management project this support must come from the minister or the deputy minister of finance.

Integration with broader reform efforts. Debt management reforms can be more effectively sustained by integrating it into broader programs, such as public sector or public financial management reforms. Such integration helps ensure project sustainability and continuity through financing, support by experts, and project supervision.[7] It is an essential part of the preparation for a Reform Plan mission to explore ongoing and planned capacity building more broadly in the ministry of finance and related institutions.

Proper sequencing. Sequencing of the project components is a significant challenge in preparing a Reform Plan. Where to start, and what follows thereafter? For each country sequencing of the project components (and the recommended actions) will differ depending on the initial state of the government's performance in managing its debt, the type of policy and institutional factors, and its expected medium-term requirements (e.g. are they expected to have access to market finance over the period? Is the debt portfolio 10 loans or 1,000 loans?). Some lessons learnt, however, can be drawn from experience. The 12-country pilot program concluded the following:

"The basic building blocks that must necessarily come first are building capacity in the back office and establishing reliable debt recording systems. These are required to ensure timely servicing of the debt, without having to rely on creditors' notifications, and to produce accurate and frequent reporting. Beyond these steps, sequencing has been varied."[8]

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[6] See *Managing Public Debt – From Diagnostics to Reform Implementation*, p. 10.
[7] Ibid, p. 13
[8] See *Managing Public Debt – From Diagnostics to Reform Implementation*, p. 11.

5. Process

Staffing of Reform Plan missions. Staffing of a Reform Plan mission should be undertaken after initial consideration of the expected priority areas to be discussed with the authorities, which will determine the needed expertise. The Reform Plan team should not be larger than 3-4 staff. The team should be composed of at least two people with practical experience in managing public debt. The selection should be made depending on the comparative skills of each member while mapping those with the requirements in the country. Continuity of work in the country should be a criterion for selection. In the case of a DMF financed mission, a representative from one or more of the implementing partners will participate. [9]

Follow-up mission. A good Reform Plan takes time to prepare, and may require a follow-up mission to calibrate the actions recommended during the initial mission. This might be particularly important to ensure country ownership of the Reform Plan. A useful indicator will also be a follow-up DeMPA that indicates elements of progress and improvements.

Bearing in mind the importance of the Reform Plan, the draft plan should be subject to a formal peer review process before it is finalized. The steps to be followed in preparing the Reform Plan are detailed in Annex 3.

6. Key steps on a Reform Plan mission

The structure of the Reform Plan for government debt management should include two main components: a report that outlines and discusses the main issues and elements of the Reform Plan (see Annex 1 for a sample table of contents); and a log-frame (see Annex 2) that provide details on the individual steps.

Key Steps:
As a first step, it is essential to analyze the likely causes for the weaknesses (the diagnosis). This is important in providing the rationale for the components of the Reform Plan.

To illustrate, the assessment has flagged flawed debt data as one of the **issues**, with debt data neither complete nor accurate. The diagnosis showed that the debt management unit responsible for recording debt data (the back-office unit) did not receive the required information in a timely manner from other government units. Also it was discovered that mistakes were made when recording the debt data due to lack of training in basic finance, and weak procedures that were lacking an independent check of all debt data entries.

Second, the **issues** or **project components** to be included in the Reform Plan need to be selected in coordination with the country authorities, based on an understanding of the causes of the problems Not all weak areas (i.e. where a "D" was scored in a DeMPA) need to be addressed or considered priority in the Reform Plan. For example, documented policies and procedures for the approval and lending of borrowed funds might be considered a low priority in a country that has

[9] The DMF-implementing partners are UNCTAD, Commonwealth Secretariat, the Macroeconomic and Financial Management Institute (MEFMI), West Africa Institute for Financial Economic Management (WAIFEM), the Centre for Economic and Monetary Studies in Latin America (CEMLA), and Debt Relief International.

not used on-lending to support a certain project during the last three years ago, and has no immediate plans to change that policy.

Third, for each pillar (project component), there should be a brief outline of the sound practice in that area. Sound practices enunciated in the World Bank – IMF Guidelines for Public Debt Management (2003) and the World Bank's Debt Management Performance Assessment Tool and Guide (2009) provide useful pointers for suggesting reforms.

Fourth, the expected **outcome** of every project component must be specified. Following the example above, the desired outcome is that the government in a sustainable manner will have complete, timely and accurate debt data in its debt recording system. Thus, the outcome of a project component reflects how the government would like to see its institutions functioning at the end of the period.

Fifth, the required **outputs** from the reform process to achieve the desired outcome should be specified. Using the example above, the expected outputs are: <u>1</u> an information flow chart and a procedures manual for debt data recording to be prepared: and <u>2</u> back-office staff is trained in concepts of finance and understand basic financial terms in loan agreements. It is important that the achievement of each **output** can be verified.

Sixth, the recommended **actions,** i.e. the specific activities or actions for capacity building to achieve the desired output, need to be determined. Following the example above on the flawed debt data, it was recommended that the following actions should be undertaken:

- <u>Action 1</u> → Preparation of information flow charts and a procedures manual for debt data recording.
- <u>Action 2</u> → Train the back-office staff in basic concepts of finance, including on the financial terms in international loan agreements.

Seventh, the timing (sequencing) of the recommended **actions** need to be specified.

Last but not least, estimated **inputs** needed to implement each **action** should be included, e.g. assistance by technical assistance provider, an international consultant, estimated costs, and sources of financing, if available. If it relates to internal ministerial orders then the same should be mentioned as these do not have explicit costs.

The Reform Plan should in a clear and succinct manner provide arguments for all recommendations following the structure presented above, and include a log-frame that summarizes the issues, recommended actions, timing of the actions, expected outputs of the actions, estimated inputs, and expected outcome for each project component. A template for the same is presented in <u>Annex 2</u>.

In a well-sequenced project with relatively few project components, the outcomes can serve as "milestones", i.e. annual progress markers of implementation of the project components scheduled for that year.

Throughout the project, it is important to evaluate whether the desired results are achieved. Did the actions lead to the expected outcomes, and if not, what were the reasons for this failure? This evaluation can take different forms. When projects are financed by development funds, such as Institutional Development Fund (IDF), it is common to undertake such an evaluation with a project audit. Another evaluation tool is the DeMPA that can be undertaken after initiation of the reforms to find out whether the scoring of the debt management dimensions that initially were considered as weak improved since the initial assessment.[10]

Disclosure Policy

The Debt Management Reform Plan reports have a default classification as restricted documents, designated for "Official Use Only. Under the World Bank's Policy (AMS 6.21, paragraph 5.3):

"Information of this type, if disclosed, may in the judgment of the relevant WBG entity cause harm to well defined interests of the WBG entities or stakeholders. Sharing "Official Use Only" information with the general public or the press is not permitted. This is the default classification level for restricted information.

Access to information classified as Official Use Only must be restricted to WBG Staff of the relevant WBG entity. Official Use Only information may be disclosed to External Parties if the disclosure, on a prudent basis, is in the interest of the WBG entity and the receiving External Party is notified that the information so disclosed may not be further disclosed without the prior consent of the disclosing WBG entity, or is otherwise under an obligation of confidentiality".

Though these reports have a default classification as 'restricted' documents, client governments are encouraged to disclose their Debt Management Reform Plan reports. This is done **only** on receipt of written authorization from the government counterparts, whereby the document is designated as public.

[10] DeMPA are usually recommended after a period of 3 years.

ANNEX 1

Sample Table of Contents

ANNEX 2

Sample Log-Frame Format

Issues/ Project Components	Actions	Timing (end-dates)	Expected Output for each Action	Inputs and lead entity	Expected Outcome for each Project Component

ANNEX 3

Guidance on Process (for World Bank Staff)

Tasks related to processing support for government Reform Plans:

1. A request for Reform Plan assistance is received.

2. The team lead is identified by the Economic Policy and Debt Department (PRMED) Reform Plan Coordinator, and he/she initiates identification of key issues and collection of basic information with relevant staff in WB, IMF etc.

3. The main counterpart in the relevant Ministry of Finance is identified and contact is established (video/audio conference meeting) to determine priority areas of the assistance and propose mission dates. The team lead commits World Bank assistance and confirms mission dates in a formal response letter to the authorities.

4. The team lead identifies the mission team and a concept note is prepared. A concept review meeting is held at least two weeks before the first Reform Plan mission. The concept note should include the following.
    a. Background and context, including an evaluation of the government's appetite for reforms in debt management.
    b. Description of planned activities, including the scope of the work and expected outcomes.
    c. Preliminary schedule and budget.
    d. Team.

5. Concept review meeting
    a. Chair: Cluster lead/Sector Manager of PRMED. Invitations to PRMED and Treasury staff, including staff preparing the DeMPA and the Country Team.
    b. Peer reviewers: Normally there will be three peer reviewers, including the country economist plus two debt management experts. The latter can be external and/or PRMED/Treasury staff working on debt management topics. Invitations and the concept note should be distributed at least one week prior to the meeting.
    c. The team lead prepares minutes to be approved by the Chair.

6. Finalize the meeting schedule. Meetings should include the relevant departments in the Ministry of Finance, Central Bank, market participants etc. Discuss this with the DeMPA team and the Country Economist. Make sure to arrange a meeting with the development partners and other potential donors that could provide funding for implementation of the Reform Plan (it is important that the debt management team participates and, ideally, are making a presentation).

7. Issue Statement of Mission Objectives to be approved by the Sector Manager, PRMED/Treasury.

8. Mission

a. Kick-off meeting with Minister of Finance or similar.
    i. Explain the purpose of the mission, its deliverables, and what will be expected from the debt management staff during and after the mission.
    ii. Discuss potential project components of the Reform Plan and how support can be provided on funding/implementation efforts.
    iii. Discuss the need for a champion to drive reforms.
    iv. Suggest that the champion be engaged with the mission and discuss the log-frame.

b. During the first day: Meet with the debt management team, and explain to them in detail the work of the mission etc. When time allows, consider arranging short workshops on areas of importance in the context of the Reform Plan to keep the debt management team in the loop and as a vehicle to get information/discuss these topics.

c. Draft the main project components of the Reform Plan jointly with the debt management team, and prepare a presentation outlining the Reform Plan, to be held at the formal wrap-up meeting (this presentation can be delivered by the debt management team).

d. Schedule a pre-wrap-up meeting with the decision-maker (normally the Minister of Finance or the Deputy Minister/Permanent Secretary) and the Head of the Debt Management Unit to present the draft Reform Plan. The purpose of this meeting is to consider the authorities views on the feasibility for the actions being proposed, in particular on institutional arrangements and HR issues. If new information is received during the meeting this needs to be considered before the formal wrap-up meeting and while drafting the Reform Plan.

e. Schedule the formal wrap-up meeting. The wrap-up presentation should be left with the authorities.

9. After returning to Washington, the team lead will submit a Back-to- Office- Report.

10. Finalize the draft Reform Plan to be peer reviewed by at least two debt management experts and the country team.
    a. The Reform Plan should be sent for peer review no later than 20 business days on returning from mission.
    b. The peer reviewers should have 5 business days to provide comments.
    c. No later than 10 business days after receiving the peer review comments, a draft Reform Plan should be sent to the authorities for comments. The authorities should be given a (proposed) 15 day deadline for comments.
    d. Upon receiving comments from the authorities, the team should finalize the report within 7 business days.

11. The team lead, through the Country Economist, should check regularly with the authorities regarding progress with implementing the Reform Plan.