Islamic Republic of Afghanistan: Letter of Intent, Memorandum of Economic and Financial Policies, and Amendment to the Technical Memorandum of Understanding

May 18, 2005

The following item is a Letter of Intent and a Memorandum of Economic Policies of the government of Islamic Republic of Afghanistan. It is being made available on the IMF website by agreement with the member as a service to users of the IMF website. This memorandum describes the policies that Islamic Republic of Afghanistan is implementing in the framework of a staff-monitored program. A member's staff-monitored program is an informal and flexible instrument for dialogue between the IMF staff and a member on its economic policies. A staff monitored program is not supported by the use of the Fund's financial resources; nor is it subject to the endorsement of the Executive Board of the IMF.
Dear Mr. de Rato,

1. We have carried out discussions with Fund staff on the fourth review under the staff-monitored program (SMP) agreed to in March 2004 and updated on September 6, 2004, December 29, 2004, and February 3, 2005, respectively. We have reached understandings on the policies for 2005/06 and on the priorities for the medium term. The focus of our strategy continues to be on achieving high rates of economic growth in a non-inflationary environment and reducing poverty through sustainable fiscal and monetary policies and structural reforms aimed at increasing revenue mobilization, rationalizing public spending, facilitating the development of the private sector, and at improving governance.

2. The attached update to the Memorandum of Economic and Financial Policies (MEFP) reviews macroeconomic developments and the implementation of structural reform measures during 2004/05, and describes the objectives and policies the government intends to pursue during the first half of 2005/06.

3. We are pleased to inform you that our program remains on track. We have met all the end-March 2005 indicative quantitative indicators and structural benchmarks, with the exception of the benchmark related to the completion of a survey of external debt. This benchmark was not met on account of the limited response from external creditors, which prevented a full reconciliation of this debt. Recognizing the importance of this survey in the design of an external debt management policy, we have reached understandings with Fund staff on a new end-September 2005 structural benchmark related to the completion of this survey. The Government of Afghanistan would appreciate assistance from the IMF in contacting our creditors and ensuring observance of this structural benchmark.

4. The government believes that the policies and measures set forth in the attached MEFP are adequate to achieve the objectives of the program. However, we also stand ready to take any additional steps as may be needed or appropriate to meet both the letter and the spirit of the reforms outlined in the program. The Government of Afghanistan will continue to work closely with IMF staff in this regard, and will provide any information required to assess the implementation of the SMP. The Government of Afghanistan authorizes the publication and distribution of this letter, the attached MEFP and the technical memorandum of understanding, and all reports prepared by IMF staff directly related to the SMP.
Sincerely yours,

/s/                      /s/
Anwar Ul-Haq Ahady      Noorullah Delawari
Minister of Finance     Governor
Ministry of Finance     Da Afghanistan Bank

Attachments:
Update to the Memorandum of Economic and Financial Policies
I. INTRODUCTION

1. This update to the Memorandum of Economic and Financial Policies (MEFP) reviews performance during the fourth quarter (January–March 2005) of the Staff-Monitored Program (SMP) and describes policies and targets for the first half of 2005/06. The program will continue to be guided by the macroeconomic and structural reform policies described in the MEFP of March 24, 2004, and in the updates of September 6, 2004, December 29, 2004, and February 3, 2005. The next review under the SMP, scheduled for August 2005, will assess performance during the first quarter of 2005/06. Key issues will include: assessing progress toward implementing tax and customs reforms; fiscal and external sustainability; and modernization of the banking system. Table 1 contains the updated quantitative targets while Table 2 sets out the structural benchmarks for end-June 2005 and end-September 2005. This update to the MEFP includes several additional reform measures.

2. Despite unfavorable security conditions, we continue, in the context of SMP, to maintain macroeconomic stability, build capacity, and improve our statistical base. We observed all end-March 2005 indicative quantitative targets and structural benchmarks, with the exception of the benchmark related to the completion of the survey of external debt, due to some creditors not responding to our requests for reconciliation of liabilities. We will take advantage of the extension of the SMP through end-September 2005 to pursue our capacity-building efforts, broaden ownership of the reform strategy, and improve policy formulation and implementation.

II. DEVELOPMENTS UNDER THE SMP

3. Real GDP growth for 2004/5 is estimated to have been in line with the SMP projection (7.5 percent), with a fall in agricultural output being more than offset by buoyant activity in telecommunications and construction. Consumer prices in Kabul increased by 3.2 percent during the fourth quarter, reflecting a further increase in food prices (5.8 percent) stemming from the poor agricultural crop. Year-on-year inflation reached 16.3 percent at end-2004/05, compared with 10.2 percent a year earlier.¹ The increase in

¹ Inflation was lower in the provinces than in Kabul: the “national” consumer price index, which covers five major cities in addition to Kabul, increased by 2.7 percent during the fourth quarter and by 10.9 year-on-year at end-2004/05.
inflation was largely attributable to the acceleration of rents, education fees, and petroleum product prices. Excluding these items, which account for less than 10 percent of the consumer basket, year-on-year inflation declined slightly in 2004/05, to 10.3 percent, from 10.8 percent at end-2003/04.

4. **Provisional data indicate that domestic revenue for 2004/05 reached Af 12,800 million, slightly above the SMP indicative target (Af 12,784 million), but below the budget forecast of Af 15,380 million (Table 3).** The SMP target was met despite the fact that administrative difficulties resulted in the delayed (May 2005) collection of Af 797 million in overflight charges, although they accrued in 2004/05. Customs duties exceeded their target by approximately 20 percent and constituted about 50 percent of revenue, compensating for a shortfall in tax and nontax revenues.

5. **The shortfall in revenue relative to the budget was more than offset by lower operating expenditures.** Although operating budget expenditure increased substantially during the fourth quarter, the annual amount of Af 26.7 billion fell short of the midyear review projection of Af 29.1 billion for 2004/05 (the original budget was Af 30.3 billion). This resulted mainly from continued delays in recruiting teachers and in implementing the main civil service restructuring program. Enhanced expenditure controls and compliance have improved fiduciary standards significantly over the year and facilitated more timely grant disbursements from the multidonor trust funds. Overall, the operating budget, including grants, recorded a modest surplus of Af 1.1 billion for the year.

6. **The rate of development spending has improved but remains well below budget expectations.** In 2004/05, core budget development spending amounted to Af 12.9 billion and external budget spending, which is implemented directly by donors, was reported at $2 billion, compared with budget estimates of Af 38.4 billion and $3.5 billion, respectively. Development spending continues to be hampered by: (i) the lack of capacity in line ministries and implementing agencies to develop and implement projects; (ii) the lead time required to design and initiate projects; and (iii) security concerns.

7. **Amendments to the income tax law and the new customs code were published in the Official Gazette in March 2005, introducing a more efficient regime for providing tax incentives to private investors.** In support of our policy of fiscal transparency, we also published an estimate of revenue forgone as a result of the previous regime of tax exemptions and concessions—estimated conservatively at $14.6 million for 2005/06, equivalent to 4.4 percent of budgeted revenue, and over $30.2 million since 2003/04. The report also highlighted the extent to which the previous tax regime favored particular sectors, such as construction, which should not have been the primary beneficiaries of such incentives.

8. **Currency in circulation increased by 38 percent in 2004/05 reaching Af 39.6 billion at end-year, slightly below the SMP indicative target (Af 39.8 billion).** To meet this target, Da Afghanistan Bank (DAB) stepped up its foreign currency auctions to $105 million (Af 5.1 billion) during the fourth quarter, so as to offset partly the monetary expansion resulting from the increase in government spending. Since increased spending was
partly financed through a drawdown of government’s deposits with DAB, foreign exchange reserves declined slightly during the fourth quarter to $1.3 billion (equivalent to 3.9 months of projected 2005/06 imports). The interest rate on the overnight capital note remained low, at 1–2 percent, while the rate on the one-month note, whose auctions remain undersubscribed, increased modestly to 5 percent at end-March. The nominal exchange rate appreciated by 3.4 percent in 2004/05 to Af 48.7 per U.S. dollar at end-year, although the rate was stable during the final quarter.

9. **Further progress was made in restructuring DAB’s balance sheet and in strengthening the banking sector regulatory framework.** The cessation of DAB’s headquarters-based commercial activities was completed by end-March: about 30 percent of the relevant current accounts and 20 percent of the savings accounts were closed, while the remainder, whose owner was not identified or that were not claimed, were transferred to a **control account.**2 The ownership of the silver and gold held in the palace vaults was transferred to DAB and an independent local expert has started working on their valuation. DAB’s commercial holdings, which comprised state-owned banks and enterprises, were transferred to the government. The audit of DAB’s end-2003/04 financial statements was finalized. The commercial banking law was published in the Official Gazette and a set of new banking regulations, related to corporate governance, foreign exchange positions, and enforcement activities, was adopted by DAB’s Supreme Council. And DAB has started to enforce reserve requirements, currently set at 8 percent.

10. **The current account deficit, excluding grants, reached 43.7 percent of GDP in 2004/05, down from 50.9 percent in 2003/04.** While foreign direct investment (FDI) and concessional borrowing increased, this deficit continued to be mainly financed by grants (Table 5). Including grants, the current account was broadly balanced in 2004/05, down from a 3.1 percent of GDP surplus in 2003/04. This mostly reflected a rise in imports not associated with reexports. External borrowing remained limited and on highly concessional terms. Net errors and omissions remained high.

11. **We recognize that there are significant challenges ahead and that security conditions, weak capacity, and bureaucratic impediments pose risks to program implementation.** Nonetheless, we will continue to implement prudent economic policies in 2005/06 with the aim of maintaining macroeconomic stability and sustaining economic growth while fighting pervasive poverty.

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2 As agreed under the SMP, foreign delegations, international agencies, government agencies, and public enterprises were permitted to keep accounts with DAB. A control account does not allow for any transaction, with the exception of a final cash withdrawal.
12. **Economic policies for 2005/06** are consistent with our medium-term objectives of spurring private sector-led growth while enhancing external and fiscal sustainability. The success of this strategy is predicated on a substantial increase in revenue, notably through better tax and customs administration, as well as improved efficiency of expenditure. Expenditures will be consistent with the priorities identified in the National Development Strategy, which we have begun to define, and should help to move towards the Millennium Development Goals.

13. **In 2005/06, real GDP growth is expected to increase to 13.6 percent, reflecting largely a rebound in agricultural output due to better precipitation.** While slowing down, activity in construction, transport, and telecommunications is expected to continue to grow steadily. Reflecting some tightening of the monetary stance, as well as an expected slowdown in food price and rent increases, inflation is projected to decline to 10 percent year-on-year by end-2005/06.

14. **There has been a reduction in poppy cultivation due to the anti-narcotics campaign and to a decline in farm gate prices triggered by the bumper harvest in 2004.** It is uncertain, however, whether this will translate into a significant reduction in opium production as yields are expected to rise due to better weather conditions. We are vigorously pursuing the anti-narcotics strategy developed with our external partners, which is built upon eradication, interdiction, alternative livelihoods, and education.

**B. Fiscal Policy**

15. **The operating budget for 2005/06 is prudent and should provide a solid base for developing a medium-term budgetary framework.** Despite an uncertain level of external funding, the operating budget was approved before the start of the fiscal year (March 21), which enabled us to avoid a repeat of the payment delays that occurred at the beginning of previous fiscal years. Although some uncertainty about the level of donor financing remains, we have maintained the no-overdraft policy and are funding the operating budget only from revenue and external grants.\(^3\) Despite demands for additional spending, recurrent expenditures are budgeted to grow broadly in line with nominal GDP.\(^4\)

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\(^3\) Grants from the Afghanistan Reconstruction Trust Fund (ARTF) and the Law and Order Trust Fund for Afghanistan (LOTFA) are expected to increase to cover over half of operating budget expenditures in 2005/06. Indications of donor commitments suggest that the ARTF and LOTFA will have sufficient funds to cover operating budget requirements.

\(^4\) The operating budget provides for a 15 percent increase in recurrent spending over the mid-year review projections for 2004/05, while the lower-than-expected outturn for 2004/05 implies an increase of around 23 percent.
16. **In anticipation of further donor commitments, an ‘interim’ development budget was approved at the start of the fiscal year.** This interim budget presented the main priorities of the government for the year, but was not fully funded as some donors had not confirmed their commitments. We will continue to request that donors channel funds through the budget, or alternatively via the multidonor trust funds. Any additional donor funding committed for 2005/06 will be allocated to development spending, unless it finances recurrent expenditures previously funded directly by donors. In the latter case, it will be absorbed within the operating budget. Any such changes would be presented in a supplementary budget. Core development spending financed through the treasury is currently budgeted to increase from 4.5 percent of GDP in 2004/05 to 13.2 percent of GDP in 2005/06. This increase reflects the growing capacity of line ministries to implement projects, the readiness of donors to implement projects through the budget, and the completion of the design stage for some large projects.

17. **Improving the consistency of the budget presentation and developing a realistic medium-term fiscal framework will help to manage expectations.** The current presentation of the budget combines cash and commitment concepts, and therefore significantly overstates the actual amount of spending expected within the year. To better manage expectations among the population regarding development spending, as well as to reflect the possibility of a limited absorptive capacity over the medium term, we will continue to improve the transparency and realism of the development budget formulation and reporting. We will adopt a more standard and consistent cash-based presentation of the budget within a medium-term framework and provide regular quarterly reports on the core budget.

18. **Developing an affordable and efficient public administration is an essential element to attain a sustainable fiscal position.** Salary costs represent about 75 percent of operating expenditures and are expected to increase over the medium term due to ongoing public administration reforms and the need to absorb additional security spending, notably the Afghan National Army. While we appreciate the need to contain pressures for generalized or sector specific pay increases, quantitative limits on the wage bill might be best introduced in the context of a comprehensive medium-term public administration reform. Until such a program is in place, hopefully for the next fiscal year, we will continue to contain the wage bill consistent with the implementation of the Priority Restructuring and Reform (PRR) program. We will also continue to limit borrowing to highly concessional external loans.

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5 The interim budget was approved prior to the Afghanistan Development Forum (ADF) donor meeting in early April 2005.
19. **Domestic revenue for 2005/06 should be higher than budgeted.** The SMP target for 2004/05 was achieved despite the delay in receipt of the overflight charges, which suggests that domestic revenue should be higher than budgeted in 2005/06.\(^6\) The SMP revenue target was revised accordingly.\(^7\) Prior to the midyear review, any additional domestic revenue above the budget forecast will be used to either: (i) offset shortfalls in budgeted grant resources for the operating or development budgets; or (ii) build the government’s prudential cash reserves. The midyear review will give us the opportunity to assess, in collaboration with the donor community and in light of the National Development Strategy (NDS), the scope for budgetary adjustments.

20. **We are committed to accelerating the customs and tax administration reform programs.** Our strategy will continue to focus on the medium-term reforms for improving compliance, on taxpayer education, and on identifying areas where the potential revenue yield appears highest, rather than on quick actions that may not necessarily lead to sustainable improvements. At the same time, we will rationalize the ‘nuisance’ taxes (notably the fixed taxes) and remove illicit charges. Priority will also be given to ensure that the large taxpayer office (LTO) identifies and starts to work with its main clients, rather than diverting scarce human resources to collect revenues from smaller taxpayers. We will accelerate the restructuring of the revenue headquarters and the new provincial revenue offices. New tax revenue enforcement powers to support the revenue administration should be in place by end-September 2005. We are also developing new regulations to support the new customs code and we will continue to improve customs infrastructure, to roll out a computerized management information system, and to introduce the new customs police service. We have requested IMF technical assistance to help review and prioritize our customs and tax reform programs.

21. **We will continue to address the structural impediments to better fiscal management.** We are committed to promulgating the new public financial management law by end-June 2005 and expect to develop the accompanying financial regulations shortly thereafter. The new system that links the Ministry of Finance with DAB enables us to more promptly reconcile the main government bank accounts with the expenditure data and we are confident of meeting this end-September 2005 structural benchmark. Finally, we have approved a timetable for the submission of the audited financial statements to parliament before end-September 2005.

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\(^6\) The updated forecast for 2005/06 accounts for the payment of two overflight charges (one paid in May 2005 but accrued in 2004/05 and one accrued and paid before the end of 2005/06), and is based on the higher-than-expected 2004/05 outturn of other domestic revenue.

\(^7\) The budget forecast will not be amended at this time.
C. Monetary and Exchange Rate Policies

22. Monetary policy will continue to be guided by the monetary program developed with Fund staff at the time of the third review. While the upward revision of growth projections for 2005/06 might have justified an upward revision of the growth of currency in circulation, we consider that, in view of the increase in prices in the fourth quarter of last year, a conservative approach is warranted at this stage. So as to allow for a possible tightening of the monetary stance at a point in the budget cycle where the government is drawing down its deposits with DAB, the end-June indicative target for gross international reserves was revised downward. The revised target is consistent with a coverage of four months of prospective imports at end-2005/06. The exchange rate will remain flexible: while DAB may intervene to smooth short-term exchange rate fluctuations, it will not resist persistent pressures on the exchange rate, especially when such resistance is not consistent with the objective of reducing inflation. Given the uncertainty surrounding both money demand and the efficiency of monetary policy, the monetary program will remain flexible, allowing for a revision of the monetary stance in consultation with the Fund when warranted by exchange rate and price developments.

23. We will continue to restructure DAB’s balance sheet and improve monetary reporting. The transfer of DAB’s commercial activities remains a priority. By end-September, we will finalize the transfer of these activities in Kabul’s 14 city branches and in the 10 provincial branches located where at least one commercial bank operates. By end-June, we will publish DAB’s audited 2003/04 financial statements. In light of the preliminary estimate of the gold and silver held in the palace vault, we will also determine whether DAB is adequately capitalized. While we anticipate DAB to be adequately capitalized, we stand ready to take action regarding its recapitalization. In collaboration with the commercial banks, we will work toward improving the timeliness and reliability of monetary reporting.

24. We will continue to modernize the banking sector. Based on the findings of the IMF technical assistance mission on monetary policy, we will explore broadening DAB’s monetary instruments, so as to strengthen its control over liquidity. In particular, we intend to develop an interbank market and to modernize our foreign exchange and capital note auctions. We also intend to tackle some of the administrative impediments to the development of the banking sector, including the absence of laws supporting financial market development (e.g., bankruptcy and corporate laws) and high fees (e.g., property registration). We will play a more active role in restructuring the state-owned banks with technical assistance from our partners. By end-June 2005, we will take a decision regarding the specific resolution process for each of the former state-owned banks that were not relicensed and begin implementation of that decision. Finally, by end-September 2005, in accordance with our shareholder responsibilities, we will prepare a long-term strategic plan for the restructuring of the three state-owned banks.
D. External Policy and Debt Management

25. **The outlook for the external accounts remains favorable.** Under relatively conservative assumptions on donor inflows, private investment flows, and ongoing structural changes in the economy, we expect the current account balance to deteriorate slightly in 2005/06, to a deficit of 0.5 percent of GDP. Over the medium term, we expect imports to remain high and to continue to be financed through donor inflows. Higher levels of domestic and foreign investment should help to expand our export base.

26. **Building upon IMF technical assistance, we have improved the framework for compiling the balance of payments in line with international standards.** Trade data have been reconciled with the national accounts, while key components of the balance of payments have been compiled using surveys. Over the next few months, we will begin to compile balance of payments data on a quarterly basis and implement other key recommendations of the IMF technical assistance mission. To this end, we are requesting further external support so that our statistical agencies can implement the proposed surveys.

27. **We remain committed to pursuing a cautious external debt management strategy, relying on grant financing and highly concessional borrowing.** While grant financing remains high, there is significant pressure from some donors to increase borrowing to fund our large investment needs, especially in infrastructure. Given the still fragile post-conflict environment, we strongly believe that uninterrupted multilateral and bilateral support is fundamental to maintain medium-term fiscal and external sustainability and ensure the success of our financing strategy. Consistent with the SMP, we will continue to adopt a prudent debt strategy, and seek generous debt relief from existing bilateral creditors.

28. **The end-March 2005 benchmark related to the completion of a full reconciliation of the survey of external debt was not met on account of the limited response from creditors.** We are committed to continue our good faith efforts to reconcile fully our external liabilities and complete the survey of external debt by end-September 2005 (a new structural benchmark). As a first step, we intend to seek the assistance of the Paris Club Secretariat to help contact Paris Club creditors regarding outstanding obligations. We also welcome the assistance of Fund staff in facilitating contacts between the government of Afghanistan and officials of non-Paris Club creditors.

E. Structural Reforms

29. **More generally, we remain committed to creating an environment friendly to private investment.** Structural reforms to that effect are underway and include work to introduce a modern and simplified tax system, establish an adequate legal framework for business, simplify procedures for enterprises, and publication in the Official Gazette of an investment law. We are also focusing our efforts on restructuring state-owned enterprises (SOEs). Classification of the SOEs by envisaged restructuring method and an economic restructuring plan should be adopted by the Cabinet by end-September 2005.
F. Poverty Reduction Strategy

30. We have started working with the donor community to prepare a National Development Strategy, which will form the basis for an Interim Poverty Reduction Strategy Paper (I-PRSP) by end-October 2005. Accordingly, we are taking steps to establish an institutional framework to coordinate and conduct work on the I-PRSP. The working group of predominantly Afghan experts is now in place and will be working under an Inter-Ministerial Committee that should be established shortly.

G. Statistical Issues

31. The improvement of the statistical database remains a central concern of the government of Afghanistan. In that context, and consistent with the current work program to implement the statistical master plan, we will adopt a statistical law by end-September 2005. In addition, with support from the donor community, the Central Statistical Office will be restructured. Finally, we intend to launch in June–July 2005 three key surveys, including the national risk vulnerability assessment survey on rural households, the integrated living standard survey on household income and expenditure, and the integrated business enterprise survey (expected to cover a sample of about 1000 medium and large enterprises). These surveys will help strengthen the statistical database and feed into the work on poverty reduction conducted in the context of the National Development Strategy.

H. Technical Assistance

32. We are continuing an assessment of the technical assistance we have received from various donors to rationalize technical assistance throughout the government. We anticipate that this assessment will lead to some redeployment of resources to broaden ownership of the reform program. We greatly appreciated the recent technical assistance program put in place by the IMF to address technical assistance needs in the fiscal, monetary, consumer price inflation, balance of payments, and legal areas.

I. Program Monitoring

33. The SMP will continue to be monitored using the definitions, data sources, and frequency of monitoring set out in the attached Technical Memorandum of Understanding (TMU). The quantitative indicators for end-June, 2005, and end-September 2005 are included in Table 1. The structural benchmarks are set out in Table 2. The government will continue to make available to Fund staff all core data, appropriately reconciled and on a timely basis, as specified in the TMU, and will notify Fund staff prior to taking any policy actions and developments that might impact upon the program.
34. **The Technical Coordination Committee (TCC) is gradually developing ownership of the program.** It will continue in the months ahead to monitor implementation of the SMP and provide core data to the Fund. At the same time, we see the need for the TCC to broaden its role and develop an analytical capacity, while reaching out to other government agencies. We will also engage the TCC with the work on the macroeconomic issues that need to be covered in the context of the work involved with the NDS and I-PRSP.

35. **Discussions on the fifth review of the program are scheduled to take place in early August 2005,** based on indicative targets and benchmarks for end-June 2005. At the time of those discussions, the quantitative indicators and structural benchmarks for end-September 2005 may be revised in light of developments.
Table 1. Islamic Republic of Afghanistan: Quantitative Indicators, 2004/05–2005/06
(In millions of Afghani, unless otherwise indicated; cumulative changes from beginning of fiscal year)

<table>
<thead>
<tr>
<th></th>
<th>2004/05</th>
<th>2005/06</th>
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<tbody>
<tr>
<td></td>
<td>Dec. 20</td>
<td>Mar. 20</td>
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<tr>
<td></td>
<td>Indicative</td>
<td>Preliminary</td>
</tr>
<tr>
<td></td>
<td>Target</td>
<td>Estimate</td>
</tr>
<tr>
<td>Currency in circulation (ceiling) 1/</td>
<td>9,265</td>
<td>8,315</td>
</tr>
<tr>
<td>Claims of the banking system on the central government (ceiling)</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Gross international reserves of the central bank (floor) (in millions of dollars)</td>
<td>115.0</td>
<td>469.5</td>
</tr>
<tr>
<td>Fiscal revenue of the central government (floor)</td>
<td>8,649</td>
<td>8,880</td>
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</table>

**External debt**

a) New medium- and long-term nonconcessional external debt (with original maturities of one year or more) contracted or guaranteed by the government (ceiling) 2/3/

b) New nonconcessional debt with an original maturity of less than one year (ceiling) 3/4/5/

**Memorandum item:**

Currency in circulation (level triggering consultation) | 10,702       | ...     | 12,392        | ...     | 3,508         | 7,298         |

Sources: Data provided by the Afghan authorities; and Fund estimates and projections.

1/ At end-2003/04, currency in circulation amounted to Af 28.8 billion.
2/ Excluding rescheduling arrangements, but including debt with maturities of more than one year.
3/ This benchmark will be evaluated on a continuous basis.
4/ Concessional debt is defined as debt with a grant element of at least 60 percent calculated on the basis of currency-specific discount rates, based on the OECD commercial interest reference rates (CIRRs).
5/ On a contracting or guaranteed basis. Excluding debt related to normal import transactions.
### Table 2. Islamic Republic of Afghanistan: Structural Benchmarks, March 2005–September 2005

<table>
<thead>
<tr>
<th>Structural Benchmarks</th>
<th>Target Date</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Publish in the Official Gazette the amendments to the revenue laws: (i) enacting the income tax reform package; and (ii) ensuring that the revenue laws supersede all other legislation in revenue-related matters.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Consolidate all recent revenue measures into the existing revenue code and publish as a single document.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Complete the survey of external debt, including reconciliation with creditors.</td>
<td>End-March 2005</td>
<td>Not Implemented</td>
</tr>
<tr>
<td>Transfer of DAB’s commercial holdings to the Ministry of Finance, and transfer of ownership of marketable gold and silver in the palace vaults to the DAB.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Improve government payments by initiating (i) a system of non-cash payments to vendors; and (ii) a pilot for direct salary payments for the employees of two ministries.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Approve (by the Cabinet) the Customs Code.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Ensure that budget allotments and authorized staff positions are established for all budget users (center and provinces) to allow timely salary payments every month.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Publish an official estimate of the annual revenue forgone as a result of tax holidays, exemptions or concessions and a time-bound plan, approved by the Ministry of Finance, to address all existing tax exemptions or concessions.</td>
<td>End-March 2005</td>
<td>Implemented</td>
</tr>
<tr>
<td>Publish in the Official Gazette the banking law.</td>
<td>End-March 2005</td>
<td>Implemented</td>
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<tr>
<td>Adopt (by the Cabinet) and publish in the Official Gazette the financial management law.</td>
<td>End-June 2005</td>
<td></td>
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<tr>
<td>Publish the financial statements of the 2003/04 external audit of DAB.</td>
<td>End-June 2005</td>
<td></td>
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<tr>
<td>Reconcile the government accounting records with the government’s bank account.</td>
<td>End-September 2005</td>
<td></td>
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<tr>
<td>Publish the 2004/05 audited financial statements (core budget).</td>
<td>End-September 2005</td>
<td></td>
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<tr>
<td>Adopt (by Cabinet) a comprehensive external debt management strategy.</td>
<td>End-September 2005</td>
<td></td>
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Table 2. Islamic Republic of Afghanistan: Structural Benchmarks, March 2005–September 2005 (concluded)

<table>
<thead>
<tr>
<th>Structural Benchmarks</th>
<th>Target Date</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contact the Secretariat of the Paris Club to assist with the comprehensive review of, and reconciliation of, debt owed to Paris Club creditors; and continue to contact the non-Paris Club creditors for a full reconciliation of external obligations, including those that did not respond to earlier requests for debt reconciliation.</td>
<td>End-September 2005</td>
<td></td>
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<tr>
<td>Publish in the Official Gazette: the proposed amendments to the income tax law to provide for administrative powers and for additional corporate tax reform measures.</td>
<td>End-September 2005</td>
<td></td>
</tr>
<tr>
<td>Commence implementation of recently approved tax measures, notably the business receipt tax on hotels, restaurants, telecommunications, and airlines and the wage withholding tax, accompanied by a taxpayer education program.</td>
<td>End-September 2005</td>
<td></td>
</tr>
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</table>

1/ Some donors did not respond to the authorities’ request for debt reconciliation.
Amendment to the Technical Memorandum of Understanding

1. Paragraph 5 will be replaced with: “Currency in circulation is defined as total currency (new Afghani) issued by DAB. It excludes currency held in the presidential palace vault, in DAB main vault, and in the vaults of DAB’s provincial branches, but includes currency in the vaults of DAB’s district branches.”