

## International Monetary Fund

[Sierra Leone](#) and the  
IMF

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Arrangement for  
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**Sierra Leone:** Letter of Intent, Memorandum of Economic and  
Financial Policies, and Technical Memorandum of Understanding

December 5, 2008

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

December 5, 2008

Mr. Dominique Strauss-Kahn  
Managing Director  
International Monetary Fund  
Washington, D.C. 20431  
U.S.A.

Dear Mr. Strauss-Kahn:

1. The attached Memorandum on Economic and Financial Policies (MEFP) supplements the one attached to my letter to you dated June 5, 2008. It describes recent economic developments and progress in the implementation of the PRGF-supported program during the first half of 2008 as well as the policies that we intend to implement during the remainder of 2008 and in 2009.
2. On July 7, 2008, the Executive Board completed the second review under the three-year arrangement for Sierra Leone under the Poverty Reduction and Growth Facility (PRGF). The Government of Sierra Leone in collaboration with staff of the IMF carried out a review under the program for the first half of 2008 during 9–23 September 2008. The mission also reviewed the program for the remaining period in 2008 and the framework for 2009.
3. Despite strong efforts, program implementation during the first half of 2008 was uneven. Two out of the 9 quantitative performance criteria (PCs)—domestic revenue and domestic primary fiscal balance—were missed. The shortfall in revenue was due to technical reasons as a payment of about Le 6 billion received from a mining company in June was not credited to the Consolidated Revenue Fund (CRF) until 2 July 2008. The target for domestic primary fiscal balance was not met because of expenditure overruns in the provision of fuel for the World Bank-supported Emergency Power Project (EPP) due to the increase in the price of oil and duplicate transfers to Local Councils. We are currently implementing revenue-enhancing measures in order to meet the revenue target for the year as a whole. We have also reduced budgetary allocations for the third and fourth quarters of 2008 to ensure that full-year budget envelopes will be adhered to (except for the provision of fuel for the EPP).
4. In view of the foregoing, the Government of Sierra Leone requests for a waiver for the non-observance of the performance criteria related to domestic revenue and domestic primary fiscal balance.

5. The Government of Sierra Leone requests the completion of the third review under the PRGF arrangement and the release of the fourth disbursement upon completion of the review. It also requests additional support from the Fund representing 10 percent of the quota to help strengthen the central bank's foreign reserve position. The government is aware that an augmentation will require completion of an update safeguards assessment of the central bank, and is fully committed to providing Fund staff with all the information and cooperation required to complete this in a timely manner.

6. The government of Sierra Leone believes that the policies set forth in the attached MEFP are adequate to achieve the objectives of its program for 2008 and 2009, but stands ready to take any further measures that become necessary for this purpose, in close consultation with the Fund. The fourth and fifth reviews shall take place in May 2009 and November 2009, respectively based on the end-December 2008 and end-June 2009 quantitative PCs and the applicable structural PCs. In addition, we will hold discussions with IMF staff on the sixth review to be completed by April 2010, based on quantitative and structural PCs for end-December 2009. The government of Sierra Leone will also continue to provide the staff of the Fund with the information required to accurately assess Sierra Leone's progress in executing the policies contained in the attached MEFP. Furthermore, it will continue to consult with the IMF on its economic and financial policies, in accordance with the Fund's policies on such consultations.

7. The government of Sierra Leone agrees, in line with its commitment to transparency and accountability, to the publication of this letter, its attachments, and the related staff report.

Very truly yours,

/s/

David O. Carew

Minister of Finance and Economic Development

Attachments

## ATTACHMENT I. SIERRA LEONE: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

December 5, 2008

### I. INTRODUCTION

1. This memorandum supplements the policies presented in our Memorandum of Economic and Financial Policies (MEFP) of June 5, 2008 (IMF Country Report N° 08/249). It reviews developments during the first half of 2008 and outlines the macroeconomic policies and structural reforms that the government of Sierra Leone (GoSL) will pursue during the remainder of 2008 and in 2009.

### II. PROGRAM PERFORMANCE IN THE FIRST HALF OF 2008

2. **Despite strong efforts, program implementation during the first half of 2008 was uneven.** Two out of nine quantitative performance criteria (PCs)—for domestic government revenue and primary fiscal balance—were missed (Table 1). On the structural front, the continuous structural PC on the monthly meetings of the Monetary Policy Committee (MPC) as well as the June structural benchmark (SB) on the legislation introducing the Goods and Services Tax (GST) were observed. The end-September structural PC on the promulgation of the interest rate and penalties for late/underpayment of taxes, as well as the end-September structural benchmark on the introduction of Tax Payer Identification Number (TIN), was observed. Also, the ban on exports of rice and palm oil instituted at the beginning of the food crisis, has been removed.

3. **The global food and fuel crisis has posed serious challenges to macroeconomic stability.** While growth prospects remain strong as evidenced by the fast growth in credit to the private sector during the first half of this year, continued intensification and expansion of food crops, and robust activity in the construction and service sector, inflation has picked up significantly reaching 18 percent at end-July (12-month inflation). The surge in food and oil prices has also been exerting heavy pressure on the balance of payments. The external current account deficit is expected to increase in 2008 and the foreign exchange reserve position of the Bank of Sierra Leone (BSL) would drop more than originally programmed, in nominal terms, to absorb the terms of trade shock.

4. **Despite stepped up revenue mobilization efforts by the National Revenue Authority (NRA), the domestic revenue target was missed.** The NRA collected Le 294.5 billion, against a target of Le 301 billion. The shortfall is due to technical reasons as a payment of about Le 6 billion received from a mining company in late June was not credited to the Consolidated Revenue Fund (CRF) until July 2. Domestic revenue not collected by the NRA was short of the target by Le 3.5 billion (less than 0.1 percent of GDP) mainly due to a decision by the Ministry of Transport to suspend the vehicle license fee pending improvement in the vehicle registration process.

5. **Budget execution during the first half of 2008 was complicated by the need to consolidate the new administration and by lapses in fiscal discipline.** Nonwage noninterest current expenditures were higher than programmed by Le 22 billion (0.4 percent of GDP) due to overruns and extrabudgetary spending. The overruns related mainly on the following items: (i) fuel cost for the World Bank-supported Emergency Power Project (EPP) due to higher-than-projected increase in world oil prices; (ii) transfers for health services administrated by local councils; (iii) domestic and overseas traveling by government officials; and (iv) recall and postings of new ambassadors and diplomatic staff. Extrabudgetary expenditures comprised essentially GoSL contribution to the Bumbuna Hydroelectric Project (BHP) and a payment for the printing of new passports. Despite underspending on wages and salaries, shortfall in revenue and spending over commitments on nonwage noninterest expenditures led to a higher-than-targeted primary fiscal deficit by about Le 23 billion (0.4 percent of GDP). The larger-than-programmed primary fiscal deficit was financed by the nonbank private sector.

6. **A final audit report on the verification of domestic suppliers' arrears for the period 2005–07 has been finalized.** Total verified and accepted arrears for 2007 amount to about Le 20 billion (0.3 percent of the 2008 nominal GDP), against an initial estimate of Le 26 billion.<sup>1</sup> Verified and accepted arrears accrued in 2005–06 also amounted to Le 20 billion. The 2007 audited arrears will be cleared in 2008 while those accumulated in 2005–06 will be in 2009–10 as fiscal space is created. With respect to the out-of-court settlement agreed with a domestic supplier to repay domestic arrears dating back to the civil war in the late 1990s, we have reached an agreement to defer implementation of the out-of-court settlement pending the mobilization of resources to retire the claims. In the meantime, a goodwill payment will be made in 2008, consistent with our strategy note on how government intends to implement the agreement reached with the creditor.

7. **On the monetary side, both reserve and broad money grew less rapidly than programmed during the first half of 2008.** This was mainly on account of lower than projected net foreign assets. The PCs on net domestic assets of the BSL and net bank credit to the government were observed.

8. **Bank credit to the private sector continued to grow strongly.** Falling lending rates in response to a drop in Treasury bill yields, continued strong demand for loans from construction, import trade, and communication sectors, and the entry of new banks with high liquidity were the main reasons for this sharp increase. Yield on the 91-day treasury bills fell significantly (by 600 basis points) to about 15 percent during the first half of 2008 due to excess demand from market participants, arising from a drop in the amount of 91-day

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<sup>1</sup>This initial estimate is the difference between the total unpaid claims of Le 41.1 billion indicated in our June 2008 MEFP, minus budgeted allocations for Local Councils that were not effectively transferred in 2007.

treasury bills offered, mainly as a result of the fact that the BSL had commenced sourcing the 182-day and 364-day treasury bills from the stock of the maturing 91-day T-bills.

9. **The banking sector continues to be saddled by rising nonperforming loans.** However, banks are making efforts to set aside adequate provisions or writing down bad loans. Loss of several staff members has strained the ability of the BSL to closely supervise the banks. Nevertheless, steadfast implementation of the recently-adopted financial sector development strategy aimed at strengthening the banking supervision capacity of the BSL will help address this problem.

### III. POLICIES FOR THE REMAINDER OF 2008

10. **We have revised slightly the macroeconomic framework to incorporate the impact of the global food and fuel crisis.** Real GDP growth is projected at 5.5 percent, down 0.5 percentage points compared to the program. Average inflation is expected to rise to 15.6 percent (against the previous projection of 14.1 percent). The deeper-than-anticipated food and fuel crisis, coupled with an unexpected drop in diamond production, would widen the external current account deficit (including official transfers) to 7.1 percent of GDP compared to the previous projection of 6.5 percent. Gross official reserves are expected to absorb some of the fuel and food price shocks, dropping from 4.6 months of imports coverage in 2007 to 3.9 in 2008.

11. **To ensure that the revenue target for the year as a whole is achieved, we have taken a number of additional short-term measures.** These include: (i) the transfer of all off-budget revenue collected by Ministries, Departments, and Agencies (MDAs) to the CRF; (ii) restoration of the excise tax and the ad-valorem import duty on petroleum products to their 2006 levels; (iii) enforcing the payment of tax arrears with the application of interest and penalties on under/late payment of tax; and (iv) the transfer of the collection of the vehicle license, mining fees, freight levy fees pharmacy license fees, and cost recovery proceeds on the sale of essential drugs from the current collection agencies to the NRA. The NRA will implement and enforce the findings of the recently concluded field audit of firms and continue to strengthen the Enforcement and Debt Management Unit of the Income Tax Department.

12. **It has become necessary to revise the projected domestic primary fiscal balance by 0.4 percent of GDP to accommodate the impact of higher fuel prices.** As indicated in ¶ 5, fuel for the EPP will cost Le 24 billion more than budgeted and the GoSL's contribution to the BHP (about Le 22 billion) was not programmed. These budgetary overruns will be partly offset by projected savings on wages and salaries (about Le 16 billion) and the remaining financing needs will be covered by the transfer of Le 2 billion per month (starting in September 2008) by the National Power Authority (NPA) to the CRF, as agreed in the context of the EPP, as well as a targeted budgetary assistance expected from the Peacebuilding Fund.

13. **Money growth will continue to be restrained to reduce inflation expectations.** The BSL will conduct open market operations to control the growth of reserve money. To aid in this effort, the government has converted in September another Le 15 billion noninterest-bearing non-marketable securities held by the BSL and plans to convert an additional Le 32.5 billion by end-2008 in order to reach Le 100 billion that has been agreed upon in MOU between the MoFED and the BSL. The Monetary Policy Technical Committee (MPTC) will continue to meet on a monthly basis and coordination between the MoFED and the BSL will be improved.

14. **Measures are being taken to strengthen the financial sector.** The BSL is promoting competition in the banking sector. Between June 30, 2008 and September 30, 2008, three new banks have commenced operation. The BSL is focusing on developing interbank market by discouraging banks to access its rediscount facility so that banks can lend/borrow from each other for their short-term liquidity needs. It is also working on introducing an efficient payments system, including a Real Time Gross Settlement System (RTGS). To help build the securities markets, the BSL has harmonized the government securities auction system, has introduced 182-day (since July 31) and 364-day (since January 15) treasury bills, and a book-entry system (BES) has been installed and is near completion. However, the use of the BES is currently restricted to primary markets auction. To reduce the vulnerability from nonperforming loans, the BSL will enforce the minimum capital requirement for all banks of Le 12 billion by end-2008 and Le 15 billion by end-2009. To prevent money laundering, the BSL has developed a draft strategy on anti-money laundering and combating the financing of terrorism. A Financial Intelligence Unit has been set up to implement the strategy once validated with stakeholders.

15. **The BSL has initiated the preparation of a comprehensive financial sector development plan (FSDP) and an internal Medium-Term Strategy (BSL-MTS).** These two diagnostic reviews are being undertaken in collaboration with other stakeholders in the financial sector and supported by development partners interested in the financial reform and are expected to be completed by end-2008. They come on the heels of the strategy for the financial sector adopted in May 2008 (a prior action for the second review). Both the FSDP and the BSL-MTS will provide the analytical and diagnostic foundation on which to modernize and increase the responsiveness of both the central bank and the overall financial system to growth, quality employment and poverty alleviation, as well as to global challenges.

#### IV. PROGRAM FOR 2009

16. **The program objectives for 2009 are to achieve real GDP growth of 5.5 percent, reduce end-of-period inflation to single digits, and rebuild foreign exchange reserves to at least 4.2 months of imports.** Output growth should continue to benefit from improved supply of energy, ongoing public initiatives to increase agriculture productivity and intensification, and higher public investment in basic infrastructure. With a

mix of domestic policies and external developments, inflation should ease but remain in double digits due to lingering effects of the world food and fuel crisis. International reserves are expected to slowly recover in 2009, helped by the requested augmentation of access under the PRGF arrangement. The government is also finalizing the second generation Poverty Reduction Strategy Paper (PRSP II), which will clearly set the Government's priorities for reducing poverty over the medium term.

## **Fiscal policy**

17. **Fiscal policy in 2009 will aim at consolidating macroeconomic stability and laying the basis for sustained economic growth.** The proposed 2009 budget envisages a significant reduction in the primary fiscal deficit (1 percent of GDP) while accommodating an increase in public investment. Its main features are:

- *On the revenue side*, total domestic revenue is projected at 12.3 percent of GDP (from 11.8 percent in 2008), based on strict enforcement of the provisions of the existing tax legislations, application of policy measures adopted in the 2007 and 2008 Finance Acts, as well as the expected improved efficiency expected from the modernization plan of the NRA, in particular the automation of the customs procedures and the establishment of the Domestic Tax Department. In addition, a “specific” excise tax will be introduced on alcohol beverages based on alcohol content and the import duty on cement will be restored (to 20 percent), consistent with the ECOWAS Common External Tariff. The government will ensure timely passage of relevant legislation for the introduction of the GST by April 2009 and fast-track the renegotiation of mineral rights to enhance domestic revenue collection. Government will eliminate discretionary tax and duty exemptions and provide logistics to the Preventive Services and Special Duties unit of the NRA to intensify border patrols to reduce cross border smuggling.
- *On the expenditure side*, the wage bill is projected to stay at around 6 percent of GDP. It includes an increase of 15 percent in basic pay for civil servants and the hiring of about 1000 police officers. Current nonwage noninterest expenditures will be limited at 6.9 percent of GDP and include an allocation of Le 42 billion (0.6 percent of GDP) to cover the government's share in the EPP during the first half of the year.<sup>2</sup> Capital spending will be increased by 1.2 percentage points of GDP to accommodate the public infrastructure improvement program. The domestic interest bill includes the cost of the planned conversion of an additional Le 60 billion from the outstanding noninterest-bearing non-convertible securities into marketable securities and the issuance of a Le 130 billion of T-bonds in two tranches to recapitalize the BSL.
- *Regarding financing items*, the government's recourse to central bank financing will be limited to the use of MDRI resources, which should not exceed Le 88 billion.

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<sup>2</sup> The BHP is expected to come on-stream by June 2009.

Commercial bank financing will be limited to Le 12 billion. Domestic financing will also include an allocation of about Le 11.9 billion to clear part of the audited 2005–06 domestic arrears.

18. **Budget execution and control will be enhanced in 2009.** In particular, control over expenditure commitments will be tightened to avoid overruns and prohibition of extrabudgetary spending will be strictly enforced. To strengthen the role of line ministries in the budget execution process, budget officers will be recruited and assigned to MDAs that have IFMIS “rolled out”, with a view to make budget committees in these public entities fully operational. The recently-adopted policy of full pass-through of world oil prices to domestic petroleum prices will help insulate the budget, and the social consequences will be effectively addressed via well-targeted subsidies for vulnerable groups.

### **Monetary and exchange rate policies**

19. **Monetary policy will continue to aim at mitigating second round effects of the food and fuel crisis.** Reserve money is projected to grow at a rate just below that of nominal GDP (13.4 percent against 14.3 percent). This level will be sufficient to accommodate the continued strong expansion of private sector credit, projected donors’ inflows, the use of MDRI resources and the rebuilding of international reserves to 4.2 months of import by end–2009. In addition, the government has committed to provide additional Le 60 billion of marketable securities to enhance the ability of BSL to control reserve money growth.

20. **The BSL will seek to increase exchange rate flexibility to allow for appropriate exchange rate responses to external shocks.** In particular, the BSL will participate, as needed, on the foreign exchange market also as a buyer, not solely as a seller. This would allow the BSL to more actively manage its foreign exchange reserves. The BSL will continue to seek to balance treasury bills sales, foreign exchange auctions, and potential foreign exchange purchases for its optimal monetary policy mix.

### **Other structural reforms**

21. **Our structural reform agenda will continue to be directed at supporting private sector development.** To this end, efforts will aim at strengthening the financial sector, restoring the financial viability of the power and water public utility companies, and improving governance and accountability in the use of public resources. The support of our development partners remains critical for the success of these reforms.

22. **Ongoing reforms in the financial sector will be actively pursued to deepen financial intermediation and ensure strong and competitive financial sector.** The action plan for the development of the financial sector adopted in June 2008 calls for a number of measures to be taken in 2009 to strengthen banking supervision in light of the large expansion in private sector credit and deterioration in banks’ asset quality. In this context, the

BSL will recruit and train staff on banking supervision. It will also adopt new off-site surveillance guidelines for banks, consistent with the requirements of the Revised Banking Act and Other Financial Services Act. Also, establishment of a credit reference bureau is under consideration. The Sierra Leone Stock Exchange Company has been granted license to operate a stock market starting in September 2008 and it plans to commence trading by the end of 2008. A number of acts (Companies Act, Securities Bill, Bankruptcy Bill, and Collective Investment Scheme Bill) have been revised or drafted to help promote financial intermediation, especially in the riskier and longer-term segments of financial markets. The Anti-Money Laundering (AML) Act 2005 is being revised to include provisions for combating the financing of terrorism (CFT) and regulations in line with international standards are being developed to enhance our AML/CFT compliance program. The BSL is also in the process of revising the Bank of Sierra Leone Act of 2000. Actions will also be taken to timely complete an audit of the 2008 financial statements of the central bank. The hiring process will be completed by end-December 2008 and the audit will be finalized by end-March 2009.

23. **The capital base of the BSL will be strengthened to enable it perform its mandates.** In line with the recommendations of the May 2008 Fund technical mission, the government will recapitalize the central bank by allowing it to convert, in two tranches, Le 130 billion of noninterest-bearing securities into 5-year T-bonds at 9 percent interest rate.

24. **Steps are being taken to accelerate the restructuring of the NPA and improve its finances.** Preparations are advancing for the adoption of a comprehensive electricity tariff policy by end-December 2008. Greater oversight over the finances and technical operations of the NPA will be henceforth exercised.<sup>3</sup> In this regard, the GoSL, in consultation with the World Bank, will appoint resident experts at the NPA for billing/collections and financial control with line authority and a Supervisory Engineer to advise the NPA Board. Under the EPP, which is partly funded by World Bank and the GoSL through the use of MDRI resources, the NPA was to be making a monthly payment of Le 2 billion starting April 2008. Up to August 2008, NPA did not pay any amount into the CRF and as a result, total amount outstanding is Le 10 billion (for 5 months). NPA will put in place a credible plan for the payment of these arrears starting this year. NPA is to make further monthly payments of Le 2 billion from September to December 2008 as well as Le 1.92 billion of a loan extended to the NPA in December 2006. This will bring total payment in 2008 to Le 11.9 billion.

25. **The government remains committed to promoting good governance and accountability in the use of public resources.** We have recently launched the national Anti-

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<sup>3</sup> NPA has been instructed to comply without any further delay with the commitment to transfer monthly Le 2 billion to the CRF.

Corruption Strategy (ACS) for 2008–13<sup>4</sup> and enacted into law in September 2008 a revised Anti-Corruption Act that strengthens the power of the ACC. The Act is now in conformity with the African Union and the United Nations Convention Against Corruption and requires that all high-level public servants declare their assets.<sup>5</sup> The GoSL will conduct semi-annual assessments of the national ACS to monitor progress in its implementation and take remedial actions as needed.

26. **Two major risks may affect the implementation of the 2009 program but steps are being made to mitigate them.** First, the lingering effects of the global food and fuel crisis may intensify pressure to increase basic pay for civil servants beyond what is budgeted for 2009. Second, the ongoing financial crisis could impact negatively on the balance sheet of commercial banks, thus constraining credit availability. Also, a decline in remittances would adversely affect the balance of payments. The government will continue to seek consensus among political and social players concerning the need to maintain fiscal discipline by executing the budget as voted by the parliament. Also, the BSL will monitor closely developments in the financial sector and will take necessary measures to avoid any major credit crunch in the economy. As in 2008, we will take the necessary steps to ensure that the 2009 budget is shielded from the potential liabilities of the contract with the second independent power provider.

## V. PROGRAM MONITORING

27. The program will be monitored based on quantitative PCs set for end-December 2008, end-June 2009 and end-December 2009, as well as on quantitative benchmarks set for end-March and end-September 2009, as indicated in Tables 1 and 2 annexed to this attachment. The program will also be monitored based on structural performance criteria and benchmarks during 2009, as presented in Table 3.

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<sup>4</sup> The government also nominated a high-powered Steering Committee to ensure that the strategy will be fully implemented.

<sup>5</sup> President Koroma has already declared his assets.

**Table 1. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2008**

(Cumulative change from beginning of calendar year to end of month indicated; Le millions, unless otherwise indicated)<sup>1</sup>

	2008											
	March		June				September				December	
	Proj.	Act.	Performance Criteria	Adjusted Targets	Act.	Met or Not Met	Indicative Targets	Adjusted targets	Act.	Met or Not met	Performance criteria Prog. <sup>2</sup>	Revised
<b>Performance criteria</b>												
Net domestic bank credit to the central government (ceiling)	50,871	47,124	116,820	95,488	82,711	Met	85,039	174,229	137,660	Met	127,200	127,200
Unadjusted target (ceiling)				116,820				85,039				
Adjustment for the shortfall (excess) in external budget support				0				57,638				
Adjustment for the issuance of treasury securities to the private sector				-21,332				31,552				
Net domestic assets of the central bank (ceiling)	37,565	21,810	90,080	90,080	66,137	Met	58,043	115,681	69,918	Met	179,209	179,209
Unadjusted target (ceiling)				90,080				58,043				
Adjustment for the shortfall (excess) in external budget support				0				57,638				
Domestic primary fiscal balance of the central government (floor)	-46,798	-31,787	-81,355	-81,355	-103,731	Not met	-107,265	-107,265	-139,227	Not met	-137,446	-165,720
Subsidies to National Power Authority (ceiling) <sup>3</sup>	0	0	0	0	0	Met	0	0	0	Met	0	0
Gross foreign exchange reserves of the central bank, US\$ millions (floor)	-2.8	-9.0	4.45	-25.82	-17.44	Met	-9.75	-27.32	-3.20	Met	-23.2	-23.2
Unadjusted target (floor)				4.45				-9.75				
Adjustment for the shortfall (excess) in external budget support <sup>4</sup>				-30.6				-17.88				
Adjustment for the shortfall in the US\$ value of IMF disbursement				0.32				0.32				
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities				0.00				0.00				
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) <sup>3</sup>	0	0	0	0	0	Met	0	0	0	Met	0	0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) <sup>3</sup>	0	0	0	0	0	Met	0	0	0	Met	0	0
External payment arrears of the public sector (ceiling) <sup>3</sup>	0	0	0	0	0	Met	0	0	0	Met	0	0
Total domestic government revenue (floor)	149,492	150,955	326,874	326,874	316,832	Not met	508,354	508,354	492,703	Not met	692,697	692,697
<b>Indicative target</b>												
Poverty-related expenditures (floor)	70,247	67,619	157,680	157,680	210,422	Met	243,362	243,362	305,143	Met	326,700	326,700
<b>Memorandum items:</b>												
External budgetary assistance <sup>5</sup>	32,230	0	0	0	0		143,043	143,043	85,405		211,200	211,200
Net credit to government by nonbank private sector <sup>6</sup>	-1,036	20,646	10,574	10,574	31,906		14,258	14,258	-17,294		-6,909	-6,909
Disbursements under the PRGF (US\$ millions)	0	0	6.92	6.92	7.24		6.92	6.92	7.24		13.84	13.84

Sources: Sierra Leonean authorities; and IMF staff calculations.

<sup>1</sup> The performance criteria and indicative targets shown in this table are defined in the Technical Memorandum of Understanding (TMU).

<sup>2</sup> EBS/08/66 (June 9, 2008)

<sup>3</sup> These apply on a continuous basis.

<sup>4</sup> The reserve accumulation target, unlike the monetary targets, was calculated to include foreign aid disbursements that did materialize in the period.

<sup>5</sup> Including program grants and program loans.

<sup>6</sup> Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

**Table 2. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2009**(Cumulative change from beginning of calendar year to end of month indicated; Le millions, unless otherwise indicated) <sup>1</sup>

	2009				
	March		June	September	December
	Indicative Prog. <sup>2</sup>	Targets Proj.	Performance Criteria	Indicative Targets	Performance Criteria
<b>Performance criteria</b>					
Net domestic bank credit to the central government (ceiling)	153,709	27,138	8,409	48,396	100,212
Unadjusted target (ceiling)					
Adjustment for the shortfall (excess) in external budget support					
Adjustment for the issuance of treasury securities to the private sector					
Net domestic assets of the central bank (ceiling)	138,436	7,594	-84,338	-33,131	-69,477
Unadjusted target (ceiling)					
Adjustment for the shortfall (excess) in external budget support					
Domestic primary fiscal balance of the central government (floor)	-10,569	-32,754	-71,596	-96,924	-116,158
Subsidies to National Power Authority (ceiling) <sup>3</sup>	0	0	0	0	0
Gross foreign exchange reserves of the central bank, US\$ millions (floor)	7.3	-8.2	26.6	24.2	39.3
Unadjusted target (floor)					
Adjustment for the shortfall (excess) in external budget support <sup>4</sup>					
Adjustment for the shortfall in the US\$ value of IMF disbursement					
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities					
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) <sup>3</sup>	0	0	0	0	0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) <sup>3</sup>	0	0	0	0	0
External payment arrears of the public sector (ceiling) <sup>3</sup>	0	0	0	0	0
Total domestic government revenue (floor)	181,108	180,745	386,640	602,667	824,014
<b>Indicative target</b>					
Poverty-related expenditures (floor)	80,292	82,069	180,993	256,398	330,623
<b>Memorandum items:</b>					
External budgetary assistance <sup>4</sup>	26,900	25,200	121,275	121,275	188,201
Net credit to government by nonbank private sector <sup>5</sup>	-1,684	5,328	-272	7,056	7,328
Disbursements under the PRGF (US\$ millions)	0.00	0.00	11.34	11.34	22.68

Sources: IMF staff projections

<sup>1</sup> The performance criteria and indicative targets shown in this table are defined in the Technical Memorandum of Understanding (TMU).<sup>2</sup> EBS/08/66 (June 9, 2008)<sup>3</sup> These apply on a continuous basis.<sup>4</sup> Including program grants and program loans.<sup>5</sup> Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

**Table 3. Sierra Leone: Structural Conditionality for 2009**

Measure	Timing	Macroeconomic Rationale
<b>Structural performance criteria</b>		
<ul style="list-style-type: none"> <li>Provide to Fund staff the Monetary and Policy Committee (MPC) monthly minutes that include the monthly projections for government revenue and expenditures made available by the Ministry of Finance to the Bank of Sierra Leone to produce a monthly liquidity forecast</li> </ul>	On a continuous basis	To enhance liquidity management at the Accountant General Department and monetary forecasting at the BSL
<ul style="list-style-type: none"> <li>Recruit and assign budget officers to MDAs that have IFMIS 'rolled out' and ensure their budget committees are fully operational.</li> </ul>	End–June	To improve budget formulation and execution
<ul style="list-style-type: none"> <li>Adoption by the BSL of new off-site surveillance guidelines for banks consistent with the requirements of the revised Banking and Other Financial Services Act, and introduction of new reporting requirements based on these guidelines</li> </ul>	End–September	To enhance the bank supervision framework as well as the supervisory ability of the central bank
<ul style="list-style-type: none"> <li>Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional</li> </ul>	End–December	To improve efficiency of revenue collection efforts
<b>Structural Benchmarks</b>		
<ul style="list-style-type: none"> <li>Adoption by the cabinet of the implementation decree for new and modernized customs law and regulations that reflects the WTO agreement and protects government customs revenue.</li> </ul>	End–June	To modernize customs law and regulations
<ul style="list-style-type: none"> <li>Adoption by the cabinet of a simplified and fully designed small taxpayer regime with supporting draft legislation</li> </ul>	End–September	To extend the tax base
<ul style="list-style-type: none"> <li>Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO).</li> </ul>	End–December	To ensure full and efficient implementation of the GST

## ATTACHMENT II. SIERRA LEONE: TECHNICAL MEMORANDUM OF UNDERSTANDING

December 5, 2008

### I. INTRODUCTION

1. This memorandum sets out the understandings between the Sierra Leonean authorities and the International Monetary Fund (IMF) regarding the definitions of the quantitative and structural performance criteria (PCs) and benchmarks for the remainder of the program supported by the Poverty Reduction and Growth Facility (PRGF) arrangement, as well as the related reporting requirements. Unless otherwise specified, all quantitative PCs and indicative targets will be evaluated in terms of cumulative flows from the beginning of the period, as specified in Table 2 of the Memorandum of Economic and Financial Policies (MEFP) of the Government of Sierra Leone (GoSL) for 2009.

2. **Program exchange rates.** For the purpose of this TMU, foreign currency denominated transactions will be converted into Sierra Leonean currency (leones) using the program exchange rates shown in the box below and the market exchange rate against the US\$ in effect on October 31, 2008 (as published in *International Financial Statistics*) for transactions in other currencies than the US dollar, the Euro, the U.K. Pound, and the Special Drawing Rights (SDR).

Leone/US\$	3,150
US\$/Euro	1.28
US\$/Pound	1.62
US\$/SDR	1.49

### II. QUANTITATIVE PERFORMANCE CRITERIA

#### A. Gross Foreign Exchange Reserves of the Bank of Sierra Leone (BSL)

3. **Definition.** Unless otherwise noted here, gross foreign exchange reserves of the Bank of Sierra Leone (BSL) are defined as reserve assets of the BSL. Reserve assets are defined in the IMF's *Balance of Payments Manual* (5<sup>th</sup> ed.) and elaborated in the reserve template of the Fund's International Reserves and Foreign Currency Liquidity: Guidelines for a Data Template. They exclude foreign assets not readily available to, or controlled by, the monetary authorities.

4. **Adjustment clauses.** The floor on gross foreign exchange reserves will be adjusted (a) downward (or upward) by the amount in U.S. dollars of the shortfall (excess) in programmed external budgetary assistance—the downward adjustment will be capped at the equivalent of US\$20 million while the upward adjustment will be equal to the amount—if

any, exceeding US\$20 million;<sup>1</sup> (b) downward (upward) for any shortfall (excess) in the U.S. dollar value of disbursements from the IMF under the PRGF arrangement; and (c) upward (or downward) for any increase (or decrease) in BSL short-term (one year or less in original maturity) foreign currency-denominated liabilities (to residents and nonresidents).

### **B. Net Domestic Assets of the BSL**

5. **Definition.** Net domestic assets (NDA) of the BSL are defined as the end-period (based on daily data) stocks, during the month of the test dates, of the reserve money less net foreign assets calculated at the program exchange rates. Reserve money includes currency in circulation and required reserves on leone deposits. Net foreign assets of the BSL are defined as gross foreign exchange reserves (defined above) minus foreign liabilities (defined below). Foreign liabilities are defined as short-term (one year or less in original maturity) foreign currency-denominated liabilities of the BSL to nonresidents and the outstanding use of Fund credit.

6. **Adjustment clauses.** The ceiling on the NDA of the BSL will be adjusted upward by the amount of the shortfall in the external budgetary assistance at the test dates, up to a maximum of US\$20 million. In the event of an excess in the external budgetary assistance greater than US\$20 million, the NDA ceiling will be adjusted downward by the amount exceeding US\$20 million. The leone value of the cumulative shortfall or excess in external budgetary assistance will be converted at the program exchange rates.

### **C. Net Domestic Bank Credit to the Central Government (NCG)**

7. **Definition.** NCG refers to the net banking system's claims on the central government and is defined as follows:

- the net position of the government with commercial banks, including: (a) treasury bills; (b) bonds issued by the GoSL; (c) loans and advances; less (a) Central government deposits (defined to include account balances under the authority of controlling officers, but excluding deposits in the sterilization account); plus
- BSL holdings of (a) GoSL statutory bonds; (b) ordinary GoSL bonds; (c) bonds in respect of loans to current and former parastatals; (d) treasury bills on the trading portfolio of BSL; (e) other government stock; (f) HIPC debt relief deposits; less (a) special noninterest-bearing government stocks to cover foreign exchange valuation losses; (b) treasury bills and treasury bearer bonds held by the BSL for

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<sup>1</sup>External budgetary assistance is defined as program grants and program loans, excluding HIPC assistance.

monetary policy operations; and (c) bonds issued by the GoSL in subscription to the paid-up capital of the BSL.

8. **Adjustment clauses.** The ceiling on the increase in NCG will be adjusted upward (downward) by up to the amount of the shortfall (excess) in external budgetary assistance. The upward adjustment will be capped at the equivalent of US\$20 million while the downward adjustment will be equal to the amount—if any, exceeding US\$20 million. The leone value of the cumulative shortfall or excess in external budgetary assistance will be converted at the program exchange rates. The ceiling will also be adjusted downward (upward) by the excess (shortfall) in the leone value of net issues of government securities to the nonbank private sector vis-à-vis the program target (specified in the memorandum items in Table 2 of the MEFP).
9. **Data source.** The data source for the above will be the series “Claims on Government (Net)” submitted to Fund staff and reconciled with the monthly monetary survey prepared by the BSL. These data will be reconciled with monthly reports with the monetary data (Treasury bill transactions, ways-and-means account, and Treasury bearer bond transactions).
10. **Definition of Central government.** Central government is defined for the purposes of this memorandum to comprise the central government and those special accounts that are classified as central government in the BSL statement of accounts. The National Social Security and Insurance Trust and public enterprises are excluded from this definition of central government.

#### **D. Domestic Revenue of Central Government**

11. **Definition. The floor on total domestic central government revenue** is defined as total central government revenue, as presented in the central government financial operations table, excluding external grants.

#### **E. Domestic Primary Fiscal Balance of Central Government**

12. **The floor on the domestic primary budget balance** of the central government is defined as domestic revenue minus total expenditure and net lending, excluding interest payments, and externally-financed capital expenditure.

#### **F. Subsidies to the National Power Authority (NPA)**

13. **Definition.** The term “subsidy” refers to any financial government support (i.e., unrequited transfers) to the NPA. It does not include the government’s on-lending of external loans for capital expenditure of the enterprise. The subsidy is to be reduced by the amount of

arrears accumulating in regard to the charges for government's electricity consumption. This PC will apply on a continuous basis.

### **G. External Payment Arrears of the Public Sector**

14. **Definition.** External payment arrears of the public sector are defined as the stock of new external overdue debt-service payments by the public sector. For the purposes of this PC, the public sector comprises the central government, regional government, all public enterprises and the BSL. **The nonaccumulation of external arrears is a performance criterion during the program period.** Excluded from this PC are those debts subject to rescheduling. This PC will apply on a continuous basis.

### **H. New Nonconcessional External Debt Contracted or Guaranteed by the Public Sector with an Original Maturity of One Year or More**

15. **Definition.** Those are defined as all forms of new debt with original maturity of one year or more contracted or guaranteed by the public sector.<sup>2</sup> This PC applies not only to debt as defined in point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274 (00/85), August 24, 2000) but also to commitments contracted or guaranteed for which value has not been received. Excluded from this PC are disbursements from the IMF and those debts subject to rescheduling. For the purposes of this PC, the "public sector" is as defined in ¶ 14 above. This PC will apply on a continuous basis.

### **I. External Short-Term Debt Contracted or Guaranteed by the Public Sector**

16. **Definition.** External short-term debt is defined as external debt stock with a maturity of less than one year contracted or guaranteed by the public sector. Debt is defined in Annex I of this TMU. For this purpose, short-term debt will exclude normal trade credit for imports. For the purposes of this PC, the public sector is as defined above. This PC will apply on a continuous basis.

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<sup>2</sup> Debt is considered concessional if it has a grant element equivalent to 35 percent or more. Calculation of the degree of concessionality of new external borrowing is based on the last 10-year average commercial interest reference rate (CIRR) of the Organization for Economic Cooperation and Development (OECD) for loans with maturities of at least 15 years and on the last six-month average CIRR for loans maturing in less than 15 years.

### III. QUANTITATIVE PERFORMANCE INDICATORS

#### Poverty-related Expenditures

17. **Definition.** Poverty-related expenditures refer to those expenditures in the areas identified in Table 2 of the Sierra Leone HIPC Decision Point Document. These budgetary expenditures include but are not limited to those sub-components that are financed by drawdown from the HIPC Relief Account at the BSL.

### IV. STRUCTURAL PERFORMANCE CRITERIA

18. The government will complete the following actions in 2009:
- The Ministry of Finance will provide monthly projections for government revenue and expenditures to the BSL for use in producing a monthly liquidity forecast to be transmitted to the Monetary Policy Committee, which will meet monthly to provide guidance on the stance of monetary policy in the month ahead. Minutes of each meeting will be transmitted to Fund staff (on a continuous basis).
  - Recruit and assign budget officers to MDAs that have IFMIS “rolled out” and ensure their budget committees are fully operational (by end–June).
  - Adoption by the BSL of new off-site surveillance guidelines for banks consistent with the requirements of the revised Banking and Other Financial Services Act, and introduction of new reporting requirements based on these guidelines (by end–September).
  - Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional (by end–December).

### V. STRUCTURAL BENCHMARKS

19. The government will complete the following actions by the specified dates:
- Adoption by the cabinet of the implementation decree for new and modernized customs law and regulations that reflects the WTO agreement and protects government customs revenue (by end–June).
  - Adoption by the cabinet of a simplified and fully designed small taxpayer regime with supporting draft legislation (by end–September).

- Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO) (by end–December).

## **VI. PROGRAM MONITORING**

20. The Sierra Leonean authorities shall maintain a program-monitoring committee composed of senior officials from the Ministry of Finance and Economic Development; the Bank of Sierra Leone, and other relevant agencies. The committee shall be responsible for monitoring performance under the program, recommending policy responses, informing the Fund regularly about the progress of the program, and transmitting the supporting materials necessary for the evaluation of PCs and benchmarks. In addition, the Net Domestic Financing Technical Committee shall provide the Fund with weekly minutes of its meetings complemented with the minutes of the monthly meetings of the Inter-Agency Committee for National Statistics progress report on the program on a monthly basis within four weeks of the end of each month, using the latest available data.

## **Implementation of the Revised Guidelines on Performance**

### **Criteria with Respect to Foreign Debt**

The term “debt” has the meaning set forth in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted on August 24, 2000 which reads as follows: “(a) For the purpose of this guideline, the term “debt” will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, i.e., advances of money to obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers’ credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property. (b) Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt”. (c) Excluded from this performance criterion are normal import-related credits, disbursements from the IMF, and those debts subject to rescheduling arrangements”.

### Sierra Leone: Summary of Data to Be Reported to IMF Staff

Type of Data	Tables	Frequency	Reporting Deadline
Real sector	National accounts	Annual	End of year + 9 months
	Revisions of national accounts	Variable	End of revision + 2 months
	Disaggregated consumer price index	Monthly	End of month + 2 weeks
Public finance	Net government position and details of nonbank financing, including the stock of the float, treasury bills, and bonds, as well as privatization receipts	Monthly	End of month + 6 weeks
	Government flow-of-funds table (Government Financial Operations Table) with supporting documentation (final) and presented on commitment and cash basis	Monthly	End of month + 6 weeks
	Petroleum product pricing formula, tax receipts by categories of petroleum products	Monthly	End of month + 6 weeks
	Stock of outstanding payment commitments with a breakdown between current and capital expenditures	Monthly	End of month + 6 weeks
	Import duty exemptions by end-users and tariff regimes and estimates of corresponding revenue losses	Quarterly	End of quarter + 6 weeks
Monetary and financial data	Monetary survey	Monthly	End of month + 6 weeks
	Balance sheet of the central bank	Monthly	End of month + 6 weeks
	Consolidated balance sheets of commercial banks	Monthly	End of month + 6 weeks
	Borrowing and lending interest rates	Monthly	End of month + 6 weeks
	Results of foreign exchange and Treasury Bills auctions	Weekly	End of week + 3 days
	Stocks of government securities	Monthly	End of month + 6 weeks
	Banking supervision ratios	Quarterly	End of quarter + 8 weeks
	Gross official foreign reserves	Weekly	End of week + 3 days
	Foreign exchange cashflow table	Quarterly	End of quarter + 4 weeks

**Sierra Leone: Summary of Data to Be Reported to IMF Staff (continued)**

<b>Type of Data</b>	<b>Tables</b>	<b>Frequency</b>	<b>Reporting Deadline</b>
Balance of payments	Balance of payments	Annual	End of year + 3 months
	Revised balance of payments data	Variable	When revisions occur
	Exports and imports of goods (including a volume of key minerals and fuels)	Monthly	End of month + 3 months
External debt	Outstanding external arrears and repayments (if applicable)	Monthly	End of month + 4 weeks
	Details of all new external borrowing and guarantees provided by government on new borrowing	Monthly	End of month + 4 weeks
	External debt service payments (separately on principal and interest payment) to each creditor	Monthly	End of month + 4 weeks
HIPC Initiative and MDRI Monitoring	Statement of special account at the BSL, that receives resources generated by the HIPC Initiative and tracks their use	Monthly	End of month + 4 weeks
	Statement of special MDRI account at the BSL and the corresponding poverty-reducing spending financed	Monthly	End of month + 4 weeks
	Minutes of the meeting of the Net Domestic Financing (NDF) Technical Committee	Weekly	End of meeting + 2 weeks
	Minutes of the meeting of the Monetary Policy Committee	Monthly	Date of meeting + 2 weeks