Comoros and the IMF

Press Release:
IMF Executive Board Completes Second Review Under ECF Arrangement with the Union of the Comoros and Approves US$2.42 Million Disbursement January 21, 2011

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

November 29, 2010

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

1. Following the courageous institutional reforms initiated two years ago, the Union of the Comoros is gradually returning to a path of political stability. This process should be consolidated after the December 2010 island and presidential elections, when the first President of the Union and Governors of the islands will be chosen in accordance with the 2009 constitutional amendments and in strict observance of the rotating Union Presidency. These important developments create a political climate that is calmer and more conducive to development efforts. The government intends to use this opportunity to accelerate the ongoing reforms to boost growth and more effectively combat poverty, with the support of the IMF and other development partners of the Comoros.

2. The government's economic policies continue to be built upon the National Poverty Reduction and Growth Strategy Paper (PRGSP) adopted in 2009, which serves as the foundation for the three-year reform program supported by the IMF under the Extended Credit Facility (ECF). In the context of this program, the government intends to strengthen its efforts to stabilize the economy to lay the foundations for sustained and equitable growth, while improving public finances and strengthening the country’s economic and social infrastructures. Thus, the government is working with resolve to expand fiscal space so as to increase spending in priority and growth-supporting sectors. To strengthen overall economic competitiveness and foster stronger growth, the ECF program continues to include an important agenda focused on restructuring public utilities. The government is also engaged in reassessing the priority actions of the PRGSP and will establish a more realistic implementation timetable for them. It intends to ensure the rigorous implementation of this refocused PRGSP action plan starting in 2011.

3. Our discussions with Fund staff for the second review of the ECF program established that all performance criteria and quantitative and structural benchmarks for end-June 2010 were observed. The primary fiscal balance was kept within the program ceiling, thanks in particular to firm control over non-transfer expenditures, including wages. In the structural area, efforts to computerize the civil service payroll are ongoing, in particular with
the coming on stream of the computerized pay slip system. However, the fiscal position deteriorated in September following delays in the collection of revenue from some taxpayers, as well as an unforeseen increase in expenditure on goods and services associated with preparations for the end-year elections.

4. The government is determined to continue its fiscal consolidation efforts. It intends, before end-November 2010, to obtain payment of tax arrears from the third quarter, and to collect additional revenues under its economic citizenship program. This would enable it to meet its revenue target for the current fiscal year. The government nonetheless recognizes that expenditures on goods and services cannot realistically be expected to be held within the program limit, because of the cost of the elections. However, by endeavoring to hold all other expenditure categories within program limits, the government should be able to minimize any slippage from its budget outturn objective. In light of these corrective measures, the government requests completion of the second review and disbursement of the related ECF resources.

5. A number of positive developments in 2010 have had a favorable impact on the country’s economic performance. Political tensions have been eased significantly, in tandem with an increase in foreign aid and the return of tourists. Moreover, after a cutback associated with the Yemenia accident in 2009, in-country visits by members of the Diaspora rose sharply in 2010. Even more important, credit to the economy has been sustained, supported by expanding financial intermediation. All these factors explain the relative acceleration in the rate of real GDP growth, which is expected to reach 2.1 percent as compared with an initial projection of 1.8 percent. Inflation remains moderate, owing to the country’s participation in the franc zone. Reflecting a significant increase in imports financed with help from grants from development partners, the external current account deficit is not expected to narrow in 2010.

6. The government’s IMF-supported reform program under the ECF is aimed at underpinning a sustainable economic recovery that is now taking shape. The program’s architecture and basic objectives remain unchanged. However, to take account of the impact of lower-than-expected budget support, we wish to request a modification of the end-December 2010 performance criterion for net credit to the government. The program will continue to focus on a prudent fiscal policy, and will seek to accelerate the structural reforms necessary to enhance competitiveness. Underpinning policies are set forth in the attached memorandum on economic and financial policies; the government intends to implement them with determination. If necessary, it would consult Fund staff before any revisions are made, in accordance with the Fund's policy on such consultation. It is expected that the third review of the ECF arrangement will take place in June 2011, and that the fourth review will be completed by mid-September 2011.
7. In line with our commitment to transparency in government operations, we agree to the publication of documents relating to our discussions with Fund staff under the second review of our ECF-supported program.

Sincerely yours,

/s/
Ahmed Abdallah Mohamed Sambi,
President, Union of the Comoros

/s/
Mohamed Bacar Dossar
Minister of Finance, Budget, and Investment

/s/
Governor of the BCC
Mzé Abdou Mohamed Chanfiou
Vice Governor of the BCC
ATTACHMENT 1

UNION OF THE COMOROS

MEMORANDUM ON ECONOMIC AND FINANCIAL POLICIES FOR 2011

I. INTRODUCTION

1. The economic reforms supported by the International Monetary Fund under the Extended Credit Facility (ECF) are aimed at improving fiscal sustainability, building institutional and governance capacity, and rehabilitating economic and social infrastructure, particularly public utilities, in order to stabilize the macroeconomic framework, enhance the competitiveness of the economy, and impart new impetus to growth so as to combat poverty more effectively. This memorandum takes stock of progress in implementing these reforms in 2010. It also sets out the measures and policies that the government plans to implement in 2011 in order to achieve its objectives.

II. ECONOMIC DEVELOPMENTS AND PROGRAM PERFORMANCE

A. Recent economic developments and outlook for end-2010

2. Economic activity recovered modestly. GDP growth is expected to reach 2.1 percent in 2010, a rate slightly higher than that of 2009. Economic growth is beginning to benefit from the effects of relative political stability and a more favorable sub-regional situation, reflected in a substantial increase in external assistance and, in all likelihood, in foreign direct investment. Inflation should continue to be contained, reflecting the country’s membership in the franc zone. Excluding the impact of spending for the elections in December 2010, overall fiscal performance has remained in line with the program’s objectives. However, tax revenues, in particular from domestic direct and indirect taxes, remain below program targets owing to the persistence of weaknesses in tax administration. Government revenue is expected to be equivalent to the 14.4 percent of GDP envisaged under the program, thanks to a good performance in customs revenues and the boost provided by nontax revenue, in particular the revenues associated with the economic citizenship program. The value of imports increased, driven by rising prices for major imported products and supported by increased external assistance. Consequently, the external current account deficit is expected to deteriorate in 2010. Foreign exchange reserves should remain at a comfortable level, equivalent to 6.1 months’ imports of goods and nonfactor services.

3. The external debt of the Comoros remains unsustainable. It is expected to be equivalent to 308 percent of goods exports (in net present value terms) at end-2010. The
government is continuing its efforts to find a comprehensive solution to its debt situation under the HIPC Initiative, for which it reached the decision point in July 2010. It intends to continue ensuring satisfactory implementation of the reforms with assistance from its partners, including the timely implementation of triggers, so as to reach the completion point in 2012. At present, in conformity with the debt rescheduling agreement reached with Paris Club members in November 2009, we have signed a debt rescheduling agreement with one of our principal creditors. Other agreements still pending should be finalized promptly; the government remains determined to honor the commitments entered into within this framework in a timely manner. This provides for a significant reduction in the debt service falling due during the mid-2009 to mid-2012 period. For 2010, various creditors have agreed to defer the settlement of external arrears and current debt service amounting to CF 21.2 billion, or 88 percent of the gross debt service for the year, pending debt relief under the enhanced HIPC Initiative on terms comparable to those agreed with Paris Club creditors.

**B. Program implementation**

4. **Implementation of the program was satisfactory in the first half of 2010.** All performance criteria and quantitative benchmarks were met, as were the structural benchmarks of the program; in particular, the revenue target was achieved. In addition, the target for the primary fiscal deficit was met despite spending overruns noted on transfers, in particular to the University of the Comoros. In the structural area, preparations for the introduction of computerized pay slips progressed; the government submitted to the National Assembly a draft law setting forth the personnel frameworks for the Civil Service; and the representative of the Office of the President of the Union on the reform monitoring committee (CREF) was appointed.

5. **Although weakened in the third quarter of the year, the fiscal position is expected to improve in the fourth quarter and to move closer to the initial program path for 2010.** A shortfall in revenue of CF 1.75 billion was recorded in the third quarter, reflecting the combined impact of: (i) the still limited effectiveness of new revenue measures under the program, the full yield of which will not be realized until the next few months; (ii) abandonment of the 5 percent increase in the tax on petroleum products, which was deemed politically sensitive; and especially (iii) the late collection of profits tax payable by the State-owned Telecommunications Company (Comores Télécom). Owing to this revenue shortfall and delays in the disbursement of financial support from some development partners, the main fiscal objectives of the program for end-September, including the target related to net credit to the government, could not be met. The government has taken corrective measures. In particular, in November it obtained settlement of the profits tax payable by Comores Télécom, as well as the payment of sizable revenues under the economic citizenship program. In tandem with the improved yield from the program’s new tax measures for 2010, in particular the introduction of fees on the use of radio frequencies, these efforts should enable the government to meet its revenue objective for the year. However, the government still faces an irreducible overrun in spending associated with the
elections, equivalent to 0.1 percent of GDP. Under these circumstances, the primary domestic fiscal deficit is expected to amount to 1.6 percent of GDP in 2010 (2.6 percent of GDP in 2009), as compared with the initial program target of 1.5 percent of GDP. In addition, owing to the cancellation of budget support expected from the European Union (CF 1.8 billion), the accumulation of government deposits with the BCC is expected to be less than projected, necessitating a change in the ceiling on net credit to the government from CF -1.130 billion to CF 156 million. These developments require a modification of this performance criterion for end-December 2010.

6. **Preparation of the public utility reforms is continuing in the second half of 2010.** The government has recruited consultants and begun work on auditing the 2009 accounts of Comores Télécom, which will be followed by an appraisal of the enterprise's net worth with a view to issuing calls for expressions of interest from potential strategic partners in the period ahead. At the same time, a committee has been established for monitoring the reform of the petroleum product-importing company (Société Comorienne des Hydrocarbures—SCH) in order to assist the government with finalizing its choice of an appropriate reform strategy. Finally, with support from the AfDB, the government is continuing preparatory work for the reform strategy for the electricity company (MAMWE).

III. **ECONOMIC AND FINANCIAL POLICIES FOR 2011**

A. **Macroeconomic Framework**

7. **In 2011, real GDP is projected to increase by 2.5 percent, and inflation to remain moderate.** Growth is expected to be driven by subsistence agriculture, private construction supported by funding from the Diaspora, the rehabilitation of economic infrastructure financed by development partners, a rebound in financial services resulting from increased financial intermediation, and a greater availability of electric power. Furthermore, attracted by the easing of political tensions, new sectors of activity are expected to emerge with some dynamism; in particular, an inter-island transport service is expected to be launched and work should begin on rebuilding the Hôtel Galawa, which will support growth. Price pressures are not projected to increase in 2011, which will help contain inflation below 3 percent. However, given the low level of exports and the continuing high demand for imports, the external current account deficit is projected to increase to 13.6 percent of GDP.

B. **Fiscal Policy**

8. **The government is resolved to continue its ongoing fiscal consolidation efforts in 2011.** The fiscal program will be focused on measures to mobilize government revenue and improve the control of expenditure, particularly wage outlays. The deficit of the domestic primary fiscal balance is not expected to exceed the equivalent of 1.3 percent of GDP, compared with an average of 2.1 percent of GDP in 2008-2009. The government’s net financing needs for fiscal 2011, after debt relief, is estimated at 2.2 percent of GDP, and will be fully covered by budgetary support from development partners. If the government
receives external budget support in excess of programmed amounts, it will consult with the IMF on its use and will establish a new supplementary budget specifying how these resources will be allocated, giving priority to the settlement of domestic payments arrears and to other priority sectors.

9. **Domestic revenue is expected to reach CF 30.175 billion (14.2 percent of GDP).** Achieving this objective will require an improvement in the efficiency of the tax and customs administrations. At the Directorate-General of Taxes (DGI), two major reforms will be carried out by end-March 2011: (i) establishment of a Board of Directors made up of the Minister of Finance of the Union and the Governors (or their delegates) and an operational unit bringing together the tax offices of the Union and the islands, with a director-general who has sole responsibility for reporting to the authorities through the Board of Directors; and (ii) the effective operation of offices of the large taxpayer unit in Anjouan and Mohéli. At the same time, the monitoring of declarations by large enterprises will be further strengthened in order to increase the voluntary filing rate to 95 percent. Implementation of these major reforms has benefited from technical assistance from the IMF’s Fiscal Affairs Department, from which a team of experts visited the Comoros in November 2010. In 2011, revenue mobilization will also reflect the full effect of new domestic tax measures taken in 2010, including the introduction of fees on the use of radio frequencies in the telecommunications sector. Regarding Customs, the ad valorem taxation of imports will be subject to closer monitoring. To this end, the operational resources of the central office responsible for the valuation, type, and origin of goods will be strengthened, and the flat tax per container will be eliminated definitively.

10. **To ensure that its fiscal objectives are fully met, the government intends to rigorously control expenditure.** Expenditures will be capped at CF 49.269 billion, or 23.2 percent of GDP, of which CF 18.350 billion for the wage bill, nearly CF 2.9 billion (1.4 percent of GDP) for investment expenditure, and CF 13 billion (6.1 percent of GDP) financed with own resources for the education and health sectors. The government will ensure the effective operation of its new computerized payroll management system, and the rapid completion of the census of government employees and officials following the election. It intends to ensure the timely implementation of recommendations from the census, including the elimination of fictitious workers. To avoid any new accumulation of payments arrears, the government will ensure the more effective operation of its Cash Flow Committee chaired by the Minister of Finance. Moreover, it will introduce measures aimed at improving over the medium-term the still poor quality of the public expenditure management system (see paragraph 17 below).

11. **The overall fiscal deficit (cash basis, including grants) is projected at CF 4.771 billion (2.2 percent of GDP).** With net external financing (including debt relief and other deferrals of external debt service) projected at CF -1.466 billion, and net domestic financing (including the use of CF 1.2 billion in 2010 budget support held in reserve) amounting to CF 1.549 billion, the government’s net financing requirements for 2011 are
estimated at CF 4.689 billion (2.2 percent of GDP). This will be covered as follows:
(i) World Bank: CF 1 billion; (ii) AfDB: CF 0.8 billion; (iii) Gulf region partners:
CF 1.1 billion; and (iv) IMF: CF 1.8 billion.

C. Money, Credit, and Financial System

12. Government borrowing from the banking system will remain prudent, to allow
an adequate expansion of credit to the private sector. Broad money is expected to grow at
a rate of 8.6 percent in 2011, faster than the growth of nominal GDP, compared with
12.7 percent in 2010. The required reserve ratio will continue to be the main liquidity
management instrument. Set at 25 percent in 2008, it was increased to 30 percent in 2010 in
response to a pronounced increase in demand for credit and in domestic prices in the third
quarter, as well as to a substantial increase in liquidity associated with sharply higher
external budget support. Subsequent changes in the ratio will continue to be subject to the
need for the BCC to provide adequate liquidity to the economy, while preserving overall
price and macroeconomic stability. The BCC will continue to ensure implementation of the
main recommendations from the safeguards assessment conducted in 2010. In this context,
the Bank’s cash holdings are already subjected to external auditing and certification; the
work to bring the BCC’s financial statements into conformity with international standards is
ongoing, and should be completed in 2011. In addition, the monetary data reported to Fund
staff are subject to prior review by the Bank’s internal controller. Finally, in 2011, the BCC
will complete its work to strengthen banking supervision, with technical and financial
support from the IMF and the Banque de France.

13. Overall, the financial position of the Comorian banking system continues to be
satisfactory. The prevalence of nonperforming loans declined in 2010, and though affected
by the crisis, the overall profitability of banking institutions—and microfinance institutions
in particular—remained stable. The government has also taken steps to begin strengthening
management of the National Postal and Financial Services Company (SNPSF), with a view
to improving the institution’s financial standing and helping protect depositors’ savings.

D. Balance of Payments and External Debt

14. The external current account deficit, including grants and private and official
transfers, is expected to widen in 2011, to 13.6 percent of GDP, compared with
10.2 percent in 2010. This largely reflects a return to normal levels of official grants,
following the strong expansion noted in the previous year. Having begun discussions for
substantial debt relief under the enhanced HIPC Initiative and on terms comparable to those
provided by Paris Club creditors, the government reaffirms its commitment to a prudent debt
policy so as to avoid jeopardizing the sustainability of the country's external debt.

15. Any external borrowing contracted or guaranteed by the government is subject
to prior approval by the Minister of Finance of the Union, and the autonomous
governments of the islands do not have the authority to contract or guarantee external
**borrowing.** As in the past, the government will neither contract nor guarantee any short-term or nonconcessional borrowing as defined in the Technical Memorandum of Understanding (TMU). The authorities will continue to consult the IMF before contracting or guaranteeing any concessional external debt in excess of US$20 million. With support from the African Development Bank, the Public Debt Directorate will soon be provided with an effective debt management software and training for staff. The government will shortly submit to the World Bank a request for technical assistance to assess its debt management capacity. On this basis, it will be able to develop an effective program for enhancing its expertise in this area.

### E. Structural Policies

16. **The government aims to impart new impetus to its public enterprise reform program.** To this end, it has notably made a request for multiyear technical assistance from the IFC. With support from the African Development Bank, by end-December 2010 it will finalize the recruitment of the consultant tasked with preparing the reform strategy for the electric company (MAMWE); the strategy should be completed by end-March 2011. In the first quarter of 2011, the government intends to call for expressions of interest from potential strategic partners for Comores Télécom and SCH. It will do the same for MAMWE before end-June 2011.

17. **Public finance structural reforms aim to improve budget management.** The government has requested World Bank assistance in drawing up a list of priority sector expenditures. By end-March 2011, it will adopt the terms of reference for a study aimed at introducing a budgetary framework and medium-term expenditure plans. Also by end-June 2011, it intends to adopt a list of priority expenditures which it will have rigorously monitored by the inter-unit committee responsible for monitoring PRSP implementation. This should help ensure that the saving resulting from the debt service reduction under the HIPC Initiative will be used to effectively finance the priority sectors defined in the poverty reduction and growth strategy.

18. **Efforts underway in the area of public administration are aimed at strengthening the sustainability of the budget in the medium term.** The National Assembly recently adopted new personnel frameworks for the civil service. These will be implemented starting in fiscal year 2011, making it possible in particular to reduce civil service staffing (including that of the army) to about 10,600, as compared with 12,300 at end-2010. This is more in line with the government’s financial resources. The government is continuing to seek technical and financial support from its development partners for the preparation and implementation of a staff separation support program.

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

19. **The government intends to make its Poverty Reduction Strategy (PRS) more operational.** It is improving the prioritization and the specificity of projects and policies,
especially those associated with the HIPC Initiative completion point triggers. With the assistance of development partners, the preparation of an action plan refocused on the PRSP will be finalized by end-2010. The government intends to implement it rigorously starting in 2011, with technical and financial support from its development partners.

20. The government is resolved to continue its efforts to improve the socio-demographic and macroeconomic database needed in the design and monitoring of its development policy. In this connection it is receiving significant technical assistance from the AfDB, particularly in respect of the preparation of the national accounts and the consumer price index. The program to improve the quality of national accounts and consumer price index statistics is expected to be completed in 2011.

IV. MONITORING OF PROGRAM EXECUTION

21. Before the discussion of the second review of the program by the IMF Executive Board, the government will (i) provide Fund staff with evidence of payment to the Treasury’s account at the BCC of the balance of the amount due from the profit tax (IBD) of Comores Télécom for 2010, namely CF 1.553 billion; as well as CF 2.247 billion in additional revenue from the economic citizenship program; (ii) request multiyear technical support from the International Finance Corporation (IFC) to implement smoothly the reforms of Comores Télécom and SCH; (iii) provide Fund staff with specimens of the computerized payroll slips for the Union, Ngazidja, Anjouan, and Mohéli; and (iv) request technical support from the World Bank to drawing up a list of social and priority expenditures.

22. The program will be monitored on the basis of quarterly targets with performance criteria established on a half-yearly basis (Tables 1 and 2). The authorities will provide the IMF with such information as needed to monitor the program, in accordance with the Technical Memorandum of Understanding. During the program period, the authorities will not introduce or intensify restrictions on payments and transfers for current international transactions, and will not introduce or modify any multiple currency practices, conclude any bilateral payments agreements that are inconsistent with Article VIII of the IMF's Articles of Agreement, or impose any restrictions on imports for balance of payments purposes.

23. The third review of the ECF arrangement will take place in June 2011. In the area of structural reforms, the review will focus primarily on measures aimed at strengthening control of the wage bill, particularly: (i) the introduction of computerized pay slips; (ii) completion of the census of government employees and officials; and (iii) implementation of the Civil Service organizational frameworks.
Table 1. Comoros: Quantitative Performance Criteria and Benchmarks under the ECF-supported Program ¹
(in millions of Comorian francs, cumulative since the start of the fiscal year, unless otherwise specified)

<table>
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</thead>
<tbody>
<tr>
<td>1. Ceiling on net credit to government (NCG) ²</td>
<td>-1,596</td>
<td>-1,709 met</td>
<td>-3,730</td>
<td>590</td>
<td>-1,130</td>
<td>156</td>
<td>1,179</td>
<td>1,811</td>
<td></td>
</tr>
<tr>
<td>2. Ceiling on the net accumulation of domestic payments arrears ³</td>
<td>-9,784</td>
<td>-7,323</td>
<td>-11,222 met</td>
<td>-10,284</td>
<td>-4,572</td>
<td>-11,914</td>
<td>-10,784</td>
<td>-10,784</td>
<td>0</td>
</tr>
<tr>
<td>3. Ceiling on new nonconcessional external debt contracted or guaranteed by the government ⁴, ⁵</td>
<td>0</td>
<td>0 met</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>4. Ceiling on new short-term external debt contracted or guaranteed by the government ⁴, ⁵</td>
<td>0</td>
<td>0 met</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td></td>
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<tr>
<td>5. Ceiling on accumulation of external debt service arrears ⁵</td>
<td>0</td>
<td>0 met</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td></td>
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<tr>
<td>7. Floor on total domestic revenues</td>
<td>12,028</td>
<td>12,039 met</td>
<td>20,491</td>
<td>18,740</td>
<td>28,838</td>
<td>28,848</td>
<td>7,008</td>
<td>14,446</td>
<td></td>
</tr>
<tr>
<td>8. Ceiling on expenditures by cash advances</td>
<td>150</td>
<td>148 met</td>
<td>150</td>
<td>148</td>
<td>150</td>
<td>150</td>
<td>150</td>
<td>150</td>
<td></td>
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<tr>
<td>9. Floor on domestically financed social spending</td>
<td>11,970</td>
<td>11,970</td>
<td></td>
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</table>

¹ Definitions of targets and adjusters are provided in the Technical Memorandum of Understanding (TMU).
² Unlike in the monetary survey, NCG includes net ECF purchases.
³ Targets and realizations adjusted as specified in the TMU.
⁴ Excluding trade credits.
⁵ Monitored on a continuous basis.
Table 2. Comoros: Proposed Prior Actions and Structural Benchmarks for the Arrangement Under the ECF, 2010-11

<table>
<thead>
<tr>
<th>Measures</th>
<th>Macroeconomic Justification</th>
<th>Date</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Prior actions</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Forwarding to Fund staff of evidence of the collection of profits tax arrears from 2010 owed by Comores Télécom, as well as of CF 2.247 billion in additional receipts under the economic citizenship program</td>
<td></td>
<td></td>
<td>Pending</td>
</tr>
<tr>
<td>Submission of a request for technical assistance from the World Bank for the preparation of a list of social and other priority expenditures</td>
<td></td>
<td></td>
<td>Done</td>
</tr>
<tr>
<td>Submission of a request for multiyear technical assistance from the IFC on the conduct of the reform of Comores Télécom and SCH</td>
<td></td>
<td></td>
<td>Done</td>
</tr>
<tr>
<td>Forwarding to Fund staff of specimen computerized pay slips for October for Civil Service employees of the Union, Ngazidja, Anjouan, and Mohéli</td>
<td></td>
<td></td>
<td>Done</td>
</tr>
<tr>
<td><strong>Structural benchmarks</strong></td>
<td></td>
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<td></td>
</tr>
<tr>
<td><strong>Public finance management</strong></td>
<td></td>
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<tr>
<td>Completion of the census of Civil Service employees</td>
<td>Improve control of the wage bill and public expenditure</td>
<td>December 31, 2010</td>
<td></td>
</tr>
<tr>
<td>Establishment of Large Taxpayer Unit (SFE) offices in Anjouan and Mohéli</td>
<td>Enhanced effectiveness of tax administration</td>
<td>March 31, 2011</td>
<td></td>
</tr>
<tr>
<td>Appointment of the Directorate-General of Taxes (GDI) Board of Directors</td>
<td>Enhanced effectiveness of tax administration</td>
<td>March 31, 2011</td>
<td></td>
</tr>
<tr>
<td>Adoption of terms of reference for the study on the budgetary framework and medium-term expenditure frameworks</td>
<td>Enhance the effectiveness of budgetary and expenditure management</td>
<td>March 31, 2011</td>
<td></td>
</tr>
<tr>
<td>Implementation of the new organizational frameworks for the administrations of the Union and the islands</td>
<td>Rightsizing the civil service to ensure medium-term budget sustainability</td>
<td>June 30, 2011</td>
<td></td>
</tr>
<tr>
<td>Adopt indicative targets for social and other priority expenditures</td>
<td>Improve monitoring of the use of HIPC resources</td>
<td>June 30, 2011</td>
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</table>
### Public enterprise reform

<table>
<thead>
<tr>
<th>Measures</th>
<th>Macroeconomic Justification</th>
<th>Date</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maintaining the flexible petroleum product price-setting mechanism</td>
<td>Permit a reliable supply of petroleum products and limit the pressures for subsidies on the budget</td>
<td>Ongoing</td>
<td></td>
</tr>
<tr>
<td>Adoption of the reform strategy for MAMWE</td>
<td>Permit a reliable supply of electrical energy and limit the pressures for subsidies on the budget</td>
<td>March 31, 2011</td>
<td></td>
</tr>
<tr>
<td>Call for expressions of interest from potential strategic partners for Comores Télécom and SCH</td>
<td>Permit a reliable supply of communications services and petroleum products and limit the pressures for subsidies on the budget</td>
<td>March 31, 2011</td>
<td></td>
</tr>
<tr>
<td>Call for expressions of interest from potential strategic partners for MAMWE</td>
<td>Permit a reliable supply of electrical energy and limit the pressures for subsidies on the budget</td>
<td>June 30, 2011</td>
<td></td>
</tr>
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ATTACHMENT 2

UNION OF THE COMOROS

TECHNICAL MEMORANDUM OF UNDERSTANDING

Moroni, November 29, 2010

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

I. DEFINITION

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

II. QUANTITATIVE PERFORMANCE CRITERIA

3. Quantitative performance criteria are proposed for December 31, 2010 and June 30, 2011 with respect to changes in net domestic credit to the government and net changes in domestic payments arrears; with benchmarks for March 31, 2011. The following performance criteria are proposed for monitoring on a continuous basis: (i) the external payments arrears of the government; (ii) the contracting or guaranteeing of new nonconcessional external debt by the government; and (iii) the contracting or guaranteeing of new short-term external debt by the government.

A. Change in Net Domestic Credit to the Government

Definitions

4. Net domestic credit to the government is defined as overall net credit extended to the government from domestic bank and nonbank sources. Net bank credit to the government reflects the net debt position of the government vis-à-vis the central bank, commercial banks, and the National Postal and Financial Services Company (SNPSF), as well as microfinance institutions. It is the difference between the government's gross indebtedness to the banking...
system and its claims on the banking system. These government claims include all deposits at the central bank and commercial banks, as well as Treasury cash holdings. The government's debt to the banking system includes central bank credit (statutory advances as well as any long-term credit and IMF net credit) and commercial bank credit, as well as net deposits at the SNPSF. Domestic nonbank credit to the government includes changes in the stock of Treasury bills placed in the domestic market, privatization receipts, and any other domestic financial debt of the government held outside the banking sector, other than arrears.

5. The change in net domestic credit to the government as of the date for the performance criterion or benchmark is defined as the difference between the stock on the date indicated and the stock on December 31, 2010.

Performance criteria

6. The amounts set out in Table 1 of the MEFP on Net Credit to Government for December 31, 2010 and June 30, 2011 are ceilings and constitute performance criteria. The amount set out in the above table for March 31, 2011 is a ceiling and constitutes an indicative target.

Reporting requirements

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

B. Domestic Payments Arrears

Definition

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

Performance criterion

9. Under the program, the government will not accumulate any new domestic payments arrears and will gradually reduce the outstanding amount of such arrears determined as at
December 31, 2010. The amounts set out in Table 1 of the MEFP on Domestic Payments Arrears and Net Credit to Government for December 31, 2010 and June 30, 2011 are ceilings and constitute performance criteria. The amount set on in the above table for March 31, 2011 represents a ceiling and constitutes a quantitative benchmark.

Adjuster

10. If external budget support is less than expected, the floor on the reduction of domestic payments arrears will be lowered by the full amount of the shortfall. In the case of a surplus in the amount of external budget support, the floor on the net reduction of domestic arrears will be raised by the full amount of the surplus. Cumulative from January 1 of the year in question, the program assumes external budget support of CF 19.300 billion by end-December 2010, CF 0 billion by end-March 2011, and CF 1.972 billion by end-June 2011.

Reporting requirements

11. The authorities will report to Fund staff any accumulation of domestic payments arrears as defined above as soon as incurred, as well as the status of outstanding balances (restes à payer) of the Treasury.

C. External Payments Arrears

Definition

12. External payments arrears are defined as the sum of payments due but unpaid on outstanding external debt (for a definition of external debt see paragraph 16) that has been contracted or guaranteed by the government, with the exception of external payments arrears arising from public debt being renegotiated with creditors, including Paris Club members.

Performance criterion

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

Reporting requirements

14. The authorities will report to Fund staff any accumulation of external payments arrears as soon as the due date has been missed. They will provide each month, within a maximum lag of 15 days, a table showing external debt due (after rescheduling) and paid.
D. Ceiling on the Contracting or Guaranteeing of New Nonconcessional External Debt or Short-Term Debt by the Government

Definition

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

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

17. The definition of debt, as specified in Point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt, reads as follows: “(a) For the purposes of this guideline, the term ‘debt’ will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debt can take a number of forms, including: (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers’ credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property; (b) Under the definition of debt set out in point 9(a), arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.”

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

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

**Performance criterion**

20. The government as defined in paragraph 19 will not contract or guarantee nonconcessional or short-term external debt as defined above. This performance criterion will be monitored on a continuous basis. It does not apply to debt rescheduling and restructuring operations. In addition, import-related credit and pre-export financing secured on export contracts of less than one year maturity are excluded from this performance criterion on short-term debt.

**Reporting requirements**

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

### III. **Quantitative Benchmarks**

#### A. Domestic Primary Balance

**Definition**

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

**Quantitative Benchmarks**

23. The benchmarks for the floor on the domestic primary fiscal balance, cumulative from the beginning of the 2011 calendar year, are set at CF –3.141 billion for December 31, CF –0.366 billion for March 31, 2011, and CF –1.354 billion for June 30, 2011.
**Reporting requirements**

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

**B. Government Revenue**

**Definition**

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

**Quantitative Benchmarks**

26. The floor on government revenue, cumulative from the beginning of the 2001 calendar year, is set at CF 28.848 billion for December 31, 2010, CF 7.008 billion for March 31, 2011, and CF 14.446 billion for June 30, 2011. These amounts are considered benchmarks under the program, for the respective dates.

**Reporting requirements**

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

**C. Expenditures Made by Cash Advances**

**Definition**

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

**Quantitative Benchmarks**

29. Responsibility for achieving the ceiling on expenditures outside of normal procedures rests with both the Union government and the autonomous island governments. This ceiling, cumulative from January 1, 2011, is set at CF 150 million at December 31, 2010, March 31, 2011, and June 30, 2011.
Reporting requirements

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

D. Domestically Financed Social Spending

Definition

31. Total domestically financed social spending (current and capital) is calculated, for each category of current expenditure (wages, goods and services, transfers and subsidies) and capital expenditure as: (1) expenditure executed by the Ministry of Health (under "health"), and (2) expenditure executed by the Ministry of Education (under "education"). Domestically financed social spending is classified according to the above categories (health and education) based on a classification of each project presented in the 2010 budget into health and education. Total domestically financed current and capital social spending includes social spending financed by domestic resources, including revenues, domestic financing, and general external budget support, and excludes all social spending financed by project-specific foreign grants and/or loans.

Quantitative benchmarks

32. The floor on total domestically financed social spending for the period from January 1, 2010 to end-December 2010 is set at CF 11.870 billion. This amount is an indicative target under the program.

Reporting deadlines

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

IV. ADDITIONAL INFORMATION FOR PROGRAM MONITORING

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

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

Classification of commercial bank loans by economic sector;

Interest rates;

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

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

Consumer price index; and

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

**Quarterly:**

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

**Annually:**

National accounts data;

Balance of payments data.

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