

Standard Summary Project Fiche

Project Number 2002/000.601.06.02

1. Basic Information

1.1. CRIS-Number: 2002/000.601.06.02

1.2. Title: Fiscal Policy Formation and Planning Structural Reforms

1.3. Sector: Public Administration, Public Finance, Privatisation

1.4. Location: Ministry of Finance of the Republic of Lithuania

2. Objectives

2.1. Overall Objective

The overall objective of this **0.566 MEUR** Project, of which **0.004 MEUR** is national co-financing is to strengthen the Ministry of Finance capacity to evaluate economic, structural, and revenue aspects of its taxation and expenditure policies as required for full implementation of the *Acquis* in the area of EMU, Taxation and financial and budgetary matters.

2.2. Project Purpose

The purpose of this project is to:

- Improve the capacity of Ministry of Finance to co-ordinate and prepare the Convergence and Stability Programmes in order to ensure implementation of the EMU.
- Create the administrative capacity to estimate the macroeconomic impact of public and private investment in order to improve budget planning and also to meet relevant requirements defined in regulation 1260/1999 for preparation of the Single Programming Document (SPD) for Objective 1 assistance to Lithuania.
- Increase the capacity of the Fiscal Policy Department to analyse the impact of indirect taxation on the Lithuanian budget (after harmonisation with taxation *Acquis* 92/12, 92/80, 92/81, 92/82/92/79, 92/83, 92/84 77/388, 90/435 and 90/434).

2.3. Accession Partnership and NPAA Priorities

The National Programme for the Adoption of the *Acquis 2001 and 2002* states that the main directions of the institutional development of the Ministry of Finance include strengthening of its institutional capacity in improving the forecasting of the impact of structural reforms, as well as preparing for the co-ordination of the forecasting of macroeconomic and financial indicators and reporting on the situation of the public finance when implementing EU requirements.

3. Description

3.1. Background and Justification

Lithuania as a candidate country for accession to the European Union seeks to strengthen the capacity of Government institutions in economic policy formation. According to the Regular Report on Lithuania's progress to meet the requirements for EU membership the procedures for selecting, monitoring, evaluating and reporting public investments and expenditure programmes need to be strengthened in order to improve the process of allocation of resources. In order to be able to carry

out the necessary tasks, the corresponding analytical capacity should be increased in Ministry of Finance.

The Fiscal Policy Department (FPD) of the Ministry of Finance of the Republic of Lithuania is the institution in the Government, which co-ordinates preparation of macroeconomic forecast. FPD releases macroeconomic forecasts twice a year. The FPD is responsible for three areas of analysis and forecasting: 1) macroeconomic, 2) fiscal and 3) sectoral. The FPD has three deputies responsible for: 1) macroeconomic forecasting, 2) public finance and 3) sectoral analysis.

According to the Government Resolution adopted 11 April 2001, Ministry of Finance was responsible for preparing the first Pre-Accession Economic Programme, which was submitted to the European Commission 1 October 2001. The Fiscal Policy Department is acting as the co-ordinating body for the preparation of the programme. Upon accession Ministry of Finance will be responsible for co-ordinating the preparation of the Convergence and Stability programmes.

The sectoral analysis group in FPD analyses impact of proposed new laws or government decisions on macroeconomic and financial/fiscal accounts. The Sector analysis group analyses the State social insurance and mandatory health insurance fund's budgets and make short-term forecasts; the department actively takes part in the process of reforming pension system, implementing multipillar system. FPD also makes forecasts of GDP using Income and Expenditure Approaches.

With the assistance of Harvard Institution for International Development (HIID) FPD has developed two micro-simulation models: one for analysing and forecasting personal income tax, and one for analysing and forecasting corporate income tax. The personnel are trained to use and maintain these models. However these two models need to be improved including having appropriate estimations of income distribution that give estimations for options of personal income taxation. This will improve the quality of policy simulation and decisions related to Tax Policy.

Ministry of Finance is preparing the Single Programming Document for EU Structural Funds assistance according to regulation 1260/1999. In this context Ministry of Finance needs to improve its capacity to analyse the macroeconomic impact of public and private investment in order to propose the most effective measures to increase economic growth and reduce unemployment in the country and to improve the budget planning process

Regarding the macroeconomic impact only macroeconomic modelling can stimulate the complex interdependencies between economic variables at this level. Ministry of Finance lacks certain techniques to analyse impact of structural interventions, including improving the existing calibration model:

- on forecasting policy impact on GDP using value Added and Expenditure Approaches;
- checking consistency of important sectors of structural reforms (SME sector, Agriculture and Social sector) with existing and medium-term economic policy and budget policy framework;
- carrying out the analysis of the impact of Structural Funds operations on employment (by sectors).

Secondly, the capacity of the Fiscal Policy Department also need to be strengthened in order to improve the analysis of the impact of indirect taxation on the Lithuanian economy and to implement the optimal approach concerning indirect taxation harmonisation with EU requirements, especially the Excise taxes (*Acquis* 92/12, 92/80, 92/81, 92/82/ 92/79, 92/83, 92/84 77/388, 90/435 and 90/434), where appropriate techniques should be further developed.

The staff of the Fiscal Policy Department would benefit from the transfer of knowledge from experienced foreign experts in these areas making the development of the Department quicker and more in line with the best practice in EU member states.

The Ministry of Finance is therefore seeking assistance under a PHARE twinning project to strengthen the administrative capacity of the Ministry of Finance in the area of the fiscal policy formation and structural reforms planning in the context of EU accession. The accurate analysis and forecasts for sector reforms, especially fiscal aspect is very important for a consistent economic policy planning.

3.2. Linked Activities

A number of agencies have provided training and conference opportunities to the FPD to develop human resources.

The IMF has provided technical assistance to the FPD to strengthen the institutional capacity in 1996-1998. Analytical papers were prepared in 1999 on structural issues, expenditure policy including health care reform. Sectoral analysis group was created at FPD under the recommendations of IMF.

In 1998 the Conference "Economic Policy in the Framework of Accession to the European Union and Economic and Monetary Union" under PHARE Project LI 9809.01.03.01 was organised. The conference was organised by the Delegation of the European commission to Lithuania and the Ministry of Finance with the co-operation of the Bank of Lithuania (i) to raise the level of knowledge of policy makers with regard to economic policy in relation to EU and EMU, (ii) to increase public awareness in Lithuania on the impact of EU integration on the economic policy, (iii) to provide an opportunity for delegates from each of the applicant countries aspiring to join the EU to share experience on EU accession and to strengthen ties between their respective countries in this respect and (iiii) to inform the business community and the public about the effect of EU integration on Lithuania and the region as a whole.

The assistance program provided by USAID was completed by the end of 1999 and was directed to macroeconomic and sectoral analysis. A great deal of attention was devoted to tax policy and revenue forecasting. Analytical paper was written on Education financing.

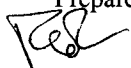
With the assistance of Harvard Institution for International Development (HIID) FPD has developed two micro-simulation models: one for analysing and forecasting personal income tax; and one for analysing and forecasting corporate income tax. The project was finalised in June 2000. The project was financed under the USAID program.

Fiscal Policy Department of the Ministry of Finance received technical support for economic forecasting according to the PHARE project. PHARE project LI 9809.01.01.01 Economic Forecasting, Institutional Development of the Ministry of Finance has been successfully accomplished by the end of October 2001.

3.3. Results

The guaranteed results expected from this project are:

- abilities of MoF to prepare the Convergence and Stability Programmes improved, in particular in terms of dealing with structural economic reforms in particular;



- skills of the staff in fiscal analysis, fiscal and macroeconomic forecasting improved; and preconditions in place for preparation of the structural reforms that form an essential part of the Convergence and Stability Programmes;
- analysis and forecasting methods advanced, and Ministry of Finance staff trained in analysing and forecasting GDP by value added approach, indirect taxation policy;
- analysis and coordination procedures concerning the consistency of important sectors of structural reforms (SME sector, Agriculture and Social sector) with existing and medium-term economic policy and budget policy framework improved;
- quality of policy simulations and decisions related to economic and taxation policies improved; administrative capacity to prepare macroeconomic evaluation of public and private investment of important sectors in Lithuania improved according to appropriate requirements for preparation of EU Structural Funds assistance;
- Corporate Income Model fully developed and ready for application;
- Household Income Model fully developed and ready for application. This will allow to monitor structural changes in disposable household income. Deep analysis of changes in household income will allow to make decisions on poverty reduction and social inequality issues and social cohesion in general;
- equipment for analysis and forecasts (PCs, software) installed and fully operational.

3.4. Activities

3.4.1. Twinning

It is expected that the twinningers will be experienced senior government officials in relevant fields. The twinningers will closely co-operate with the relevant counterparts on the Lithuanian side. The project envisages participation of long-term and short-term experts.

The activities will in particular relate to:

- assistance in developing framework (techniques) and institutional ability to forecast GDP by Value Added Approach;
- assistance in developing framework to analyse the consistency of target reforms in Agriculture sector (investment, financing, tax exemptions, support), in SME sector and in Social sector with in existing and medium-term macroeconomic and fiscal framework; to set up coordination procedures for structural reform inclusion into economic policy and budget policy framework;
- carrying out the analysis of the impact of structural funds operation on GDP and employment by sectors;
- review and support in developing Corporate Income micro-simulation model, which would take into account important behavioural responses, especially on investment decisions, to changes in the profits tax;
- review and support in improving the Personal Income micro simulation model. The extension of Personal Income to Household Income analysis should be made;
- assistance in developing framework (techniques) to analyse Indirect Taxation Policy impact on Lithuanian Budget after the Lithuanian Accession to EU;
- study tour for 3 - 4 officials from the FPD to the relevant institutions in EU member to get acquainted with the policy and analysing and forecasting techniques by: working with the relevant member states officials for one or two weeks during their visit; bringing back to Lithuania the templates and documentation related to the items corresponding to the assigned task. It is envisaged that a study tour may last up to 20 days.




The twinning input will be delivered by one PAA (16 months) and by short-term advisers (16 months). An indicative schedule of inputs is shown in the table below.

Indicative inputs for the advisers ¹			
Activity	PAA	STA	Total Months
GDP by VA approach		3	3
Establishing coordination and consistent programming procedures in the important sectors (Agriculture, SME, Social)		7	7
Corporate Income micro-simulation model	8	1	9
Household Income micro simulation model	8	1	9
Indirect Taxation Policy		4	4
TOTAL	16	16	32

Profile of PAA

The PAA (16 person months) having the overall responsibility for the project should have extensive practical experience in tax modelling, particularly in micro simulation modelling. The PAA will be responsible for the development of Household Income and Corporate Income micro simulation models.

Profile of Short Terms Advisers

The short-medium-term advisers (STA) will act as tutors to the Lithuanian staff implementing the analysis and forecasting modules. The pool of person/days for these experts is estimated at 16 months.

The STAs should have excellent communication skills with some experience of training and be able to cover the following areas:

- Forecasting GDP by Value Added approach;
- Expenditure Policy;
- Analysis of impact of EU structural funds operations;
- Household Income Taxation;
- Corporate Income Taxation;
- Indirect Taxation Policy.

Appropriate short-term adviser should be appointed to analyse the particular area.

The short-term advisers, who will work as advisors on Household and Corporate Income Taxation policy issues, should have experience in micro simulation modelling.

¹ The activities prescribed in the table encompass the development of techniques, training and consultations as well as preparation of materials and documents.




All the STAs should be fluent in English and should be capable of providing training covering workshops, classroom training, on-the-job training as well as personal advice.

3.4.2. Supply

Equipment will be limited to **0.016 MEUR**, of which **0.004 MEUR** is national co-financing and will cover computer equipment and software needed to ensure the quality of micro simulation models running and analysis making.

3.5. Lessons learned

Considering the experience obtained in the previous projects:

- a counterpart for each expert shall be selected from among the staff of the Department;
- the arrival schedule and work to be carried out by the STAs shall be agreed upon one month in advance.

4. Institutional Framework

The main institution responsible for the economic and fiscal policies is the Ministry of Finance (MoF). It implements the fiscal policy and ensures its co-ordination with the monetary policy.

The project will be implemented by the Fiscal Policy Department (FPD) at the Ministry of Finance. Presently FPD of the Ministry of Finance has 15 employees. 3 additional Lithuanian officers should be employed at Fiscal Policy Department dealing with sectoral policy. 10 officials of the Ministry of Finance will participate in the training programme.

Successful implementation of the project depends on working from outset with the professional staff of the FPD of the MoF that will be involved in developing and running the new techniques and methodology.

Each Lithuanian staff member shall be paired with a EU short-term tutor (adviser) and with a corresponding project task. The matching of tasks shall be determined in the Twinning Covenant.

In addition, a Lithuanian assistant/interpreter/translator should be hired on a full-time basis.

5. Budget (in MEUR)

Project Components	Investment Support	Institution Building	Total PHARE (I+IB)	National Co-financing	Total
Twinning		0.55	0.55		0.55
Supply	0.012		0.012	0.004	0.016
Total	0.012	0.55	0.562	0.004	0.566

The Phare amount is binding as a maximum amount available for the project. The ratio between the Phare and national co-finance amounts is also binding and has to be applied to the final contract price. The national co-financing is a tax-excluded net amount.

6. Implementation Arrangements

6.1. Implementing Agency

The CFCU is responsible for contracting and accounting of the project.

PAO: Zilvinas Pajarskas
Director of Central Financing and Contracting Unit under the Ministry
of Finance
Address: J.Tumo-Vaižganto 8^A/2 Telephone: 370 2 685367
2600 Vilnius Fax: 370 2 225335
Lithuania e-mail: info@cfcu.lt

Responsible person:

R. Vaicenavičius, Director of Fiscal Policy Department, Ministry of
Finance
Address: J.Tumo-Vaižganto 8^A/2 Telephone: 370 2 390141
2600 Vilnius Fax: 370 2 390102
Lithuania e-mail: r.vaicenavicius@finmin.lt

6.2. Twinning

The beneficiary institution is the Ministry of Finance of the Republic of Lithuania, J.Tumo Vaižganto 8^A/2, 2600 Vilnius, Lithuania.

The contact persons are:

- R. Žutautienė, Deputy Head of Fiscal Policy Department, Tel: +370 2 390 044, Fax: + 370 2 390 102, E-mail: r.zutautiene@finmin.lt
- A.Kirkilaitė, Senior Economist at Fiscal Policy Department, Tel: +370 2 390 108, Fax: +370 2 390 102, E-mail: a.kirkilaite@finmin.lt

6.3. Non-standard aspects

There are no non-standard aspects to this project and the CFCU will ensure that the PRAG and the Twinning Manual will be strictly followed. The project has two components: twinning and supply.

6.4. Contracts

There will be two contracts of the project:

Value of Twinning – **0.55 MEUR**;

Value of Supply contract – **0.016 MEUR**, of which **0.004 MEUR** is national co-financing.

7. Implementation Schedule

Component	Start of Tendering	Start of Project Activity	Project Completion
Twinning	3Q/02	2Q/03	3Q/04
Supply	4Q/02	2Q/03	3Q/03

8. Equal Opportunity

Equal opportunity principles and practices in ensuring equal gender participation in the Project will be guaranteed. Equal participation in the training programme, study tour by women and men will be assured.

9. Environment

The investment components of this Project all relate to Institutional Building activities.

10. Rates of return

The investment components of this Project all relate to Institutional Building activities.

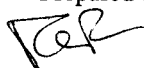
11. Investment criteria

The investment components of this Project all relate to Institutional Building activities.

12. Conditionality and sequencing

For a fair and appropriate succession of the project, it is necessary to define actions and directions to be undertaken during the project and after its completion. These elements will also be used as quality indicators and will help to identify and correct when needed. The key milestones of this project are:

- The selection of staff for each elementary module has been made.
- Analysis and forecasting methods developed and documented and accepted by the staff of MoF.
- The micro simulation models (Household Income Taxation and Corporate Income Taxation) developed and ready for application.
- The quality of analysis is sufficient for policy making.
- The study tour is finalised in terms of duration, number of participants and number of EU countries to be visited.
- Equipment (PC and software) tender launched.
- 4 PCs of proper quality delivered in time.
- E-views software installed in time.



ANNEXES TO PROJECT FICHE

- 1. Logical framework matrix**
- 2. Detailed Implementation Chart**
- 3. Contracting and Disbursement Schedule**
- 4. Preliminary PC Specification and Software**



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LOGFRAME PLANNING MATRIX FOR Project: Fiscal Policy Formation and Planning Structural Reforms				Programme Name and number:	L12002-X-XX
				Contracting Period Expires: 4Q/2004	Disbursement Period Expires: 3Q/2005
				Total Budget 0.566 MEUR	Phare Budget: 0.562 MEUR
Overall Objective Full implementation of EMU and Taxation <i>Acquis</i>				Source of Verification Regular Reports from the Commission	
Project Purpose <ul style="list-style-type: none">Improve the capacity of Ministry of Finance to co-ordinate and prepare the Convergence and Stability Programmes in order to ensure implementation of the EMU.Create the administrative capacity to estimate the macroeconomic impact of public and private investment in order to improve budget planning and also to meet relevant requirements defined in regulation 1260/1999 for preparation of the Single Programming Document (SPD) for Objective assistance to Lithuania.Increase the capacity of the Fiscal Policy Department to analyse the impact of indirect taxation on the Lithuanian budget (after harmonisation with taxation <i>Acquis</i> 92/12, 92/80, 92/81, 92/82/92/79, 92/83, 92/84 77/388, 90/435 and 90/434).				Source of Verification <ul style="list-style-type: none">Convergence and Stability Programmes and EC assessment	Assumptions <ul style="list-style-type: none">Continued Government commitment to achieving the remainder of the Taxation and EMU <i>Acquis</i>
Results <ul style="list-style-type: none">abilities of MoF to prepare the Convergence and Stability Programmes improved, esp. in terms of dealing with structural economic reforms in particular.Analysis and forecasting methods advanced, and Ministry of Finance staff trained in analysing and forecasting GDP by value added approach, indirect taxation policy.analysis and coordination procedures concerning the consistency of important sectors of structural reforms (SME sector, Agriculture and Social sector) with existing and medium-term economic policy and budget policy framework are improved.quality of policy simulations and decisions related to economic and taxation policies improved; administrative capacity to prepare macroeconomic evaluation of public and private investment of important sectors in Lithuania increased according to appropriate requirements for preparation of EU Structural Funds assistance.Household Income Model and Corporate Income Model fully developed and ready for application.				Source of Verification <ul style="list-style-type: none">Reports by CFCU, PAA, and project leadersManuals and training programmesWorking papers	Assumptions. <ul style="list-style-type: none">Ministry of Finance will support and allocate resources to ensure sustainability of the project resultsTrained staff will be retained within the system.

<ul style="list-style-type: none"> Equipment for analysis and forecasts (PCs, software) installed and fully operational. 			
Activities <ul style="list-style-type: none"> Develop analysis and forecasting techniques, and build up the corresponding institutional abilities for GDP forecasting by Value Added Approach, indirect taxation impact analysis. Develop framework to analyse the consistency of target reforms in important sectors of structural reforms (Agriculture, SME and Social sector) with in existing and medium-term macroeconomic and fiscal framework; set up coordination procedures for structural reform inclusion into economic policy and budget policy framework. Develop micro-simulation models to analyse impact of taxation on disposable household income and on corporate behaviour, which would take into account any behavioural responses, especially on investment decisions, to changes in the profits tax. 	Means <ul style="list-style-type: none"> Twinning and training package including one PAA for 16 months and short-term advisers for 16 months for the development and introduction of analysis and forecasting techniques, Supply of data processing equipment and software. 		Assumptions <ul style="list-style-type: none"> Local co-finance available when required
	Preconditions <ul style="list-style-type: none"> Qualified Twinning partner institution should be selected for the project 3 additional Lithuanian officers employed at Fiscal Policy Department dealing with sectoral policy 		

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Annex 2

Detailed Implementation Chart for the Project

Year	2002												2003												2004												2005													
Month	7	8	9	10	11	12	1	2	3	4	5	6	7	8	9	10	11	12	1	2	3	4	5	6	7	8	9	10	11	12	1	2	3	4	5	6	7													
Twinning																																																		
Supply																																																		

design
tendering
implementation

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CUMULATIVE CONTRACTING AND DISBURSEMENT SCHEDULE (0.562 MEUR)

	Date												
	2002			2003			2004			2005			
	30/06	30/09	31/12	31/03	30/06	30/09	31/12	31/03	30/06	30/09	31/12	31/03	30/06
Contracting													
• Twinning					0.55								
• Supply					0.012								
Total contracting (cumulative)					0.562								
Disbursement													
• Twinning					0.206	0.263	0.321	0.378	0.435	0.493	0.55		
• Supply					0.007	0.011	0.012						
Total disbursement (cumulative)					0.213	0.274	0.333	0.39	0.447	0.505	0.562		

Preliminary PC Specification and Software*

PC (4 units)

1. IBM compatible PC, ISO 9001 certificate
2. Processor – MS windows compatible, about 2 MHz
3. Memory - 256 MB or more for MS Windows Family OS
4. Hard disk - min. 30GB
5. Optical storage – CDRW device
6. Video system – video adapter and LCD 17” monitor
7. LAN – 100BASE-T adapter
8. Keyboard (Lithuanian), mouse
9. Operating system – latest MS Windows Family
10. Software – latest of MS Office Family

Software (one licence for 5 users)

The E-views software is needed.

* The **preliminary** specifications are noted due to quick changes in PC development.

