International Monetary Fund

Sierra Leone and the IMF

Press Release:
IMF Executive Board Completes First Review Under ECF Arrangement with Sierra Leone and Approves US$6.83 Million Disbursement
December 6, 2010

Country's Policy Intentions Documents

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

November 17, 2010

LETTER OF INTENT

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

Freetown, November 17, 2010

Dear Mr. Strauss-Kahn:

The attached Memorandum of Economic and Financial Policies (MEFP) supplements the one attached to my letter to you dated May 18, 2010. It describes recent economic developments and progress in the implementation of the ECF-supported program during the first half of 2010 and presents our policies planned for the remainder of 2010 and 2011.

All June 2010 quantitative performance criteria and indicative targets were met. The two structural benchmarks for June were met, but with a slight delay: the automatic domestic fuel-pricing formula was adopted in October to bring the domestic pump prices in line with international oil prices and the BSL adopted the new off-site surveillance guidelines for banks in November.

Although fiscal policy remained on target in the first half of 2010, spending accelerated in the second half of the year due to unanticipated expenditures on emergency power project, hiring of health care workers, higher interest payments, outlays for road construction, and payments of arrears to oil marketing companies because of delays in implementing full pass-through of international fuel prices. While tax collections are anticipated to exceed program projections, mostly explained by very good performance of the GST introduced in January, additional domestic financing of 0.9 percent of GDP will be required in 2010. Hence, the Government of Sierra Leone (GoSL) requests that the target for end-December 2010 on net domestic bank credit to the central government be modified. To further boost domestic revenue in 2011, we have raised royalties on diamonds to 6.5 percent, in line with the Mines and Minerals Act 2009. The GoSL is committed to present to Parliament a 2011 budget that constrains non-priority spending and target net domestic bank financing of about 2 percent of GDP.

On this basis, the GoSL requests that the second disbursement be made available upon completion of the first review under the ECF arrangement.

The GoSL believes that the policies set forth in the attached MEFP and Technical Memorandum of Understanding (TMU) are adequate to achieve the objectives of the new program, but stands ready to take any further measures that become necessary for this purpose, in consultation with the Fund. The GoSL will consult with the Fund in advance of revisions to the policies contained in the MEFP and continue to provide the staff of the IMF the information required to accurately assess Sierra Leone's progress in executing the policies in the MEFP. The second, third, and fourth reviews under the current program shall take place in June 2011, December 2011 and June 2012, respectively. Furthermore, the GoSL will continue to consult with the IMF on its economic and financial policies, in accordance with the IMF's policies on such consultations.

The GoSL agrees, in line with its commitment to transparency and accountability, to the publication of this letter, its attachments, and the related staff report in accordance with the procedures for publication.

Very truly yours,

________/s/__________
Samura M. W. Kamara
Minister of Finance and
Economic Development

____________/s/_____________
Sheku S. Sesay
Governor of Bank of Sierra Leone

Attachments

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

I. INTRODUCTION

1. This memorandum reviews recent economic developments and outlines the macroeconomic policies and structural reforms that the Government of Sierra Leone (GoSL) will pursue under the current Extended Credit Facility (ECF).

II. RECENT ECONOMIC DEVELOPMENTS

2. **Economic activity appears to have picked up in 2010.** Exports of diamonds have rebounded and indicators point to buoyant agricultural output. Real GDP growth is projected at 4.5 percent in 2010, compared to 3.2 percent in 2009. While lower fuel and domestic food prices eased inflationary pressures during most of 2009, inflation rose in the first half of 2010 due to the depreciation of the leone in late 2009, the introduction of the goods and services tax (GST) in January, and higher domestic fuel prices. The CPI increased by 18 percent in the 12 months through August 2010. However, so far this year, the leone has been stable against the US dollar.

3. **Fiscal policy was broadly implemented as programmed through June.** Revenue collections were above the target and current spending was close to the program, but the wage bill was higher due to higher than anticipated hiring in the health care sector. Capital expenditures were lower than programmed due to shortfalls in external project support. However, domestically financed capital spending was higher than envisaged.

4. **Monetary policy remained tight in the first half of 2010.** Growth in reserve money and broad money decelerated significantly in the first half of 2010, as programmed. Private sector credit continued to expand in the first half of 2010, albeit at a slower pace. With a stable value of the leone, the amount offered on the BSL's weekly foreign exchange auctions fell as envisaged in the program to less than US$1 million by June.

5. **Program performance was satisfactory in the first half of 2010.** All June 2010 quantitative performance criteria and indicative targets were met (Table 1) and the two structural benchmarks for June have been implemented, though with some delay (Table 2). Moreover, two of the structural benchmarks for September have been implemented, though with a slight delay, and the remaining benchmark is expected to be implemented in November 2010.

III. MEDIUM-TERM FRAMEWORK

6. **The medium term outlook for the Sierra Leonean economy is favorable.** Real GDP growth is expected to recover to 4.5 percent in 2010 and increase to 6 percent by 2012, benefiting from the recent completion of the Bumbuna power station, investment in basic infrastructure, and initiatives to improve the business climate and raise agricultural productivity. The global economic recovery will increase export demand for minerals and

cash crops, which should contribute to exchange rate stability. Combined with expanding domestic food production, this should ease inflationary pressures. Monetary and exchange rate policies will also aim at returning to single-digit inflation, with inflation projected to decline from 16 percent in 2010 to 8 percent in 2012. However, import coverage of gross foreign exchange reserves is expected to decline from 6.1 months in 2009 to 4.6 months in 2012, as imports recover with economic recovery and expansion in investment.

7. **The economic impact of newly signed mining lease agreements for iron ore could be significant.** Assuming full implementation of the planned investments, exports and tax revenue would increase substantially in the medium- and long-term. However, since these projects are still in their infancy and there are uncertainties about the timing and production volumes, they have not been incorporated in the medium-term macroeconomic projections. Moving forward, the government wishes to level the playing field for new mining investments and it will therefore apply the fiscal regime defined in the Mines and Minerals Act (MMA) 2009 and existing tax and custom acts to future mining lease agreements. Also, the government will consider, as stipulated for in the MMA, demanding an equity stake in future larger mining projects to participate in windfalls and to gain insight into the mining business.

8. **Consistent with the priorities laid out in the Agenda for Change 2008-12 (PRSP II), the emphasis will be to create fiscal space to improve basic infrastructure while maintaining macroeconomic stability**. Since grants and concessional budget financing from donors are likely to decline to pre-crisis levels in the next few years, the government recognizes the urgent need to increase domestic revenue and strengthen the efficiency of public spending. Reflecting efficiency gains from the introduction of GST and improvement in tax administration, the aim is to raise domestic revenue above 13.5 percent of GDP by 2012. To achieve this target, the GoSL will fully apply the fiscal regime stipulated in existing tax and customs acts and will resist issuing discretionary tax exemptions. Fiscal space will further be created by containing non-priority spending, and raising public sector efficiency, especially on project selection and implementation. The GoSL is committed to keeping domestic financing below 2 percent of GDP to maintain debt sustainability and prevent crowding out of the private sector.

9. **Debt sustainability will remain a priority.** The GoSL is committed to a conservative strategy of external borrowing on concessional terms. A comprehensive national debt law and procedures manual will be adopted in 2010. In collaboration with the Public Debt Unit of Ministry of Finance and Economic Development (MOFED), government agencies are working on improving the quality of debt data and reporting in order to better monitor commitments, disbursements, and debt service obligations. The Commonwealth Secretariat Debt Recording and Management System (CS-DRMS) will be electronically linked with IFMIS. In order to further improve on debt management, the Government is requesting assistance from the World Bank and the Fund with respect to developing a comprehensive Medium-Term Debt Management Strategy (MTDS).

IV. Policies for the Remainder of 2010

10. **The fiscal deficit is projected to be higher than programmed in 2010.** Fiscal spending has accelerated in the second half of 2010 due to the hiring of an additional 3,000 health care staff, unanticipated outlays for the emergency power project that was supposed to expire in June, payments of arrears on fuel subsidies, and additional infrastructure projects particularly on roads. For the year, total expenditures, including payments of arrears, are projected to be 1.5 percentage points of GDP higher than programmed. On the revenue side, the GST continues to perform better than anticipated and revenues are therefore projected to exceed the program target by 0.6 percentage points of GDP. With unchanged program budget support grants and loans, domestic bank financing is projected to increase to 3 percent of GDP from 2.1 percent as envisaged in the program. The overall fiscal deficit, excluding grants, is projected to increase to 11.5 percent of GDP from 10.8 percent of GDP in the program. In case domestic revenues, including any prepayment of taxes, exceed Le 988 billion, the additional revenue will be used to reduce domestic bank financing in 2010.

11. **The GoSL has consolidated several existing tax incentives from a number of sector-specific acts into the tax and customs acts.** The aim is to maintain the current incentives without introducing new ones, while working towards eliminating all discretionary tax incentives and exemptions. To this end, the GoSL has submitted the Revenue Management Act 2010 to Parliament for enactment. The purpose of the act is to regulate the granting of tax incentives and discretionary duty waivers. Furthermore, to evaluate the costs and benefits of this policy, the GoSL will prepare a policy review by March every year covering the previous calendar year. This review will contain a list of all projects that have benefited from the catalogue of incentives, specify the purpose of the projects, and report foregone revenue. The review will be made publicly available and submitted to the Parliament.

12. **A new Mines and Minerals Act came into effect on January 1, 2010.** In line with the act, a 6.5 percent royalty for diamond mining became effective in November 2010. The annual revenue effect is estimated at 0.2 percent of GDP.

13. **Monetary policy will remain tight to prevent the second round effects of the increase in inflation from the introduction of the GST earlier this year and from higher domestic fuel prices.** Reserve money is targeted to grow by 7.5 percent in 2010, consistent with 14 percent growth in broad money. Despite higher domestic financing of the budget, private sector credit is still anticipated to expand by a healthy 26 percent in 2010. The BSL will stand ready to tighten monetary policy further, should inflationary pressures increase. With a stable leone against the US dollar, the amount offered in the foreign exchange auction will remain at a reduced level.

14. Direct credit from the BSL to the government increased significantly in the second half of the year to finance accelerated budgetary spending. In September, government overdrafts in BSL amounted to about 2.7 percent of GDP. However, almost immediately, the BSL was able to withdraw liquidity by selling significant amounts of its holding of treasury bills to keep monetary policy on course. The GoSL recognizes shortcomings of relying on central bank financing. Hence overdrafts in BSL was reduced to about Le 175 billion in early November 2010 and will be further reduced to Le 150 billion (2 percent of GDP) by end-November 2010. In line with the BSL Act, all direct credits provided in 2010 will be repaid no later than 93 days after end-2010. Also, the GoSL is committed to revise the BSL Act to limit the use of direct credit to government in the future (see section VI).

V. Policies for 2011

15. Macroeconomic policies for 2011 will aim at improving basic infrastructure and social services while maintaining macroeconomic stability. This should help facilitate higher economic growth and lower inflation.

Fiscal policy

16. The 2011 budget envisages higher domestic revenue, a significant increase in capital spending, mainly financed by external grants or concessional loans, and a moderate domestic financing need.

17. On the revenue side, domestic revenue is projected to increase to 13.3 percent of GDP from 13 percent of GDP in 2010, reflecting an increase in diamond royalties to 6.5 percent and continued efficiency gains from GST. This projection does not incorporate any revenue from ongoing iron ore investment projects, except for the annual license fee. Grants remain at 6.8 percent of GDP as the decrease in budget support by 0.9 percentage points is compensated by an increase in project grants. Privatization proceeds are projected at 0.6 percent of GDP, reflecting sales of shares in Rokel Bank and Sierra Leone Commercial Bank, as well as proceeds from the concession of the port in Freetown.

18. On the expenditure side, a shift from current to capital spending is envisaged**.** In line with the priorities laid out in the Agenda for Change to build basic infrastructure, capital spending will increase from 8.4 percent of GDP in 2010 to 10.2 percent in 2011, financed by external grants and concessional project loans (7.5 percent of GDP) and domestic sources (2.7 percent of GDP). Wages and salaries are envisaged to decrease from 6.8 percent of GDP in 2010 to 6.5 percent in 2011, reflecting a 15 percent increase in basic salaries and savings accruing from the pay reform that would start implementation in the second half of the year. In order to conduct fair, peaceful and democratic elections in 2012, current expenditures will include Le 20 billion (0.3 percent of GDP) on elections, with additional donor support of Le 44 billion.

19. The overall fiscal deficit, excluding grants, is envisaged to increase to 12.5 percent of GDP from 11.5 percent of GDP in 2010. However, domestic bank financing is projected to decline to 1.8 percent of GDP from 3.3 percent of GDP in 2010, reflecting an increase in external project financing and privatization proceeds.

Monetary and exchange rate policies

20. **Monetary policy will aim to achieve single digit inflation by the end of 2011**. Reserve money is envisaged to grow at 14 percent that will imply a 20 percent growth in broad money and will accommodate a 31 percent growth in private credit. With a constrained access to direct credit from the central bank by the GoSL, liquidity management will be eased.

21. The authorities are committed to maintaining a flexible exchange rate to facilitate adjustment to external shocks. The BSL will limit its foreign currency sales to absorb foreign-financed budget spending and smooth short-term market volatility.

VI. Structural Reforms

22. **The structural reform program will complement macroeconomic policies to promote an efficient public sector and higher sustainable private sector-led economic growth.** Structural policies will continue to focus on improving tax administration, strengthening public financial management, and developing the financial sector (Tables 2 and 4). Policies for the two latter areas will be based on the Integrated Public Financial Management Reform Program (IPFMRP) and the Financial Sector Development Plan (FSDP), respectively.

Improving tax administration

23. **The GoSL will further step up efforts to improve tax administration and broaden the tax base**. The current tax administration suffers from inefficiencies arising from separate tax departments for GST and income and it is not conducive to enhance tax compliance. To this end, the National Revenue Authority (NRA) will integrate GST operations (taxpayer services, filing and returns processing, and coordinated audit operations) with the Large Taxpayer Office (*Structural Benchmark for December 2010*). Moreover, NRA will transfer all eligible taxpayers to the Medium Taxpayer Office (MTO) and integrate the GST administration with MTO to improve the efficiency of tax collections (*Structural Benchmark for September 2011*).

24. **The NRA will step up efforts to improve tax collection and compliance.** Measures include applying penalties for non-filing of returns and underestimation of quarterly installment payments; and levying and collecting interest on late payment of tax. In a similar vein, a new small taxpayer regime will be implemented to improve voluntary compliance (*Structural Benchmark for December 2011*).

Strengthening public financial management

25. **The GoSL will strengthen the Medium-Term Expenditure Framework (MTEF) by enhancing the planning, monitoring and evaluation process for capital projects.** The government will fully integrate a three-year public investment plan with the budget process

for 2012 budget in line with the amendments to the Government Budget and Accountability Act (*Structural Benchmark for December 2011*).

26. The GoSL is committed to building a high quality workforce in the public sector. To improve working conditions for the public service and to attract staff of high caliber, the government will develop and start implementing a multiyear pay reform (*Structural Benchmark for June 2011*). The reform will (i) realign current discrepancies in qualifications and grade placements; (ii) decompress the wage structure; (iii) retrench redundant staff; and (iv) gradually raise compensation to competitive levels financed partly from the restructuring and, if necessary, a moderate increase in the total public sector wage bill.

27. **The roll out of IFMIS to MDAs will continue to strengthen budget execution.** So far, IFMIS has been rolled out to 11 key MDAs with 2 additional MDAs in the process, accounting for about 65 percent of expenditures. The MOFED will continue to provide training and support to IFMIS users across MDAs to ensure that activities are properly and adequately captured within the system.

Financial sector measures

28. **The independence of the BSL will be strengthened by amending the BSL and Banking Acts (***Structural Benchmark for June 2011*). The amendments will enhance the independence of the BSL and align the acts with the Basel Core Principles for Effective Supervision, as recommended by recent IMF TA missions.

29. **There is a need to limit the use of BSL direct credits to the government.** This will encourage the government to improve its cash flow management and support the development of securities market. Also, the amendments to the BSL Act will (i) set a limit of the annual flow of direct credits to the government (loans and advances) to 5 percent of the actual domestic revenue in the previous budget year; (ii) require that such direct credits are repaid within 93 days from the end of the financial year (repayments may be made with marketable treasury bills that mature before the 93 day deadline); and (iii) stipulate that the BSL may purchase government securities strictly for monetary policy purposes and provided that such purchases are only made in the secondary market. While these amendments are not likely to be approved before mid-2011, the government and the BSL are committed to adhere to the above principles for BSL direct credits to the government from the beginning of 2011.

30. **The BSL will strengthen its supervisory role to reduce the vulnerabilities arising in the financial sector from NPLs**. This will be achieved by developing a new IT platform and filling open staff positions in the Banking Supervision Department of the BSL. Also, the BSL will gradually move to a risk-based supervision system. In addition, the BSL has aimed to increase the minimum capital requirement from Le 15 billion to Le 30 billion over a 5 year period, starting in 2010.

31. **To develop a long-term capital market,** the MOFED and the BSL will engage market participants, including the commercial banks, NASSIT and other non-bank financial

institutions, to develop a long-term bond market consistent with the government's financing need. The GoSL will also strengthen the capital market regulatory structure and governance by enacting the Securities and Exchange Commission's (SEC) Act and implement associated regulations, and deepen the long-term capital market with the privatization and divestiture of slated public enterprises.

32. Private sector development is constrained by limited access to financial services. Lack of financial development is evident in low credit to the private sector. Access to credit will be enhanced by strengthening information structure through establishing a credit reference bureau (*Structural Benchmark for December 2010*). To improve efficiency of transactions in the economy, the BSL is working towards strengthening the payments and settlement systems. In this context the AfDB is financing the automation of the payment system, which includes: (i) Real Time Gross Settlement; (ii) Automated Cheque Processing and Automated Clearing House; (iii) Scriptless Securities Settlement System; (iv) Core Banking Application; and (v) Infrastructure Upgrade. Contracts have been awarded to solution providers for all components and studies to gauge the scope have been conducted for most of them.

33. **To prevent opportunities for money laundering,** by the end of this year the government will submit to the parliament a new law on Anti-Money Laundering and Combating the Financing of Terrorism.

Other reforms

34. **The GoSL has committed to the principles of Extractive Industries Transparency Initiative (EITI).** The first EITI Report (covering mining for 2006–07) was published in March, and the final validation report was submitted on August 9, 2010. The validation report recommends a number of improvements to the governance and management of the process which are being considered. Furthermore, there are on-going efforts to disseminate the first Sierra Leone EITI report.

35. **There is a need to strengthen Sierra Leone's capacity to collect and disseminate economic statistics.** The GoSL is seeking technical assistance from the IMF to improve the reporting of national account and price statistics. There is a particular need to improve collection of data on agriculture output and to compute one single reliable consumer price index.

VII. Program Monitoring

36. The program will be monitored based on quantitative performance criteria for end–December 2010, end-June 2011 and end-December 2011 (Tables 1 and 3), and structural benchmarks for 2010 and 2011 (Tables 2 and 4).

Table 1. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2010 1/
(Cumulative change from beginning of calendar year to end of month indicated; Le billions, unless otherwise indicated)

	2009	2010					
		June					
	Actual Stock	*Prog.*	*Adj. Prog.*	*Act.*	*Status*	*Sept. 2/*	*Dec.*
Performance criteria							
Net domestic bank credit to the central government (ceiling)	647.3	191.5	240.4	206.5	Met	202.7	250.3
Unadjusted target (ceiling)			191.5				
Adjustment for the shortfall (excess) in external budget support			31.5				
Adjustment for the issuance of government securities to the nonbank private sector			17.3				
Net domestic assets of the central bank (ceiling)	-442.3	198.6	247.7	192.4	Met	235.5	235.1
Unadjusted target (ceiling)			198.6				
Adjustment for the shortfall (excess) in external budget support			31.5				
Adjustment for exchange rate depreciation (appreciation)			17.6				
Gross foreign exchange reserves of the central bank, US$ millions (floor)	336.4	-8.7	-24.3	-23.2	Met	-11.8	0.0
Unadjusted target (floor)			-8.7				
Adjustment for the shortfall (excess) in external budget support 3/			-7.9				
Adjustment for the shortfall in the US$ value of IMF disbursement			-7.2				
Adjustment for the increase (decrease) in BSL short-term foreign currency liabilities			-0.4				
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) 3/	…	0.0		0.0	Met	0.0	0.0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) 3/	0.0	0.0		0.0	Met	0.0	0.0
External payment arrears of the public sector (ceiling) 3/	…	0.0		…		0.0	0.0
Indicative target							
Total domestic government revenue (floor)	…	432.8		438.1	Met	676.8	987.9
Poverty-related expenditures (floor)	…	252.2		294.5	Met	337.9	417.0
Memorandum items:							
External budgetary assistance (US$ million) 4/	…	29.6		21.7		52.1	77.8
Net credit to government by nonbank sector 5/	…	44.0		26.7		45.4	18.4
ECF disbursements (SDR millions)		11.4		7.0		11.4	15.9
Exchange rate (Leones/US$)	…	3,990		3,906		3,990	3,990

1/ The performance criteria and indicative targets are defined in the Technical Memorandum of Understanding (TMU).
2/ Indicative targets.
3/ These apply on a continuous basis.
4/ Including grants and loans.
5/ Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the nonfinancial private sector.

Table 2. Sierra Leone: Structural Benchmarks for 2010

Measures	Timing	Macro Rationale	Status
• Adopt a domestic fuel pricing formula that reflects full pass-through of international oil prices.	End– June	To enhance transparency and eliminate risks for the budget in case of external shocks.	Met with delay. Implemented in October 2010.
• Adoption by the BSL of new off-site surveillance guidelines for banks.	End– June	To enhance the supervisory role of the BSL for financial sector development.	Met with delay. Implemented in November 2010.
• Establish a Domestic Tax Department (DTD) as the vehicle for achieving integration of domestic tax collection and make it functional, including recruiting Commissioner and Deputy Commissioner.	End-September	To improve efficiency of revenue collection efforts.	Not met. Following interviews held in October 2010, the NRA Board has appointed a Commissioner and a Deputy Commissioner for the Domestic Tax Department.
• Submit to parliament amendments of the Government Budgeting and Accountability Act (2005) and Financial Management Regulation to ensure that only viable capital projects enter into the budget.	End–September	To improve efficiency of public investments and achieve the program growth targets.	Met with delay. Implemented in October 2010.
• Establish reverse repo rate as the benchmark interest rate and announce the rate after every Monetary Policy Committee meeting.	Continuous from end-September	To increase the effectiveness of monetary policy and help develop a yield curve.	Not met. Expected to be met in November 2010.
• Establish a credit reference bureau.	End-December	To improve informational infrastructural and promote credit access for credit-worthy customers.	The Credit Reference Bill was gazette on September 9, 2010. This bill has been sent to parliament and a pre-legislative hearing is scheduled for the third week in November.
• Integrate the Goods and Services Tax (GST) administration within the Large Taxpayer Office (LTO).	End-December	To ensure full and efficient implementation of the GST to achieve domestic revenue target.	An action plan has been developed and sent to the Board. NRA Management intends to execute the establishment of the LTD and to integrate the GST administration within the same framework but at different dates of end September and end December, respectively. The next step is to seek approval by the NRA Board.

Table 3. Sierra Leone: Quantitative Performance Criteria and Indicative Targets for 2011 1/

(Cumulative change from beginning of calendar year to end of month indicated; Le billions, unless otherwise indicated)

	Dec. 2010	2011			
	Stock	*Mar. 2/*	*Jun.*	*Sept. 2/*	*Dec.*
Performance criteria					
Net domestic bank credit to the central government (ceiling)	897.6	64.6	106.6	137.6	152.1
Net domestic assets of the central bank (ceiling)	-207.5	63.7	112.8	146.6	159.5
Gross foreign exchange reserves of the central bank, US$ millions (floor)	336.4	-22.7	-14.8	-24.7	-9.9
Contracting or guaranteeing of new nonconcessional external debt by the public sector with maturities of one year or more (ceiling) 3/	…	0.0	0.0	0.0	0.0
Outstanding stock of external debt owed or guaranteed by the public sector with maturities of less than one year (ceiling) 3/	…	0.0	0.0	0.0	0.0
External payment arrears of the public sector (ceiling) 3/	…	0.0	0.0	0.0	0.0
Indicative target					
Total domestic government revenue (floor)	…	260.0	549.7	831.8	1,156.6
Poverty-related expenditures (floor)	…	134.6	271.0	382.5	514.2
Memorandum items:					
External budgetary assistance (US$ million) 4/	…	16.7	31.3	42.5	53.5
Net credit to government by nonbank sector 5/	…	12.4	18.2	25.9	43.2
ECF disbursements (SDR millions)			4.4	4.4	8.9
Program exchange rate (Leones/US$)	3,990	3,990	3,990	3,990	3,990

1/ The performance criteria and indicative targets are defined in the Technical Memorandum of Understanding (TMU).
2/ Indicative targets.
3/ These apply on a continuous basis.
4/ Including grants and loans.
5/ Comprises treasury bills purchased by the National Social Security and Insurance Trust (NASSIT) and the non financial private sector.

Table 4. Sierra Leone: Proposed Structural Benchmarks for 2011

Measures	Timing	Macro Rationale
• Submit amendments to the BSL and Banking Acts.	End–June	To increase operational independence of the BSL and improve regulation and supervision of the financial sector.
• Develop and start implementing a pay reform for public servants.	End-June	To improve the quality of civil services by providing competitive wages.
• Transfer all eligible taxpayers to the Medium Taxpayer Office (MTO) and integrate GST administration with MTO.	End-September	To improve efficiency of revenue collection efforts.
• Implement new small taxpayer regime.	End–December	To improve voluntary compliance and raise tax revenue.
• Strengthen the medium-term expenditure framework by completing a three-year public investment plan, fully integrated with the budget process, to be submitted with 2012 budget.	End-December	To improve efficiency of public investments and achieve medium-term growth targets

ATTACHMENT II. SIERRA LEONE: TECHNICAL MEMORANDUM OF UNDERSTANDING

November 17, 2010

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 performance criteria (PCs) and structural benchmarks (SBs) for the program supported by the Extended Credit facility (ECF) 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 3 of the Memorandum of Economic and Financial Policies (MEFP).

2. **Program exchange rates.** For the purpose of the program, foreign currency denominated values in 2010 and 2011 will be converted from their U.S. dollar denominated value into Sierra Leonean currency (leones) using a program exchange rate of Le 3,990/US$.

II. QUANTITATIVE PERFORMANCE CRITERIA

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

3. **Definition**. Unless otherwise noted, 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* (5th 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.

Adjustment clauses

4. The floor on the change in gross foreign exchange reserves will be adjusted (a) downward (upward) by the amount in U.S. dollars of the shortfall (excess) in programmed external budgetary assistance[1]—the downward adjustment will be capped at the equivalent of US$20 million; (b) downward (upward) for any shortfall (excess) in the U.S. dollar value of disbursements from the IMF under the ECF arrangement; and (c) upward (downward) for any increase (decrease) in BSL short-term (one year or less in original maturity) foreign currency-denominated liabilities (to residents and nonresidents).

[1] External budgetary assistance is defined as program grants and program loans, excluding HIPC assistance.

B. Net Domestic Assets of the BSL

5. **Definition.** Net domestic assets (NDA) of the BSL are defined as the end-period stock of the reserve money less the end-period stock of net foreign assets calculated at the program exchange rates. Reserve money includes currency issued (equal to currency outside banks plus cash in vaults), deposits of commercial banks with the BSL and the BSL liabilities to other private sector. Net foreign assets of the BSL are defined as gross foreign exchange reserves (defined above) minus foreign liabilities. Foreign liabilities are defined as foreign currency-denominated liabilities of the BSL to nonresidents and the outstanding use of Fund credit. For program purposes, foreign liabilities exclude SDR allocation.

6. **Adjustment clauses.** The ceiling on changes in NDA of the BSL will be adjusted upward (downward) by the leone value of the shortfall (excess) in the external budgetary assistance at the test dates—the upward adjustment will be capped at the equivalent of US$20 million.

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 as calculated by the BSL. It is defined as follows:

- the net position of the government with commercial banks, including: (a) treasury bills; (b) treasury bearer bonds; and (c) loan and advances of commercial banks to the government; less government deposits in commercial banks;

- the net position of the government with the BSL, including: (a) treasury bills; (b) treasury bearer bonds, excluding holdings of special bonds provided by government to cover the BSL losses; (c) the stock of non-interest bearing non-marketable securities (NIBNMS); (d) the difference between converted NIBNMS into treasury bills and proceeds from their sales; and (e) ways and means; less (a) central government deposits; and (b) HIPC and MDRI relief deposits.

8. **Adjustment clauses.** The ceiling on changes in NCG will be adjusted (a) upward (downward) by up to the leone value of the shortfall (excess) in external budgetary assistance—the upward adjustment will be capped at the equivalent of US$20 million; (b) 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 assumption (as specified in the memorandum items in Table 3 of the MEFP).

9. **Data source**. The data source for the above will be the series "Claims on government (net)", submitted to the IMF staff and reconciled with the monthly monetary survey prepared by the BSL.

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. External Payment Arrears of the Public Sector

11. **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.

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

12. **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 (see paragraph 11 for definition of public sector) based on the residency criterion. This PC applies not only to debt as defined in the Guidelines on Performance Criteria with Respect to Foreign Debt (Decision No. 12274 (00/85), August 24, 2000, Point 9, as revised on August 31, 2009, (Decision No. 14416-(09/91)) 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 ¶11 above. This PC will apply on a continuous basis.

13. Any external debt of which the net present value, calculated with the reference interest rates mentioned hereafter, is greater than 65 percent of the nominal value (grant element of less than 35 percent) is considered nonconcessional, with the exception of IMF lending. For debt with a maturity of more than 15 years, the average of the ten-year commercial interest reference rates (CIRRs) published by the OECD is used to calculate the grant element. The average of the six-month CIRRs is used for debt with shorter maturities. For loans in foreign currencies for which the OECD does not calculate a CIRR, calculation of the grant element should be based on the CIRR in SDRs. The Government will report any new external borrowing and its terms to Fund staff as soon as external debt is contracted or guaranteed by the government.

F. External Short-Term Debt Contracted or Guaranteed by the Public Sector

14. **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 (see paragraph 11 for definition of 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 in ¶11 above. This PC will apply on a continuous basis.

III. Quantitative Indicative target

A. Domestic Revenue of Central Government

15. **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.

B. Poverty-Related Expenditures

16. **Definition**. Poverty-related expenditures refer to those expenditures in the areas identified in Table 2 of the Sierra Leone HIPC Decision Point Document.

IV. Program Monitoring

17. The Sierra Leonean authorities shall maintain a program-monitoring committee composed of senior officials from the MoFED, the BSL, and other relevant agencies. The committee shall be responsible for monitoring performance under the program, recommending policy responses, informing the IMF regularly about the progress of the program, and transmitting the supporting materials necessary for the evaluation of PCs and benchmarks. The committee will provide monthly reports to the IMF on progress in implementing the program's quantitative targets and structural benchmarks.

ANNEX 1: 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 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 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 bases	Monthly	End of month + 6 weeks
	Petroleum product prices and 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 BSL	Monthly	End of month + 6 weeks
	Consolidated balance sheets of commercial banks	Monthly	End of month + 6 weeks
	BSL monitoring sheet of net financing of the financial sector to the government	Monthly	End of month + 6 weeks
	BSL monitoring sheet of treasury bills and bonds holdings	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

Sierra Leone: Summary of Data to be Reported to IMF Staff (concluded)

Type of Data	Tables	Frequency	Reporting Deadline
Monetary and financial data			
	Gross official foreign reserves	Weekly	End of week + 1 week
	Foreign exchange cashflow table	Monthly	End of quarter + 4 weeks
	Revised balance of payments data	Monthly	When revisions occur
	Exports and imports of goods (including the 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, including the associated concessionality calculation (percentage) for each new loan.	Monthly	End of month + 4 weeks
	External debt service payments (separately on principal and interest payment) to each creditor, including and excluding new disbursements in the debt recording system. Also, including and excluding HIPC relief.	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 Monetary Policy Committee	Monthly	Date of meeting + 2 weeks