Strengthening Public Investment Management in Lebanon

2023

Acknowledgments

This report was prepared by the Institut des Finances Basil Fuleihan and Insights Analytica sarl.

The work was mandated by the Ministry of Finance. It was supervised by Ms. Lamia Moubayed Bissat, President of the Institut des Finances Basil Fuleihan, and led by Ms. Sabine Hatem, Senior economist and Director of Cooperation and Partnerships at the Institute with substantive contributions by Mr. Iskandar Boustany, Public Financial Management expert, Judge Faysal Makki, Legal expert and Ms. Tonia Salameh, Economist and Data Specialist.

Analysis and findings draw from prior assessments of Public Finance Management and Public Investment Management in Lebanon, available fiscal data and international benchmarks and practices.

The report was reviewed and enhanced by Mr. David Bernstein, Lead Public Sector Specialist at the World Bank, Ms. Rima Koteiche, Senior Governance Specialist, Mr. Ousmane Maurice Megnan Kolie, Senior Public Sector Specialist, and Ms. Fabienne Mroczka, Senior Public Financial Management Specialist.

The Arabic language version of the related policy brief was edited by Ms. Josiane Chebli. The design and layout were done thanks to Ms. Jide Begdache Bacha.

The report was prepared under the World Bank's Implementing 3RF Governance Activities Project. The Institute of Finance and Insights Analytica team are grateful to the Lebanon Financing Facility (LFF) for financing this foundational work.

The Lebanon Financing Facility (LFF) is a multi-donor trust fund administered by the World Bank to kickstart the immediate socio-economic recovery of vulnerable populations and businesses affected by the Port of Beirut explosion of August 2020 and to support the Government of Lebanon catalyze reforms and prepare for medium-term recovery and reconstruction. The LFF is kindly supported by Canada, Denmark, the European Union, France, Germany and Norway.

Disclaimer

ISBN 978-9953-9043-6-8

Table of Contents

Table of Figures

Rationale and objectives of the report

Since 2019, Lebanon has been facing one of the most severe top three crisis episodes of its recent history (World Bank , Spring 2021); a crisis qualified as a man-made catastrophe **resulting from failed government policies** (UN, 2022).

Economic contraction is estimated to have reached 28% in 2020 (Ministry of Finance, 2022), while inflation soared at an average rate of 155% in 2021 (Central Administration of Statistics, 2022). Living conditions have deteriorated dramatically, leading to a large increase in poverty and multidimensional poverty that reached 82% of the Lebanese population (ESCWA, 2021), and in unemployment and emigration. The fallout of the combined crisis and accumulated deficiencies in managing the prior crisis, among which the hosting of more than 1.5 million refugees, have strained public infrastructure to a breaking point and led to large disruptions to vital public services, such as extended electricity blackouts, water shortages, internet cuts, and others.

On April 7th, 2022, the Lebanese authorities reached a Staff-Level Agreement (SLA) with the IMF, including a set of comprehensive economic policies supported by a 4-year USD 3 billion loan facility. The SLA foresees to:

- Backstop the recession, restore macroeconomic stability and spur economic growth;
- Consolidate public finances along debt sustainability objectives while enhancing social safety nets and rehabilitating infrastructure;
- Ensure fair and equitable burden sharing of financial sector losses;
- Allow the banking sector to resume its activity of extending credit to the private sector;
- Re-focus monetary policy;
- Mend the social fabric torn by rising levels of poverty and growing income disparities;
- Improve public sector institutional governance, transparency, and accountability.

The agreement will be subject to approval by the IMF management once a set of Prior Actions are timely implemented by the Government of Lebanon.

In parallel, the Government of Lebanon finalized and submitted to Parliament in May 2022 a Financial Recovery Strategy and Memorandum of Economic and Fiscal Policies that includes fiscal adjustment measures and tackles in particular Public Investment Management under Article 8 (Council of Ministers, 2022).

Prior to that, and in the aftermath of the Port of Beirut explosion, the WB, EU and UNDP had enacted the Lebanon Reform, Recovery and Reconstruction Framework (3RF) to bridge the immediate humanitarian response and the medium-term recovery and reconstruction efforts following the Beirut Port Explosion in August 2020 and put Lebanon on a path of sustainable development. The 3RF includes the reconstruction of critical assets, services, and infrastructure to provide equal access to quality basic services and enable sustainable economic recovery. It also foresees the implementation of reform to support reconstruction and to help restore people's trust in governmental institutions by improving governance. It relies on policy measures investments, and institutional strengthening to address the urgent needs of the most vulnerable populations and small businesses and focuses as well on critical reforms that address governance and recovery challenges including the reconstruction of critical assets, services, and infrastructure and the unlocking new sources of public and private finance.

The revamping of capital spending or what can be referred to as Public Investment is a key reform measure foreseen by the Government of Lebanon and the donor community to rehabilitate failing infrastructure and improve its efficiency, rationalize expenditures, restore the country's competitiveness, and enhance the business climate to attract new investments, in support of growth and stability. It is also a key pillar of inclusiveness that would allow to restore an acceptable level of access to public services to all citizens.

To address identified weaknesses and shortcomings, the donor community is requesting an effective PIM system to be ready for when reconstruction and investment opportunities arise, in ways that would support and promote the effective and efficient use of scarce financing resources. Building an effective PIM System is seen as a multi-year task that would require coordinated efforts across a multitude of institutions and stakeholders.

The current project seeks to analyze the existing options for the formalization of a PIM legal and regulatory framework that would improve efficiency and effectiveness in the use of recovery and reconstruction funding and to propose:

1. A clear mandate and role for a PIM unit or institutional arrangement to supervise the implementation of a PIM action plan including its location, reporting lines, key functions, financial and human resources needs, and relationship with external stakeholders.
2. An updated action plan among stakeholders to promote ownership and implementation.

A first inception report presented a brief assessment of the current governance framework and weaknesses, a review of the legal framework and a mapping of the various actors and/or existing PIM units/functions under line ministries and institutions, their respective roles and mandates.

The present report provides a quick summary of the main shortcomings of Public Investment Management in Lebanon further analyzed in the first inception report. It identifies best practices, country experiences and guidelines that can inform the design of a solution relevant to the Lebanese context before proposing two possible scenarios for the institutionalization of a PIM function and related requirements for success. Finally, it sheds the light on needed enhancements at the level of the various stakeholders directly involved in PIM.

What is Public Investment and why does it matter?

Public investment broadly refers to public capital expenditure for the acquisition, maintenance or improvement of fixed assets (box 1). Such fixed assets are funded through the State budget, through public-private partnerships, or regulated private entities. The largest parts consist of infrastructure projects. These often entail significant up-front costs, have long lead times for both design and implementation, and involve sunk costs including fiscal costs which often carry risks with significant macro-economic implications.

Box 1: There are two main categories of fixed assets.

Tangible assets include:

- Buildings and structures, including all amounts payable for site clearance and preparation and the cost of all fixtures, facilities, and equipment that are integral parts of buildings and structures.
- Machinery and equipment (when separate from buildings and structures).
- Weapons systems (*Some countries exclude weapons systems from PIM for security issues*).

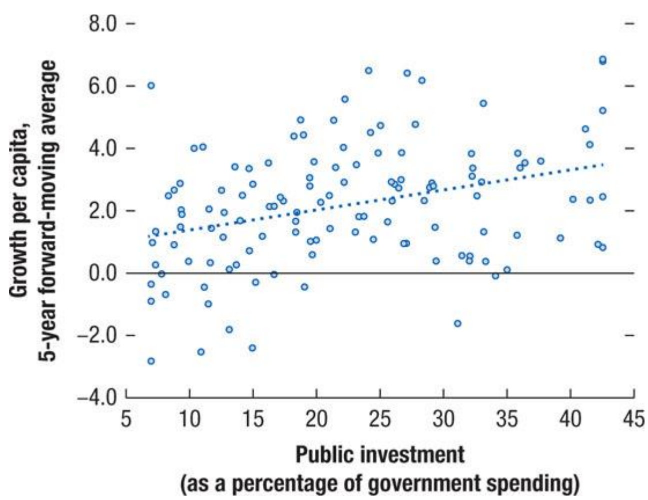
Intangible assets are:

- Intellectual property products, such as research and development, academic fundamental research, applied research and R&D grants and contracts to private sectors, computer software and databases, etc.

__Source__: IMF, 2014, Government finance statistics manual 2014, URL: https://www.imf.org/external/pubs/ft/gfs/manual/2014/gfsfinal.pdf and European Commission, 2013, URL: https://economy-finance.ec.europa.eu/system/files/2022-10/dp154_en.pdf

A higher share of public investment in government spending is associated with stronger growth (figure 1). When they are well-planned, well-implemented, and sustainable, such investments are key drivers of inclusive economic growth and the reduction of inequalities (IMF, 2020). Public investment also encourages new private investment. Nonetheless, despite strong evidence, it is observed that capital spending is often cut down in times of crisis or fiscal consolidation.

Figure 1: Public Investment and Growth



Source: IMF Capital Stock Data Set; and International Financial Statistics.

Public Investment Management (PIM) relates to the ways governments public investments are managed, i.e. how governments plan, select, construct and maintain their fixed assets. A weak PIM often leads to projects that are poorly designed, have large costs overruns, experience long delays in construction, and/or yield poor social dividends. Moreover, public investment projects, particularly in infrastructure, are prone to corruption, the direct costs of which include loss of public funds through misallocations or higher expenses and lower quality (IMF, 2020). IMF research estimates at 30% the average global efficiency gap between money spent and the coverage and quality of resulting infrastructure. This ratio could reach 53% in low-income countries (IMF, 2020)

Historically, PIM approaches concentrated public investment into the hands of a separate ministry of planning. This approach proved to have many weaknesses including i) the tendency to become disconnected from fiscal constraints; ii) a mismatch between required funding in the plan and budgetary allocation; iii) procyclical spending; iv) dual budgeting in which investment spending is handled separately from the rest of the budget; v) ineffective sequencing and prioritization of projects; vi) and inadequate planning, design, and monitoring of projects (box 2).

Box 2: The experience of Ministries of Planning

Large Ministries of Planning were established across the world, notably in MENA countries (Jordan, Egypt, Palestine, Iraq, etc.) and across Africa, with the mission to spur infrastructure planning and construction, economic transformation and growth or even large and long-term sustainable development strategies and plans.

Although some experience has been successful, many other countries have opted against founding such large and standalone ministries, and instead preferred either merging this function with that of an existing ministry (e.g. Finance or Economy) or creating independent councils and units for Planning and Public Investment.

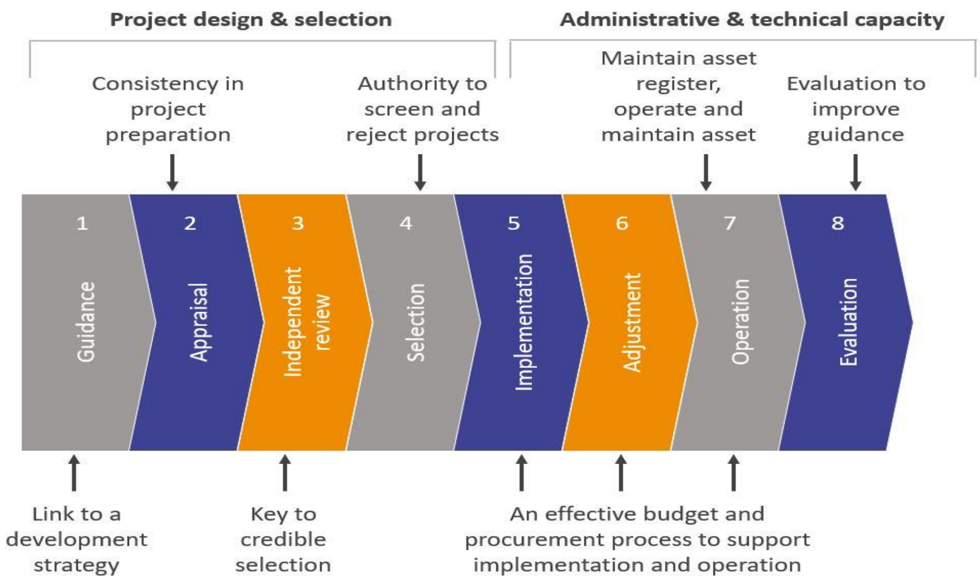
This indicates that while the function of planning in and of itself is an important necessity, delegating it in the form of a ministry is not. Constant changes in government leadership and lack of a common vision for a country's future impede successful strategic planning, putting it at the mercy of electoral cycles and deadlines and therefore jeopardizing multi-year planning and the set-up of national priorities (Couto&Gomide, 2022). It leads to (i) poor coordination between capital expenditure decisions and their recurrent consequences, usually seen in an under provision of the operational budget of new facilities, and (ii) failure to consider trade-offs between capital and current expenditures, often to the detriment of current spending and frequently resulting in the suboptimal maintenance of capital stock.

Another approach consisted of entrusting investment management to line ministries and making them responsible for harmonizing their investment and recurrent spending. This scenario also carried challenges. Budgets by line ministries tended to be overoptimistic and disconnected from fiscal constraints. Ministries failed to evaluate accurately operating costs and procyclical spending. Dual budgeting, a practice according to which investment spending is handled separately from the rest of the budget, created large fiscal risks. Other shortcomings included ineffective sequencing and prioritization of projects, and inadequate planning, design, and monitoring of projects (Cangiano, Curristine, & Lazare, 2013).

Consequently, many countries opted for arrangements that are both fiscally realistic and effectively integrated into the annual budget process; arrangements that combine effective

medium-term budgetary frameworks and the independent reviews of project appraisals (figure 2). Modern PIM frameworks thus favored a clear designation of roles and responsibilities for project implementation as well as legal clarity with respect to standardized rules for project adjustment and procurement. This led many countries to opt for either merging the PIM function into the existing ministry in charge of budgeting (e.g. Finance, Budget or Economy) or creating independent councils/units for Planning and Public Investment and endowed them with technical and financial resources including skilled workforce, analytical tools, specific regulations, etc.

Figure 2: Key features of a Modern Public Investment Management System

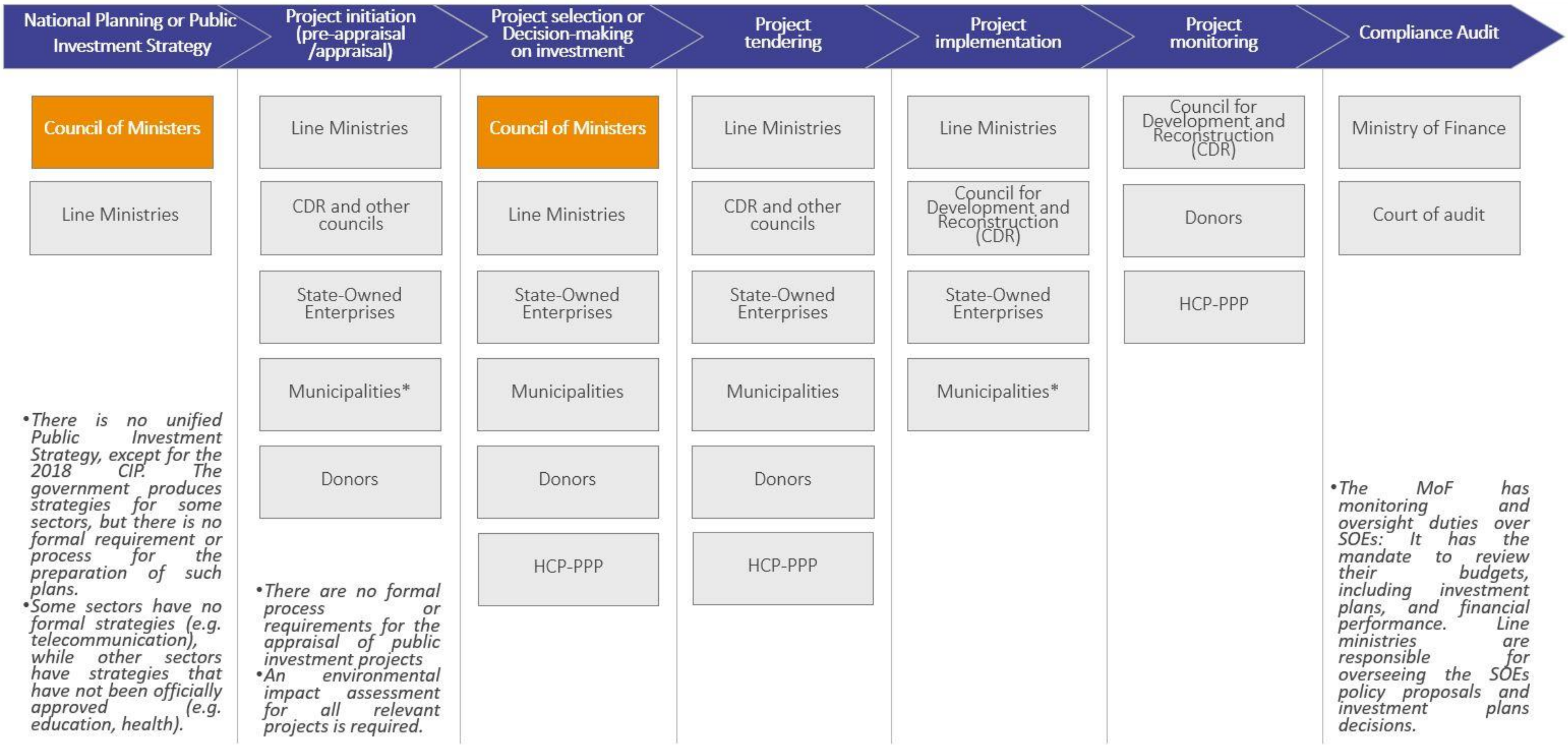


Source: Rajaram, Anand, Tuan Minh Le, Kai Kaiser, Jay-Hyung Kim, and Jonas Frank, Editors, (2014), The Power of Public Investment Management: Transforming Resources into Assets for Growth, The World Bank (adapted)

Where does Lebanon stand?

Public investment management in Lebanon is fragmented between several institutions (figure 3). The process initiates at the levels of the line ministries or public institutions, but also within municipalities, independent extra-budgetary funds and public corporations, with little coordination at central government level to steer sectoral trade-offs and meet resources constraints, often leading to the duplication of infrastructure projects. Often, prerogatives related to project selection, implementation and monitoring overlap, while coordination mechanisms are weak across government. There is no systematic approach to project appraisal and selection. Monitoring and oversight by the Court of Accounts are limited in scope and efficiency (IMF, 2018).

Figure 3: A schematization of Lebanon's Public Investment Management process

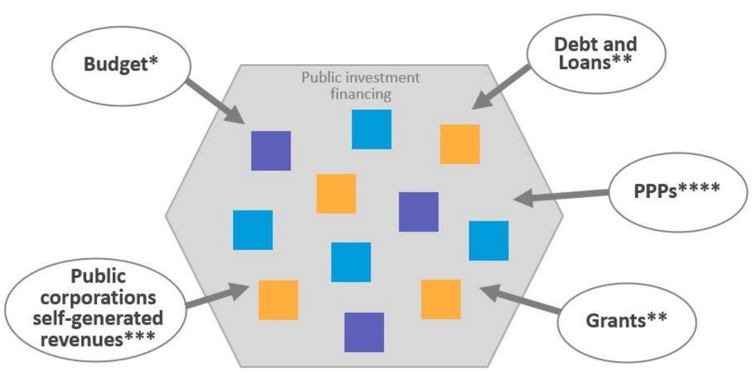


Financing is also scattered across various sources and not all PI projects are channeled through the budget (figure 4). A large share of donor financed projects are not included in the annual budget as well as the capital spending of State-Owned Enterprises and public institutions. Therefore, the Ministry of Finance does not have at hand a comprehensive overview of the volume and financing of PI. For instance, no data on the number and amount of capital spending projects implemented by SOEs, public institutions and extra-budgetary funds is shared with the MoF. This largely undermines fiscal management and create sizable fiscal risks on the budget and hampers the strategic role of the Ministry of Finance as the custodian of fiscal management and of the Parliament in charge of financial oversight.

Public investment conducted by public corporations is difficult to evaluate. Despite its mandate to exercise financial oversight over these entities by reviewing their budgets, investment plans, and financial reports, the Ministry of Finance does not receive the necessary financial data. Furthermore, line ministries that are in charge of overseeing investment plans and decisions do not carry out their supervisory responsibilities in a systematic manner.

In addition, and since the information on the government's asset stock is either incomplete or out of date, the MoF is unable to put in place an efficient asset management policy and ultimately improve revenue collection. Therefore, PIM reform should be coupled with a central strategic policy framework for the overall management of state assets and the creation of a centralized registry for accurate, complete, reliable, and detailed record keeping.

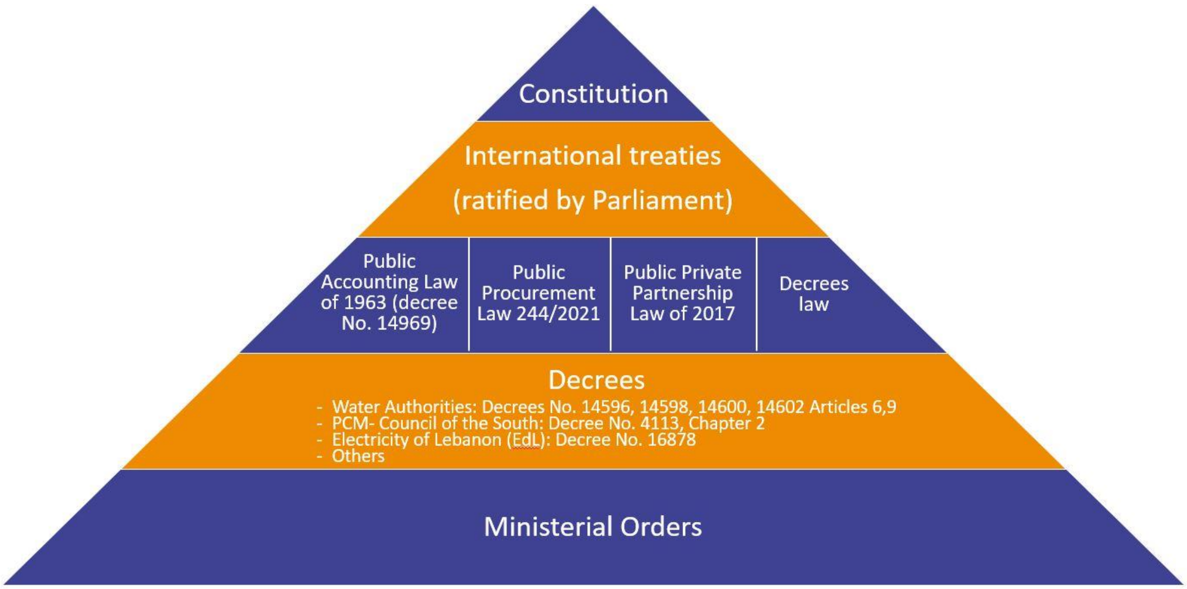
Figure 4: Financing of Public Investment projects[1]



1 *On budget capital spending was estimated in 2018 to reach 60% and to be mostly dedicated to economic infrastructure (IMF, 2018).
**In 2016, 20% of the central government capital projects were foreign financed through loans and/or grants. They were not informed in the budget and mainly executed by the CDR (IMF, 2018).
*** The total amount investment made by public corporations/SOEs from their own revenues and by municipalities remains unknown as there is no consolidated information available.
**** In 2017, PPP contracts represented 20% of capital expenditures.

Regulations are also sourced in a variety of legal texts, from laws to internal regulations, that are seldom aligned (figure 5). There is no single or unified PIM legislation. Regulations and practices in place are weak and only partly aligned with good practices (figure 5). Strategic planning was weak and only recently rendered mandatory with the entry into force in August 2022 of the Public Procurement Law 244/2021 that compels all spending entities to submit their annual procurement plan (including works) to the Public Procurement Authority (article 11).

Figure 5: The legal framework for Public Investment Management (based on the Kelsen pyramid)

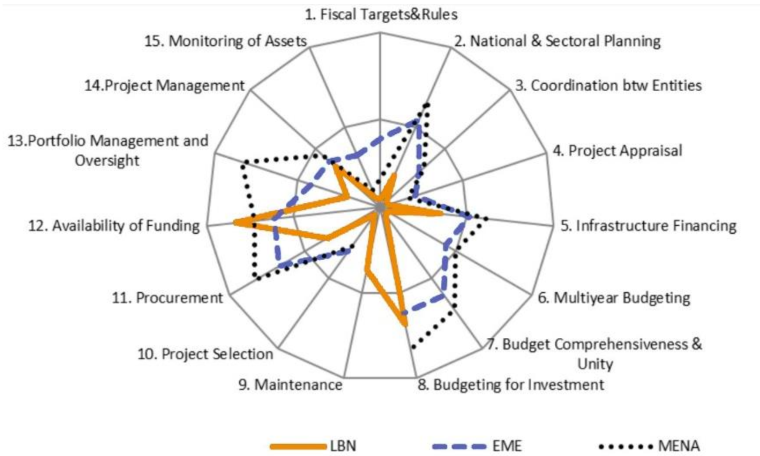


The proper oversight process of regulators over public institutions and their activities, notably on public investment, is hampered as sector-specific regulatory authorities are:

- Either mentioned by law but not established (electricity, aviation)
- Or established and not functional (Telecommunication Regulatory Authority)
- Or functional and not effective (petroleum)

Most of them are asked to report to a minister which jeopardizes their independency.

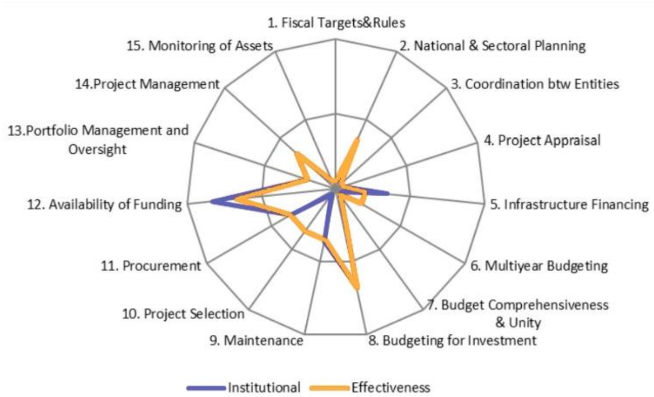
Figure 6: PIM Institutional design in Lebanon v/s MENA and emerging markets



Source: IMF, 2018, Lebanon Public Investment Management Assessment

This fragmentation is weakening the overall PIM institutional capacity notably for functions of Fiscal discipline, Coordination between entities, Project Appraisal, Budget comprehensiveness and unity and the Monitoring of assets in which Lebanon scores zero; and for functions of National and Sectoral Planning and Project management in which performance is weak (figure 6), that were all pinpointed as high priority areas of reform by the IMF PIMA in 2018 (box 3).

Figure 7: Lebanon – Comparing Institutional design v/s Effectiveness



Source: IMF, 2018, Lebanon Public Investment Management Assessment

Box 3: Public Investment Management Assessment (PIMA)

PIMA is a comprehensive framework designed by the IMF to assess infrastructure governance practices for countries at all levels of economic development. Specifically, PIMA evaluates 15 institutions involved in the three key stages of the public investment cycle:

- ✓ Planning of sustainable investment across the public sector;
- ✓ Allocation of investment to the right sectors and projects;
- ✓ Implementation of investments projects to deliver productive and durable public assets.

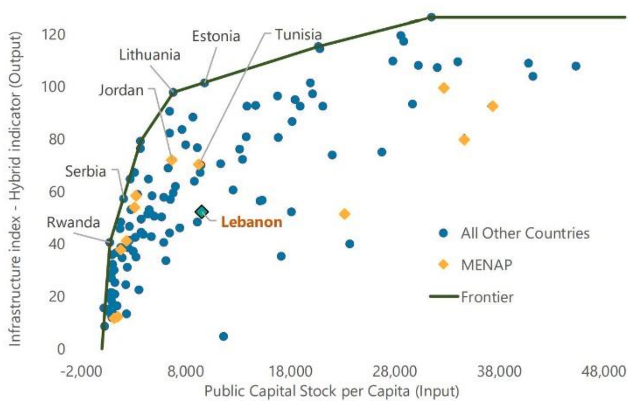
Each institution is assessed on both institutional strength (organization, policies, rules and procedures on paper) and effectiveness (degree to which the intended purpose is being achieved in practice or there is a clear useful impact).

PIMA also covers a qualitative assessment of three cross-cutting factors that often impact the overall effectiveness of public investment management: (1) the legal and regulatory framework, (2) staff capacity, and (3) IT systems.

Source: https://infrastructuregovern.imf.org/content/PIMA/Home/PimaTool/What-is-PIMA.html

As well, it is undermining the effectiveness and quality of public investment and leading to an efficiency gap estimated at 43%, twice less than in other countries with a similar level of public capital per capita (figure 8) (IMF, 2018). The level of public investment remains persistently low, standing at less than 2% of GDP per year – much lesser than peer countries (6%). The same applies to the overall low stock of public capital, that reached 38% of GDP (2015) – one of the lowest among peers - and is rapidly deteriorating (IMF, 2018).

Figure 8: Efficiency frontier



Source: IMF, 2018, Lebanon Public Investment Management Assessment

The lack of consolidated processes and information on public investment is creating indirect costs with long term repercussions on fiscal discipline. The absence of a strong central regulation framework and of systematic appraisal and monitoring processes are increasing undetected fiscal risks with the creation of both explicit and implicit contingent liabilities[2] that may on the long term

[2] Explicit contingent liabilities are Government liabilities as recognized by a law or contract. Implicit contingent liabilities are moral obligations of government that reflect public and interest-group pressures. They can take the

further impair the government's fiscal adjustment plan and macroeconomic forecasts on debt, revenue, and spending. It also impairs competitiveness and therefore value for money.

Weak enforcement of existing regulations and oversight have been conducive to corruption, the cost of which is estimated to have reached, according to the UNDP, USD 5 billion a year (UNDP, 2020), due to misallocation of public funds and limited returns on investments, in addition to losses in economic opportunities related to capital flight and the reluctance of potential investors. Bid-rigging, collusion and market sharing mechanisms have dominated infrastructure contracts with politically connected firms capturing the majority of investment projects as of 2008.

Public investment has also a critical role to play in Lebanon's recovery prospects. IMF research shows that increasing public investment by 1% of GDP in emerging market economies could help revive economic activity from the sharpest and deepest global economic collapse and boost GDP by 2.7%, private investment by 10%, and employment by 1.2% (IMF, 2020).

Finally, with the deterioration of current infrastructure assets, lack of maintenance and absence of a proper asset monitoring and management strategy, risk are looming of seeing development outcomes reversed.

The economic and social costs incurred by the fragmentation and weaknesses of public investment management processes, the absence of the proper safeguards and the deterioration of existing infrastructure, are all putting forth the urgency to revamp public investment management in Lebanon.

Where do we go from here? The need for a consolidated Policy Framework for PIM

International practice and standards conclude to a set of recommendations around the need for institutional set-up and functions of a proper public investment management system. These guidelines are summarized below and in appendix 1, and recommendations drawn to inform the rationale behind the establishment of such a function in the Lebanese public sector panorama.

Seven reasons why Public Investment needs a well-established management system

1. **Public investments are multi-year projects with long planning and implementation phases** that are difficult to synchronize with the budget cycle. Special arrangements help address these shortcomings.
2. **They are large and costly projects, often irreversible.** Any mistake or delay can be very costly on governments. Risk management is therefore a core component of PIM.

form of unaccounted for future recurrent costs of public investments or in the event of municipalities or public entities' default on nonguaranteed debt and other obligations arising from contracts they have committed to but not included in the budget.

3. **They entail long forecasting horizons**, that amid existing uncertainty, requires sophisticated skills for assessing and analyzing their long-term costs and benefits and impact on society and the environment.
4. **If they can boost economic growth, they also create important opportunity costs on scarce public resources** which requires a well-established prioritization mechanism.
5. **They are subject to systematic planning errors** and to "excessive optimism" (Atif, Flyvbjerg, Budzier, & Lunn, 2014) that necessitate clear arrangements to strengthen planning and impartial appraisal and reviews.
6. **Given their financial size and complexity, they are highly subject to political interference and corruption** - 57% of corruption cases worldwide are linked directly to procurement transactions (OECD , 2014)- resulting in higher costs than necessary and in the selection of unqualified contractors.
7. **They are the main vehicles for the provision of quality public services.** Corruption or the poor monitoring of project implementation can lead to the delivery of "inefficient" assets that are unable to provide for good quality public services.

Figure 9: Common problems and potential consequences of PIM failings

COMMON PROBLEMS	POTENTIAL CONSEQUENCES
● Development plans disconnected from actual budgets or projects and vise versa ● White elephant projects with little socioeconomic value ● Lack of pipeline of high-quality projects ● Projects awarded to unqualified firms ● Opaque resource-for-infrastructure deals without due safeguards for ensuring good value ● Corruption or delays in procurement ● Delays in land or site acquisition ● Cost escalation, time overruns ● Contract disputes or abandoned projects ● Poor quality of completed projects ● Poor operation and maintenance of completed assets ● Institutional inertia or no systemic response to problems	● Creation of few valuable public assets ● Lack of key public facilities ● Stock of decaying infrastructure: power and water shortages, road and railway accidents, crowded hospitals, deteriorating human development index ● Failure of investment to spark growth and improve social welfare ● Difficulty of countercyclical expansion of investments ● Creation of a liability if investment is financed by debt ● Burden on citizens and private sector if investment is financed by taxes ● Reduction in net wealth if investment is financed by the extraction of finite natural resources ● Macroeconomic instability ● Political instability ● Fiscal pressures and risk

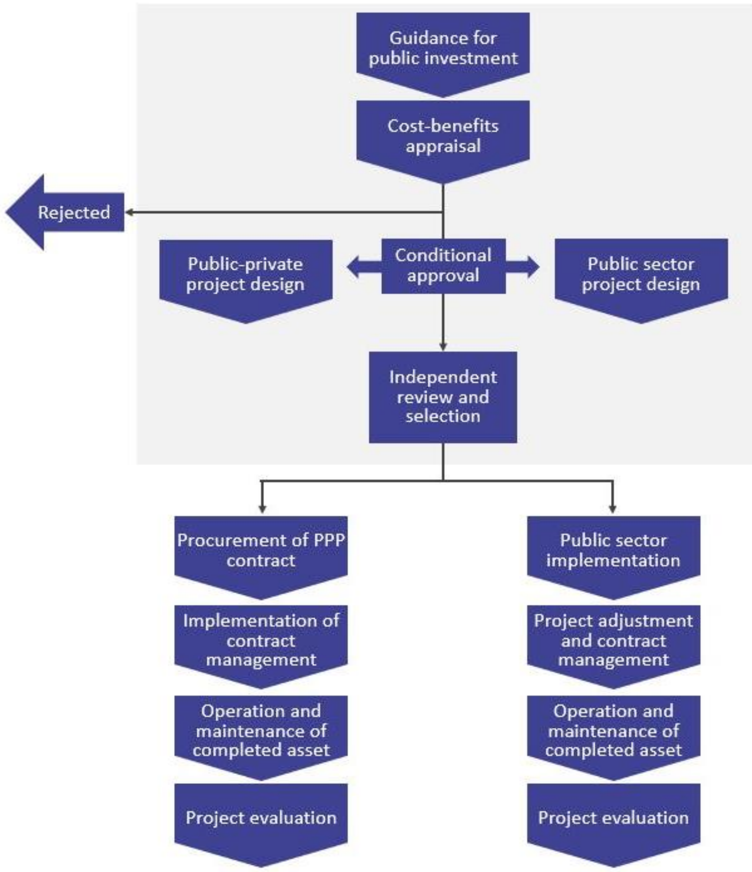
Source: *World Bank (2020), Public Investment Management Reference Guide*

Guiding principles and must-have features of an efficient PIM system

A consolidated PIM framework can help efficiently address usual shortcomings provided it:

1. **Defines systematically each step of PIM.**
2. **Applies to all projects, either financed from the budget, from aid development or in the form of PPP** (figure 10).

Figure 10: A unified framework for decision-making on Public Investment Management projects



Source: Rajaram, Anand, Tuan Minh Le, Kai Kaiser, Jay-Hyung Kim, and Jonas Frank, Editors, (2014), The Power of Public Investment Management: Transforming Resources into Assets for Growth, The World Bank

Eight "must-have" features of a consolidated PIM framework that would help minimize associated risks and are applicable in low-capacity contexts were identified by the World Bank (World Bank, 2020). They provide countries with a systematic approach to creating the institutional capacity to manage investment. Detailed explanation on each feature is provided in Appendix 1. In summary, PIM frameworks should:

1. **Provide for strategic investment guidance, project development and pre-appraisal screening**. In the case of Lebanon, such guidance may be derived from the bailout plan that would be ratified with the IMF, from an updated Capital Investment Program or from a new medium to long term recovery and development vision that would be adopted by the Government. Existing sectoral strategies would provide for more disaggregated and detailed information. Provided guidance may be referenced in the annual budget circular.
2. **Lay down a formal project appraisal process.** The case of Chile in presented in Box 4 as an example.

Box 4: The benefits of systematic appraisal of public investment projects in Chile

Chile's Modern project appraisal for public investment started in 1975, with the establishment of the National System of Investments (SNI) at the Ministry of Planning (MoP), administered jointly with the Ministry of Finance (MoF).

The SNI, with the adoption of transparent cost-benefit analysis for all public investment projects, managed to improve the quality of its public investment, promote economic growth, and maintain fiscal discipline in Chile.

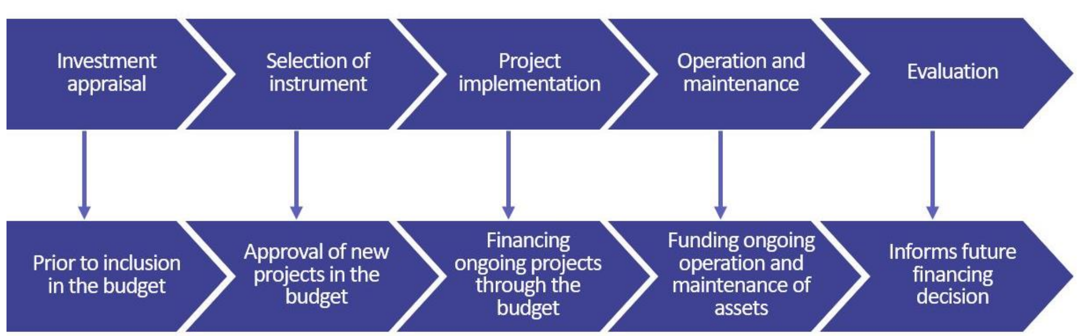
Key investments in the country's basic infrastructure backbone that were essential for economic development and welfare were successfully rolled-out allowing Chile to achieve near-universal access to basic and essential services. Additionally, gross domestic product (GDP) per capita was raised drastically, from USD 4,787 in 1990 to USD 22,197 in 2015.

The unique appraisal process of the Chilean system starts with a 'policy idea' advanced by a government unit that enters it into a data bank of projects (BPI), where it gets assigned an ID. This 'idea' is then developed into a project profile that is subsequently subjected to a pre-assessment study—including an examination of legal and technical issues, as well as a socio-economic analysis. Once the required documentation is put together, the project ID is entered into the SNI. The MoP proceeds with its appraisal which includes a review of legal issues, and of alignment with policy priorities. It consequently issues a positive or a negative recommendation. Upon a positive initial recommendation, a full-fledged Cost-Benefit Analysis is performed, and based on its results, the MoP—also taking into account the MoF's sectoral draft budget envelopes—issues either a positive recommendation or rejects the project.

Sources: (World Bank, 2006); (OECD, 2017)

3. **Secure an independent review of appraisal**.
4. **Make a final decision on project selection and budget using a clear budget process**, even if both processes run along different timetables (figure 11). **This is one of the most critical stages of the investment management cycle and can only be achieved if a strong gatekeeping function is put in place at the Ministry of Finance (boxes 5 and 6).** Such a process is inexistent in Lebanon. Even in the recent PPP law (2017), the Ministry of Finance is not granted the authority to prevent or stop a project if the later creates sizable liabilities on public finances.

Figure 11: Linking the project and annual budget cycle



Source: Overseas Development Institute (2016), Public investment management: A public financial management introductory guide

Box 5: How to put in place a gatekeeping function?

Having a gatekeeping function in place establishes quality-at-entry processes and compliance checks that prevent ineligible projects from being “parachuted” into the budget. It is usually performed by the Budget department at the Ministry of Finance and the latter is provided with the authority to veto or stop PI projects that endanger fiscal sustainability at any stage of the project cycle.

Operating an efficient gatekeeping function would require from the Ministry of Finance to have the capacity to:

- Assess projects’ affordability at the different stages of the project lifecycle.
- Perform analysis on long-term fiscal implications of any PI project.
- Propose decisions to the Minister of Finance to be shared with PI decision-makers.
- Ensure an adequate financing per project.
- Provide a medium-term perspective for fiscal and expenditure planning, notably that related to PI to allow for strategic investment planning, prioritization and decision-making in view of limited resources available through the budget.
- Fix a binding ceiling (or resource envelop) for capital budgeting in the annual budget.
- Facilitate the inclusion of projects in the budget process and allow for multiyear expenditure programming[3].
- Monitor project implementation against related disbursements.
- Assess, monitor and manage fiscal risks arising from the various PI projects;
- Report on the fiscal implications of PI projects.

The absence of this function is a significant shortcoming of a good and efficient PIM system.

Box 6: The case of South Africa in putting in place proper budget safeguards.

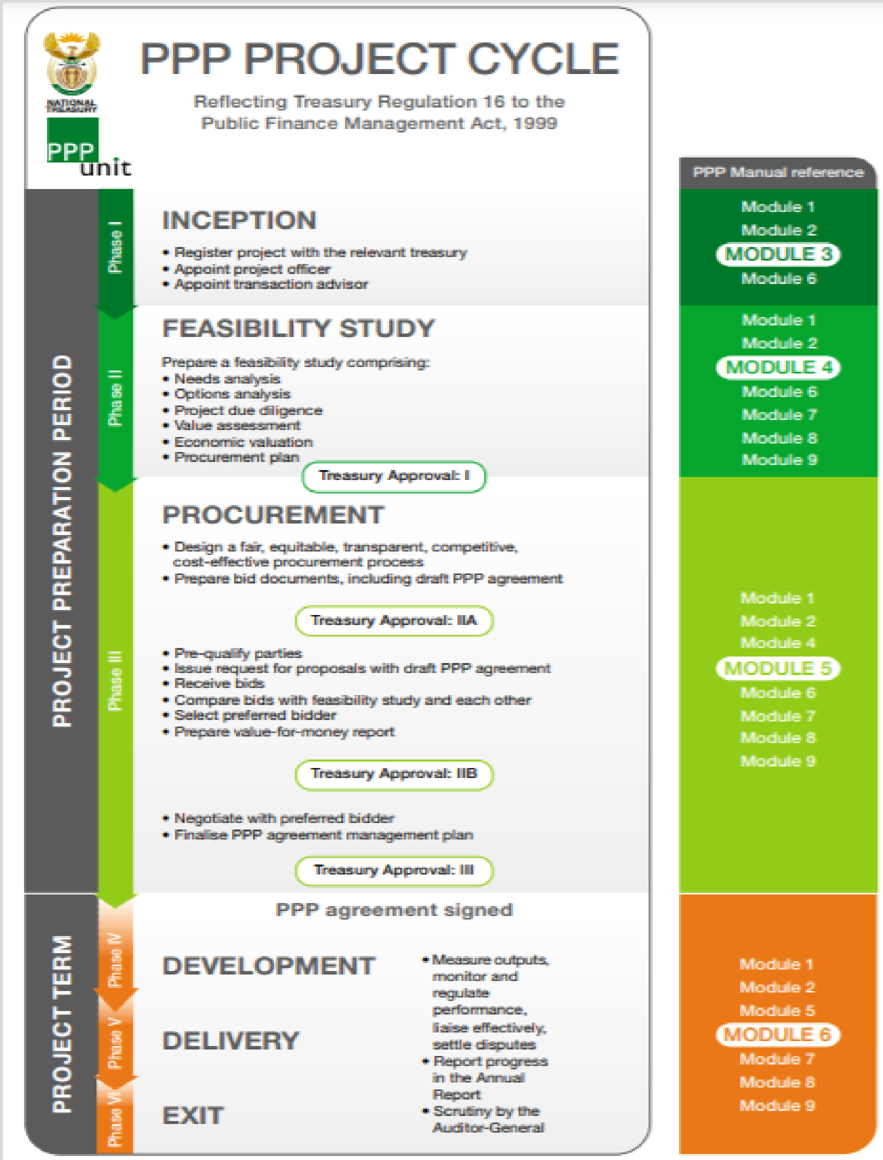
South Africa has put in place a "gateway review process" that examines PI programs and projects at key decision points in their lifecycle.

The gateway process takes the form of a points system through which all PI projects are screened by the National Treasury to provide assurance that they can progress successfully to the next stage, notably:

1. After concluding the feasibility study
2. Once tender documents are completed (including draft PPP contracts)
3. Upon the bidder selection and preparation of a "value-for-money" report
4. Upon the finalization of negotiations with the bidder
5. Upon the finalization of the PPP agreement/contract, and
6. During any renegotiation.

[3] In the absence of medium-term planning, it is essential to prepare forward estimates that capture the implications of ongoing public investment projects for future expenditures and to integrate them later into the related budget.

Moreover, article 16 of the Public Financial Management Law has created a PPP unit within the National Treasury in 2000, with the aim to stop PPP projects that are fiscally unstainable, set clear rules of collaboration and enhance financial surveillance.



Source: Republic of South Africa, 2012, Standard for an Infrastructure Delivery Management System

5. **Strengthen project implementation**. Good project implementation also requires having an accounting system that captures and reports all project costs and allows for the tracking of multi-year budgeting. This is an important shortcoming to be addressed in the case of Lebanon as appropriations are annual.
6. **Create the capacity for project adjustments**.

7. **Make provisions for the sustainable operation of facilities.** Asset valuation is a critical aspect that needs to be addressed across Lebanon's government agencies as most their existing assets have not been accurately valuated and reflected in their balance sheets for the past 30 years.
8. **Conduct systematic completion review and ex-post evaluation**.

Roles and responsibilities within an efficient PIM system

The application of these features however differs depending on the country's capacity and context. Roles and responsibilities should be allocated depending on capacity in a way that ensures the following 4 key functions are performed across the system (World Bank, 2020):

1. **Proposer**: Identifies the need or emerging problem and formulates the response in the form of a project.
2. **Appraiser**: Analyzes and assesses the project's economic, social and environmental value.
3. **Reviewer**: Evaluates the quality and robustness of the analysis at each step and advises decision makers.
4. **Decision-maker:** Validates the decision to move on to the next stage based on the findings and recommendations of the prior stages.

These four functions do not need to be performed by the same body or agency. If the proposer and appraiser can be the same, the reviewer should be different, while decision-making is usually done at the level of the Council of Ministers. The allocation of roles and responsibilities may differ according to project size, sector, level of government, or all three. Related thresholds are usually defined in tier 2 decisions or regulations. The various roles and responsibilities of major PIM players are summarized in Appendix 2. Key institutional players in the Lebanese context are listed in Box 7.

Box 7: Key institutional players in the PIM process

- **Line ministries and other spending units** with their departments and subordinated agencies, where projects originate and are implemented.
- The **Ministry of Finance**, which has a critical role in coordinating capital budgeting for new and ongoing projects and in "validating" resources' availability.
- The **Council of Ministers** or an **inter-ministerial committee** (or similar committee), which may have a role in confirming appraisal decisions and selecting projects to compete for budget funding
- A **ministerial committee**—made up of finance, public works and others infrastructure related ministers—with powers delegated from the council of ministers for major projects and for guiding policy formulation.
- The **High Council for Privatization and Public-Private Partnerships.**
- The **Council for Development and Reconstruction**
- The **Parliament** that makes the final decisions on project funding through the budget process.

Well-informed, structured decision making prior to implementation is essential for a good PIM system.

Source: Adapted from World Bank, 2020, Public Investment Management Reference Guide, Chapter 4.

The Regulatory Framework

A fundamental enabler of the proper functioning of the PIM system is a well-designed regulatory framework. International benchmarks point out to three models of PIM regulatory frameworks (World Bank , 2020):

1. Specific primary legislation such as a PIM law
2. Directly through the budget law or fiscal responsibility law (or equivalent)
3. Indirectly through the budget and fiscal systems legislation (or equivalent)

In Lebanon, there is no specific reference to PIM in any of the legislation in place[4]. Fragmented guidelines can be found in a set of existing financial laws (figure 3), namely:

- The Public Accounting Law of 1963 (decree No. 14969)
- The Public Private Partnership Law of 2017
- The Public Procurement Law 244/2021

This fragmentation renders the design and enactment of a modern regulatory framework a high priority. However, given the current constraints linked to the political economy of financial reform in Lebanon, the legal framework is not covered in the scope of this report. Alternatives arrangements are proposed to fit the current legal framework, with minor legal amendments at the level of Tier 2 and 3. One efficient alternative would be to introduce PIM legislation alongside the reform of the budget and the design of a new organic budget law.

Establishing a dedicated PIM unit

PIM related activities are among the most specialized in Public Financial Management. Where there is no specific institution that manages these four functions, establishing a dedicated PIM unit can help create the needed expertise and streamline processes.

In spite of a diversity of administrative arrangements related to their location and reporting lines, these units usually share similar responsibilities with respect to PIM and are usually **of an advisory nature.** They include undertaking and/or coordinating independent reviews, acting as centers of excellence for the development and dissemination of guidance material and best practice methodologies and assuming broad monitoring roles (World Bank, 2020). None of them is directly involved in capital budgeting, which remains the responsibility of the Ministry of Finance. As well, final decision-making lays elsewhere in government. Their role can usually involve one or more responsibilities among the following:

- Establish and facilitate the implementation of a robust regulatory framework to guide Public Investment Management.

[4] A detailed analysis of the legal framework in place, of its strongpoints and weaknesses was provided in the initial project inception report.

- Lead on the design and /or update of the national public investment strategy or plan, prepare studies on investment opportunities and challenges, and provide advice to the Government.
- Take part to the mobilization of foreign financing for public investment including of innovative financing instruments, in coordination with the Ministry of Finance and the High Council for Privatization and PPP.
- Set standards and guidelines and develop manuals for the pre-appraisal and appraisal phases and monitor their application.
- Build and maintain a database of public investment projects.
- Offer technical assistance and advice to line ministries and spending agencies in preparing their calls for projects.
- Act as a Secretariat for the Government or equivalent national body in charge of decision-making on public investment.
- Escalate concerns and risks to concerned ministers and decision-makers.
- Coordinate planning with the Ministry of Finance.
- Work with ministries and implementing agencies to build capacities across the cycle of PIM.
- Manage land acquisitions, expropriations, etc. when needed for a public investment project.
- Conduct or coordinate independent reviews and provide advice on proposals.
- Carry-out or oversee the ex-post evaluations
- Provide an annual review of progress on the implementation of the public investment plan or strategy.
- Publish data and information related to PIM.

It is recommended that capital budgeting remains the responsibility of the finance ministry like it was the case in Chile and Ukraine.

Possible institutional arrangements for Lebanon

Lessons learned from countries in fragility and aid-dependent

In their extensive work on Public Investment Management, Rajaram and al (Rajaram, et al., 2014) were able to draw "PIM System Typologies" that capture distinctive patterns of PIM system functionality given the countries' profile.

Two of these typologies can inform the current prospective work conducted for Lebanon, namely the ones that applies to:

- ***Aid dependent states:*** With the current crisis, the sharp drop in revenues, level of debt and of fiscal deficits, future public investment in Lebanon is expected to be largely financed on donor funding.

- *Fragile states*, as Lebanon is seeing its policy and institutional capacity rapidly deteriorate (Institut des Finances Basil Fuleihan, 2022).

Lessons drawn from these two types of PIM and patterns to reform that may be applicable to the case of Lebanon are listed below:

1. **If aid is largely provided in the form of budget support, weaknesses in government capacity for project appraisal create an immediate risk of seeing low quality projects being selected for financing and implementation**. Given the scarcity of capital and implementation capacity, this would impose a high opportunity costs on citizens that would not benefit from the implementation of more "context-relevant" and potentially more valuable projects.
2. **A good PIM system in an aid-dependent state requires strong central coordination mechanisms** to avoid overlaps in projects' design and allow for their smooth sequencing across sectors and for the coherent integration of both external and domestic investment projects. **It also requires the accurate estimation of recurrent costs, and an independent government review of both locally and donor-appraised projects** to ensure that full account is taken of domestic conditions and capacity constraints and to counter potential "optimism bias".
3. **If the strategic planning function of the government collapses, donors may decide to base their investment decisions on multi-donor needs assessments and trust funds**, potentially leading to further fragmentation and uneven development across the country.
4. In such set-ups, **budgeting can be substantively weakened by the volatility and unpredictability of donor funding** (especially budget support) and by the lack of integration of capital and current expenditures that can in turn impair the operation and maintenance of investments upon their completion.
5. **The set-up of Project Implementation Units (PIUs), or parallel administrations,** usually established to speed-up project appraisal and implementation **carries forward major risks pertaining to domestic capacities and procurement, accounting and reporting systems**. Lebanon has experimented in the post-civil war period with such arrangements as the country was lacking both staff and infrastructure to provide basic public services (Zein & Sims, 2004). The set-up of PIUs staffed with consultants and contractual staff were helpful on the medium term but did not allow over the long term to inject a new and skilled workforce into the public administration (Institut des Finances Basil Fuleihan, 2022), and substantively undermining its overall capacity to initiate or manage projects.
6. **Approaches to PIM reform in aid-dependent settings usually focused on starting to strengthen project implementation capacity through:**
    - 6.1. **Procurement reform with the modernization of procurement laws, the establishment of new procurement authorities, the training of procurement staff and the strengthening of internal and external audits.** This reform was initiated in 2019 in Lebanon and a new law was passed in 2021. It entered into force in August 2022, with the establishment of the Public Procurement Authority and the on-going training of procurement officers across government and in municipalities. External procurement audits practices still need to be reviewed to align with the new law.
    - 6.2. **High-level political impetus to monitor progress of project implementation**, showing a major shift from past practices and focusing on the execution of the annual budget.

6.3. **Rationalizing and reducing the number of PIUs by combining existing capacity under a single institution, and streamlining planning and budgeting function with the introduction of medium-term fiscal frameworks.**

7. **Approaches to PIM reform in fragile settings follow similar patterns** while prioritizing the development of a strategy for public investment, establishing mechanisms to coordinate donor financing and procurement reform.

Figure 12: Main PIM reform priorities in Aid-dependent countries and fragile contexts

Aid-dependent countries	Post-conflict and fragile settings
• Preliminary screening of projects against comprehensive, authoritative, and costed national and sector strategies • Building capacity for project preparation and appraisal • Consistency between development and recurrent budgets • Strengthening budget gatekeeping • Better insulation of investment spending from donor funding volatility • More effective project accounting, reporting, and monitoring • Strengthening implementation of procurement • Rationalizing and mainstreaming PIUs • Basic post project review, effective compliance audits of projects by supreme audit institution, and more effective asset management and service delivery	• Reestablishing national consensus over public investment priorities • Donor coordination • Building capacity for basic project appraisal • Consistency between development and recurrent budgets • Basic project accounting, reporting, and monitoring • Procurement capacity • Basic post project review • Transparency of public investment across PIM cycle • Managing the transition from emergency to development assistance

Source: World Bank (2014), The Power of Public Investment Management Transforming Resources into Assets for Growth

Box 8: Georgia's long road towards gradual PIM reform

In Georgia, public investment management performs well due to a set of good practices: (1)Fiscal rules in place give predictability of funding for public investment; (2)During implementation, investment is appropriately funded, and nonfinancial assets including depreciation are reported in government consolidated financial statements.

However, several challenges still exist. Strategic planning is solely focused on new policy initiatives and does not provide a solid base for the budget process. Roles and responsibilities of the various stakeholders are not clearly defined, and multiyear budgeting is not well implemented in practice, providing limited medium-term guidance for investment decisions. As well, project evaluation, selection, and management are weak, and there is no standard methodology for determining maintenance needs.

Several efforts to improve the PIM function have been underway such as Georgia's development policy operation programmatic series (2009 to 2012), which helped establish a long-term vision for public investment management reforms. However, gaps in the system remained unattended. Commitments to reform PIM were renewed in 2018 when the MoF requested the assessment of Georgia's public investment management framework and assistance for the development of a reform strategy with a prioritized action plan for strengthening public investment management. Starting in 2019, the initial PIM methodology was updated and comprehensive, up-to-date, and user-friendly PIM guidelines were developed, in addition to a number of regulations related to PPPS and others, taking into consideration the recommendations of the International Monetary Fund (IMF). These measures are expected to improve the system's effectiveness, accountability, and transparency and to increase general government investment spending from 6.1% of GDP in 2017 to 8% of the GDP by 2023.

Sources: (IMF, 2018); (Policy and Management Consulting Group, 2019)

Possible institutional arrangements for setting-up a PIM unit in Lebanon

To face existing fragmentation, harmonize capital expenditure management, enhance the effectiveness, monitoring and quality of public investment in Lebanon, and maximize the use of potential donor financing, a number of reform measures need to be undertaken, starting with the establishment of an overall regulatory and institutional framework for PIM to define roles and responsibilities during the PIM cycle, and define common standards and methods in a consistent manner. However, given the constraints and challenges related to the enactment of a new financial law in Lebanon, propositions made in this report focus solely on the establishment of a PIM central unit, in the context of the existing regulatory framework and taking into account its limitations. However, it remains fundamental to note that to achieve the objectives of a better PIM, the regulatory and institutional reform should go hand-in-hand.

The main reform measure that can be introduced within the institutional framework is the establishment of a new PIM unit, that would be the single government agency in charge of overseeing quality-at-entry processes, coordinating strategic planning and ensuing systematic oversight and monitoring of the entire pre and post investment processes (figure 13).

This unit shall ensure that all projects comply with the PIM System regulations, providing a "Seal of Approval" to any investment initiative, before its transfer to the Council of Ministers for the final investment decision. Detailed responsibilities and tasks to be handed by this unit are available in section 3.4 above.

In summary, this unit shall exercise supervisory functions of public and mixed investment projects conducted by all entities disbursing public funds, including SOEs, public corporations and municipalities, issue recommendations, raise awareness of decision-makers on existing risks, develop standards, technical and economic procedures, guidelines, rules and methodologies for the pre appraisal, appraisal and post-evaluation phases, and propose updates, instructions and norms to enhance the overall PIM system.

It shall focus its work on:

- Improving PI planning and prioritization, in line with national needs and objectives
- Enhancing resource allocation for public investments
- Developing comprehensive and efficient project implementation systems

It shall be endowed with enough autonomy and margin of maneuver to liaise with all spending entities across governments and to report directly to key decision-makers such as the Council of Ministers, the Ministry of Finance or the Parliament.

Figure 13: Five steps to reform the regulatory and institutional environment of PIM

International practice and guidelines allow to draw two possible institutional arrangements for the establishment of a PIM unit in Lebanon:

Scenario 1: Establish a new PIM unit within the Ministry of Finance

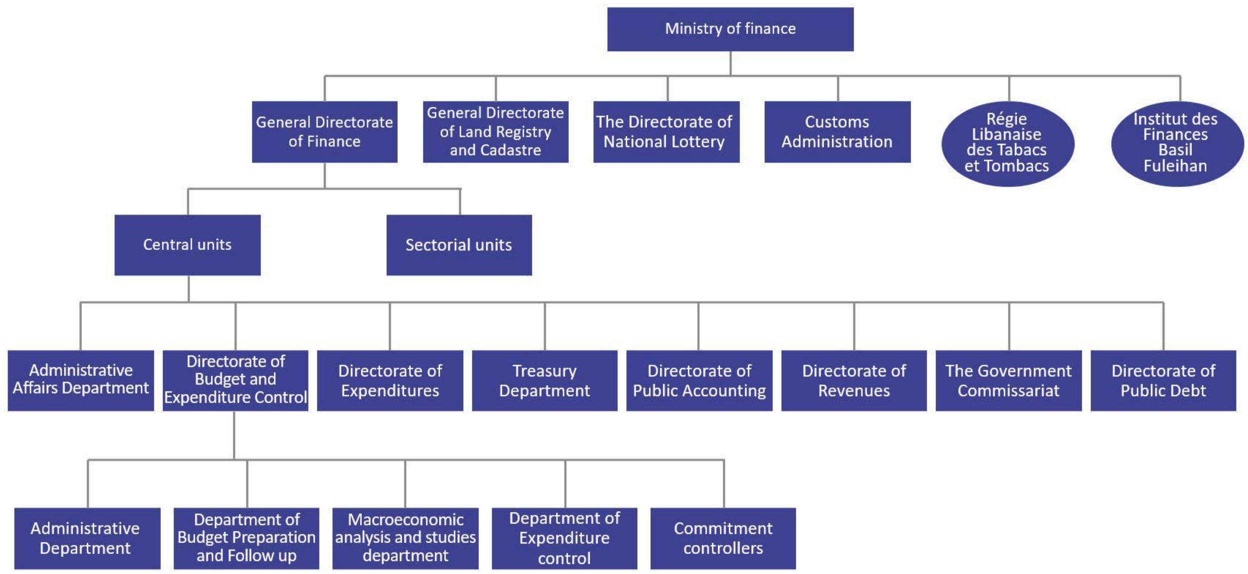
Scenario 1 would allow to streamline all planning, budgeting and spending functions of PI under the umbrella of the Ministry of Finance.

Usually, if a PIM unit is created within the Ministry, it shall be located at departmental level therefore guaranteeing direct lines of communication with senior officials and decision-makers and ensuring adequate staff resources that are already familiar with core functions of capital spending. Placing this unit under at the level of sub-department or unit could potentially leave it isolated, without influence, and unable to properly work with other government institutions, especially in weak institutional contexts (World Bank, 2020).

Based on the organization of the Ministry of Finance (figure 14), a PIM unit could be created as a new Directorate in the DGF (similar to the Directorate of Budget and Expenditure Control, Directorate of Debt, etc.). This administrative arrangement would provide the newly established unit with a direct line of communication with the Director General and/or Minister and with the ability to liaise with senior decision makers. It would give it a seat at the table in designing the PFM strategy and other strategy decisions related to the Ministry of Finance, therefore reinforcing checks and balance in decision-making.

This administrative arrangement would require the vote of a law to be presented by the Council of Ministers or by Members of Parliament (based on the Legislative Decree No.111 dated 12/6/1959).

Figure 14: Organigram of the Ministry of Finance of Lebanon[5]



Scenario 2: Transform the CDR into a Council for Public Investment and Development in charge of planning and overseeing PIM

Scenario 2 proposes to aggregate all existing PIM functions under a single institution, currently known as the Council for Reconstruction and Development, and to amend its current role, shifting it gradually to an institution in charge of planning and overseeing public investment management.

This would allow to capitalize on the know-how accumulated by the CDR in managing a large share of capital investment projects since 1977 (Decree No. 5 dated 31st January 1977).

The CDR is a public institution enjoying administrative and financial autonomy. It operates under the premiership of the Council of Ministers (Legislative Decree No. 5 dated 01/31/1977). It is endowed with planning, advisory, management, execution, resource mobilization, financial management and oversight functions, among which to:

a. Prepare plans for reconstruction and/or development[6], and propose economic, financial and social measures coherent with this plan to serve specific development objectives and submit them for approval to the Council of Ministers;
b. Prepare budget estimations for these plans to be integrated into the state budget;
c. Draft laws in relation to reconstruction and development;

---

[5] Public institutions operating under the tutelage of the Minister of Finance are not included under this organigram.

[6] Reconstruction and development projects refer to physical, economic and social infrastructure projects as well as to investments made in the productive sectors.

d. Develop a guiding framework for urban planning and submit it to the Council of Ministers;
e. Prepare feasibility studies for reconstruction and development projects;
f. Request from various ministries, departments, public institutions and municipalities to initiate projects and prepare pre-appraisal documents;
g. Execute reconstruction and development projects or assist and monitor the execution of these projects by public administrations, institutions, and municipalities or by private contractors;
h. Establish cooperation with countries, bodies, foreign institutions and organizations able to provide technical assistance to Lebanon in the field of reconstruction and development;
i. Submit proposals for financing to financial institutions and donors to finance reconstruction and development projects;
j. Conduct research in the fields of development and reconstruction;
k. Prepare and publish statistics and studies related to reconstruction and development projects.

Until 2016, the CDR used to execute around 34% of on-budget public investment, 20% of central government capital projects directly financed by donors and 27% of central government expenditures financing public investment for municipalities (IMF, 2018).

Transforming the CDR into a Council for Development and Public Investment, still operating under the direct supervision of the Council of Ministers, would require:

1) Issuing a law by the Parliament to amend its name and prerogatives.
2) Conducting an institutional assessment to determine strengths and weaknesses and to assign areas of improvement or reorganization for the new entity to meet its new mission.

However, when an agency outside the Ministry of Finance is handling PIM related functions, it is important to have a clear demarcation of the roles and responsibilities of the Ministry of Finance versus those of the PIM unit and clear coordination between the two entities, to optimize the management and outcomes of PI projects and ensure that projects are developed within a realistic macro-fiscal framework and with an appropriate level of financial resources.

The PIM Unit would provide strategic guidance, manage pre-appraisal and appraisal stages as well as independent reviews, and take the lead on monitoring, ex-post review and evaluation.

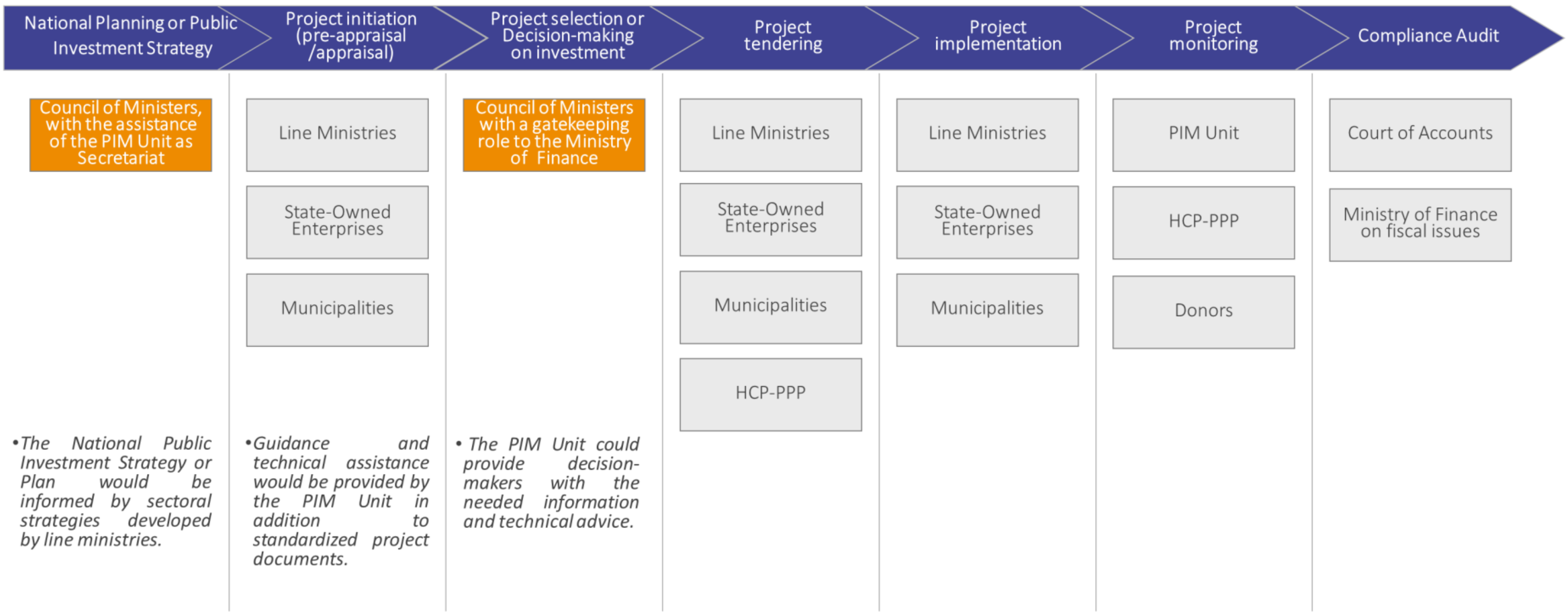
Capital budgeting shall remain the responsibility of the Ministry of Finance, like it was the case in Chile and Ukraine. In some Sub-Saharan African countries–for example, Ghana and Tanzania– poor coordination with the finance ministry has resulted in unaffordable strategies and plans, which have limited use in guiding public investment choices (World Bank, 2020).

Figure 15: Possible scenarios for institutionalizing a PIM unit in Lebanon within the current legal framework

Scenarios	Opportunities	Weaknesses
Scenario 1: Establish a new PIM unit at the Ministry of Finance in the form of a Directorate of Public Investment	• Strengthening capital spending and enhancing integration with the budget	• Existing shortcomings in budget planning and execution need to be addressed • Depleting HR at the Ministry of Finance
Scenario 2: Transform the CDR into a Council for Public Investment and Development	• Capitalize on existing expertise in managing capital investment projects	• CDR mixed track record • Requires a thorough institutional assessment for the restructuring of the CDR • Requires clear coordination mechanisms with the MoF for capital budgeting

Figure 16 provides an update on the PI workflow in comparison to Figure 3.

Figure 16: PIM workflow following the establishment of a PIM Unit



Resources needed for the PIM Unit

Notwithstanding the scenario that will be adopted for Lebanon, the powers of the PIM unit shall extend to all spending entities involved in Public Investment.

As a regulator, the PIM Unit shall be subject to the ex-post audit of the Court of Accounts, and to the control of the Central Inspection Board and the Civil Service Board.

In terms of staffing and human and financial resources, indicative staff and budget structures are proposed below but shall be refined and approved upon the pre-establishment of the PIM unit, depending on the administrative arrangement this unit will take, whether inside the Ministry of Finance or through a transformation of the CDR.

In general:

This unit shall be headed by Director (category 2 with Lebanon's civil service), appointed according to article 12 of law no. 222 dated 29/5/2000.

A tentative distribution of functions foresees the establishment of six departments within the Unit:

1. **The Policy and Legal department**: concerned with the development and interpretation of the regulatory framework for public investment (premier and secondary legislation), the formulation of policy improvements, the review of instructions, guidelines and other standard documents prior to their official adoption, the provision of responses to legal advisory requests, and the coordination of local and international cooperation.
   Tentative number of staff*: one head of department and four staff persons*
2. **The Strategic Planning department:** concerned with the design and /or update of the national public investment strategy or plan, preparation of prospective and market studies on investment opportunities and challenges, provision of investment advice, coordination with sectoral entities, and the mobilization of sectoral expertise.
   Tentative number of staff*: one head of department and three staff persons*
3. **The Investment Projects department:** concerned with the review of instructions, guidelines and other standard documents, the provision of technical assistance to spending entities, the review of projects' pre-appraisal and appraisal documents, the preparation of TORs for the mobilization of external experts and consultants, the management of the review process and the issuance of the "seal of approval" for selected projects.
   Tentative number of staff*: one head of department and six staff persons*
4. **The Resource Mobilization department**: concerned with mobilization and coordination of foreign financing including of innovative financing instruments, coordination with the Ministry of Finance, coordination with the High Council for Privatization and PPP, and donor reporting.
   Tentative number of staff*: one head of department and three staff persons*
5. **The Monitoring and Analysis department**: concerned with the monitoring and assessment of the function of the PIM framework and in particular with the design and deployment of PIM Information System, the collection, analysis and publication of PI related data, the preparation and publication of reports, the development of a risk management strategy, the conduct of

performance and compliance measurements, and the review of reports published by other stakeholders related to PI.
Tentative number of staff*: one head of department and four staff persons*

6. The Operations department: concerned with administrative and financial affairs including the preparation of an annual work plan and budget, the management of daily operations, the management of HR functions, the reporting on budget execution, the processing of correspondence and the handling of official communication.
   Tentative number of staff*: one head of department and four staff persons*

Recruited or appointed staff shall hold at least an advanced academic degree in economics, engineering, project management, procurement, finance, law or related fields of activity and have proven experience in investment management related functions.

The team of professionals working in the various departments shall be responsible for reviewing the strategic and operational activities of the PIM unit and for coordinating and overseeing the work of the various committees that would assist the unit in conducting its prerogatives. The two institutional scenarios propose above allow to mobilize the expertise already available in the public sector.

The team can be supported by external consultants to mobilize expertise that may not be available within the unit or the public sector, in particular for the project appraisal or reviewer phases. In that case, it is recommended that the PIM unit retains the ownership of the project by ensuring that the project design is in line with the original concept, that the proposer takes charge of the pre-appraisal and of providing the final recommendations to the decision makers. For instance, in Norway, consultants are employed through framework contracts to assist the Ministry of Finance in its reviewer role as part of the country's two-step quality-at-entry process for major projects. In France, the General Commission for Investment contracts individual private sector experts to conduct independent reviews of major projects (World Bank, 2020).

The PIM unit shall have an independent budget provided by the Government of Lebanon from the Budget Law to cover for its operations. Grants or donations by donors shall be subject to the provisions of conflict of interest.

This yearly allocation shall be deposited and managed in a dedicated account at the Central Bank of Lebanon, in accordance with the rules and regulations of the Public Accounting Law.

A budget of around USD 3,428,000 is estimated to be needed for the establishment, set-up and first two years of operations of the PIM Unit. A detailed estimation is provided in Appendix 3.

The roadmap ahead – Requirements for success

In addition to the establishment of a dedicated PIM unit, a number of measures and adjustments need to accompany this institutional arrangement and ensure the smooth implementation of the foreseen changes.

Part of these measures are concerned with the legislative and regulatory framework governing PIM as well as with the capacities of the new unit.

Another set of enhancements should be carried out by other PIM stakeholders, notably the Ministry of Finance, the High Council for Privatization and PPP, the Court of Accounts and the various spending agencies (line ministries, SOEs, municipalities).

Regulatory and operational enhancements related to the set-up of the new PIM unit

1. Develop relevant primary legislation that would endow the PIM unit with agreed upon prerogatives and organizational structure as well as needed secondary legislation (organization decrees, etc.) to be passed by Parliament and the Council of Ministers.
2. Recruit/Assign and train a core team.
3. Update the existing Capital Investment Plan to integrate the challenges brought forth by the economic, financial and fiscal crisis as well as the recommendations of the negotiations and Staff Level Agreement reached with the IMF. This update should be used as an opportunity to make informed trade-offs between critical needed projects and resources available and establish strong linkages with a sustainable development approach rather than politically-driven PI projects. This first exercise would pave the way for a regular monitoring and systematic review and update of any CIP.
4. Start developing basic procedural guidelines to be used by spending units, with the technical assistance of the international community. Prioritize pre-appraisal and appraisal documentation to streamline both processes, support existing capacity and circumvent the risk of seeing low quality or politically-backed projects get selected for financing and implementation.
5. Establish and gradually deploy a PIM Information System.
6. Propose a regulatory framework for state assets management.

Enhancements related to the work and operations of other stakeholders

Enhancements related to the Ministry of Finance

Whether the new PIM unit is established within or outside the Ministry of Finance, the latter shall remain the sole responsible of capital spending. It shall therefore work towards the integration of capital and recurrent expenditures in a in medium-term budget framework, to better align selection criteria with resource envelopes and make the best use of public investment as a instrument of public expenditure management.

Enhancements to be introduced by the Ministry of Finance include:

1. Estimate a capital baseline, and strengthen capabilities in capital budgeting
2. Set a "Gateway Process" applicable to all investment projects, including PPPs (refer to box 2 on how to set-up a gateway process)

3. Account for contingency to allow the government to better manage fiscal costs and risks arising from complex long-term PI contracts.
4. Introduce multiannual commitment appropriations through a MTBF.
5. Integrate capital and recurrent budgeting.
6. Modernize accounting standards to better capture PI and PPPs specificities in the Government's balance sheets and ensure transparent and realistic budgeting, accounting, and reporting.

Enhancements related to the High Council for Privatization and PPP[7]

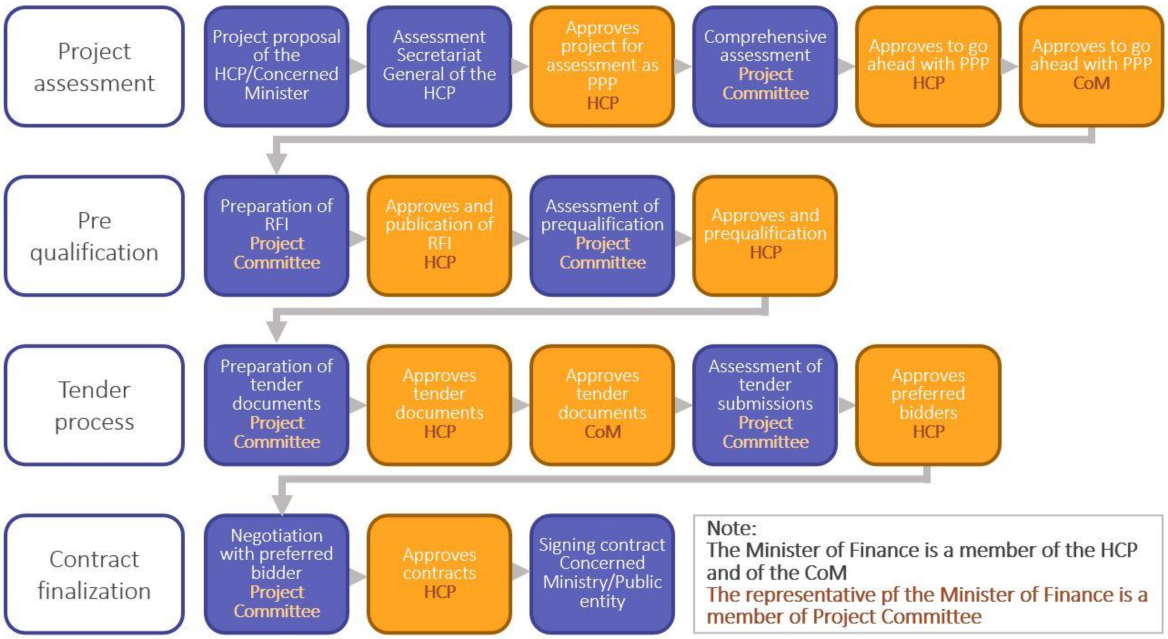
In the current regulatory framework, the Ministry of Finance does not have an explicit responsibility nor the power to stop PPP projects that are not affordable or that endanger public finances. The PPP law passed in 2017 granted the authority to the High Council for Privatization and PPPs to handle PPP long- term agreements between the Government of Lebanon and the private sector. However, the law failed to put in place the needed institutional arrangements with the Ministry of Finance to make sure the fiscal impact of such projects are properly managed.

As for all public investment projects, PPPs are not part of a multi-year investment plan nor linked to a resource envelope. The process of PPPs is run in parallel to that of Public Investment and of the Budget. Their fiscal accounting and reporting are very limited and not all costs emanating from PPPs are properly reflected in the government's accounts. Finally, the responsibilities of the various stakeholders are not clearly defined:

- Decisions of the HCP are taken by absolute majority vote. The Minister of Finance has only one vote in the six-member HCP committee and consequently does not have the power to stop a project that is unaffordable;
- Roles and responsibilities of the members of the Project Committee that is formed for each project to study the potential implementation of PPP are not detailed.

[7] The present section was developed based on the recommendations of two workshops conducted with the HCP, the MoF and the IMF Middle East Technical Assistance Center in 2019, 2020 and 2021 to assess and manage the fiscal risks of PPPs in Lebanon.

Figure 17: Preparation and Procurement Process of PPS as provided for in the Lebanese PPP Law



Given these shortcomings, it is important to provide the Ministry of Finance with the authority and resource to act as "gate keeper" with the authority to stop projects that endanger fiscal sustainability at key stages of the project cycle. This may require amendments and/or clarifications to the existing PPP law (2017).

Figure 18 proposes a distribution of responsibilities between the entity in charge of the PPP and the Ministry of Finance.

Figure 18: Proposed distribution of roles and responsibilities between the spending entity in charge of the project and the Ministry of Finance

	Project Manager (line ministry / supervising ministry)	Ministry of Finance
Pre-appraisal phase	Prepare and submits project proposal to MoF	Assess whether the proposed project is expected to be viable and affordable
	MoF provides opinion on project based on review	
Appraisal phase	Prepare and submits feasibility study and a project appraisal to the MoF	Review project appraisal and feasibility studies and assesses viable and affordable of the project Unless the project is likely to be not viable or unaffordable, the project is proposed to be included in the projects pipeline

	Gateway 1: Minister approves / rejects project for inclusion in the pipeline	
Pre-Tendering phase	If a project is proposed to be implemented as a PPP: Prepare assessment of efficiency of PPP as procurement method	Review efficiency assessment and ensure that the project is most efficiently implemented as a PPP, and that the project is viable and affordable as a PPP.
	Gateway 1B: Minister approves / rejects for inclusion in the pipeline as PPP	
Financing phase	Include projects from the pipeline list in budget proposal based on sectoral priorities.	Review sectoral budgets to ensure that the sectoral budgets are in line with sectoral policy, with long-term fiscal sustainability, and that PPPs do not undermine long-term sustainability (breach PPP ceilings where these exist).
	Gateway 2: Minister approves / rejects project to be included in budget proposal	
Council of Ministers approves projects as part of the budget proposal		
Parliament approves projects as part of the Budget Law		
Procurement phase	Prepare and submit to the MoF tender documents for projects that are included in the budget	Review tender documents to ensure project is within proposed scope and stays within approved expenditure, i.e., remains affordable.
	Gateway 3: Minister approves / rejects tender documents	
Implementation phase	Submit project with contract negotiated with selected bidder to MoF	Review negotiated contract to ensure that the project remains viable and affordable.
	Gateway 4: Minister provides non-objection / objection to negotiated contract	
Monitoring and adjustment phase	Submit proposal for any substantial changes to the contract for approval to the MoF	Review the proposal to ensure that changes are viable and affordable.
	Gateway 5: Minister approves / rejects adjustments	

The implementation of these enhancements requires close coordination between the PIM Unit, the MoF and the HCP.

Enhancements related to other spending agencies

Modern governance models have increasingly delegated PIM functions to spending units, with the aim of giving them full responsibility for their own projects from preparing and proposing them to implementing them, provided a central PIM unit is established and empowered to provide strong guidance and monitoring.

To help these spending units fulfill their roles efficiently, it is important to:

- Sensitize them on the changes to be made to the PIM framework and to good international practice.
- Train them since early stages of the PIM reform to consolidate their capacities in strategic planning, procurement, budgeting, and project preparation, and to create sufficient capacity in sectoral entities.

- Train them on the use of the new procedures.

Enhancements related to SOEs, Public corporations and Municipalities

By law, SOEs and municipalities enjoy a substantial degree of autonomy in public investment decision making. In addition, the exact volume of the public investment they carry remains unknown, since they do not send all their financial and fiscal information to the Ministry of Finance, it is highly recommended to:

- Make their reporting to MoF mandatory and based on unified standards and create a centralized and integrated SOEs' fiscal database
- Establish a process or worfklow of information linking SOEs and municipalities to the MoF to support risk analysis and improved oversight.
- Provide them with assistance in asset valuation.
- Make them by law abide to the PIM rules and regulations.

Various arrangements were experimented worldwide. In Georgia, where the central government has no power over the expenditure decisions of local governments, nevertheless the budget law allows the Ministry of Finance to regulate their budget process, notably through a capital budgeting methodology for public investment. In Chile, all spending entities at all levels of government are required to use the SNI for all their projects. In Korea, all projects implemented by municipalities and that request funding from are subject to the PIM regulations (World Bank, 2020).

Enhancements related to the Court of Accounts

Some of the prerogatives of the Court of Accounts may need to be revisited in the framework of a renewed PIM framework, such as the removal of pre-approvals and the application of strict deadlines for the Court to issue its opinions. It will also be crucial to develop the capacities of the Court of Accounts in conducting value-for-money audits on capital investment projects. This step could start gradually with pilot projects on recently implemented PI projects.

The following table summarizes the roles expected from the main stakeholders and the changes they need to own.

(icon ■ refers to importance and ● influence; color gray refers to low, yellow to medium and red to high)

Stakeholder	Current role in PIM	Changes to be introduced into the current framework
The Ministry of Finance ■ ●	• Approve and coordinate capital budgeting • Assess and manage fiscal risks generated from PI projects	Establish a "Gateway Process" (Boxes 7 and 8) for all investment projects, account for contingencies, introduce multiannual commitment appropriation, integrate capital and recurrent expenditures, estimate a capital baseline, modernize accounting

		standards and strengthen its capabilities in capital budgeting.
The High Council for Privatization and PPP ■ ●	• Plan and implement privatization programs • Manage PPPs	• Amend the 2017 PPP law to grant the Ministry of Finance a gatekeeping role with the authority to stop projects that endanger fiscal sustainability at key stages of the project cycle. • Put in place the needed institutional arrangements and tools (e.g. risk matrix) to make sure that the fiscal impact of PPP projects are properly identified, assessed and managed. Integrate PPPs in a multi-year investment plan linked to a resource envelope.
Line ministries / Spending agencies ■ ●	• Originate and implement PI projects	• Be aware and trained on PIM framework and practices. • Get acquainted with the new procedures in view of taking at a later stage full responsibility for their own projects.
SOEs, public corporations and municipalities[8] ■ ●	• Originate and implement PI projects	• Comply with the new PIM rules and regulations. • Regularly publish financial reports on Public Investment projects based on unified standards.
The Court of Accounts ■ ●	• Provide an external review and judgement on the legality and probity of the Government's financial statements and performance	• Introduce value-for-money audits on pilot PI projects • Release the CoA from pre-approvals to focus on post audit • Apply strict deadlines for issuing legal opinions.

[8] Most of these entities currently operate off-budget.

Appendix 1: Eight "must-have" features of a consolidated PIM framework

1. **Provide for strategic investment guidance, project development and pre-appraisal screening**: This includes broad guidance to anchor public investment decisions and projects into national development plans and objectives and steer potential sectoral trade-offs and preliminary screening to ensure that proposed projects meet minimum criteria. The framework shall also outline clear and institutional guidance to line ministries and spending entities on how to initiate public investment projects, in the form of operational guidance and the provision of templates for pre-appraisal. Project profiles would allow for a first-level screening to retain or reject proposed projects.
2. **Lay down a formal project appraisal process**: Following the first screening, a formal project appraisal process shall be actioned, based on formal technical guidance publicized on how to conduct prefeasibility and feasibility studies (e.g. preliminary design, cost-benefit analysis and environmental and social impact assessments as well as risk assessment). This step is mandatory to be completed and independently evaluated prior to the discussion on financing. It is recommended to validate new investments only when the rehabilitation of existing assets is less cost-effective than undertaking a new investment. Capacity building and training on the use of these guidelines should be made available to line ministries and spending entities. In low-capacity environments like Lebanon, it is advised to focus on:
    a. Having a coherent justification for the project;
    b. Clearly specifying its objectives;
    c. Identifying alternatives and conducting broad comparative analysis;
    d. Examining the most promising alternative;
    e. Accurately and fully estimating project costs;
    f. Assessing qualitatively project benefits.

    It is advised to record all appraised projects in a database for both historical data and future reference.
3. **Secure an independent review of appraisal**: Good practice recommends subjecting project appraisals to an independent review to address potential bias coming from those who developed the project, such as an underestimation of costs or an overestimation of demand. This function can be performed by the PIM unit or by the Ministry of Finance, provided none of them has conducted the appraisal. It is also important to subject all projects, whether government-funded, donor-funded or subject to a PPP agreement, to the same appraisal stages.
4. **Make a final decision on project selection and budget using a clear budget process**, even if both processes run along different timetables. **This is one of the most critical stages of the investment management cycle** as it is often subject to political interference and pressure from the side of private lobbyists and contractors looking to influence the selection process. Therefore, it is essential to link the selection process to the budget cycle, through the fiscal framework, the designation of specific budget envelops for public investment and active assets management (figure 9). All investment projects, including PPPs, should go through a single pipeline to be assessed and selected according to the same criteria —

cost benefit assessment, policy priorities, and affordability. Forward costs and funding during budgeting should be closely scrutinized.

This can only be achieved if a strong gatekeeping function is put in place at the Ministry of Finance. That is probably the most important "must-have" feature of a PIM system that allows to strengthen fiscal discipline and limit waste, inefficiency and corruption.

5. **Strengthen project implementation** by strengthening procurement, project management and monitoring capacities, and issuing guidelines on these functions. Often, implementation challenges and delays result from poor project planning, selection and budgeting and from shortcomings in procurement.
6. **Create the capacity for project adjustments**: Monitoring needs to address progress against both the initial implementation plan and the funding envelop and should be able to take account of changes in project circumstances. Spending entities are therefore required to submit progress reports on both physical and financial implementation. Cost escalation should be closely monitored. In case it reaches a point where it is no longer incrementally beneficial, there should be a process to halt the project or its disbursements until an updated cost-benefit analysis is carried out.
7. **Make provisions for the sustainable operation of facilities**: Upon project completion, a clear mechanism should be in place to (a) ensure for the handover of management responsibility for future operation and maintenance of the created assets, and (b) foresee that budget funding is allocated to operate and maintain these assets. After that, agencies that are operating the asset are required to register the asset, record its value and maintain it in their record keeping. Asset valuation is a critical aspect that needs to be addressed across Lebanon's government agencies as most their existing assets have not been accurately valuated and reflected in their balance sheets for the past 30 years.
8. **Conduct systematic completion review and ex-post evaluation,** checking (a) whether the project was finished within the original (or amended) budget and time frame, and (b) whether the outputs were delivered as specified. In addition, the Court of Accounts should conduct compliance audits over investment projects.

   Ex-post evaluations, usually carried out two to three years or more after project completion on a selective basis, shall install a process of learning from experience. It should provide feedback to the government for improving future project design and implementation and trigger corrective measures for the overall PIM system. For countries with weak PIM capacities, ex-post evaluations can serve as a diagnostic tool to identify weaknesses and gradually address them.

Appendix 2: Roles and responsibilities of key players in Public Investment Management

Stage or Role	PROPOSER	APPRAISER	REVIEWER	DECISION MAKER
Pre-appraisal	Identifies and develops the project concept in response to an identified need or emerging problem, in discussion with relevant stakeholders Secures funding for appraisal if the ultimate decision is positive	Prepares an assessment (pre-appraisal) of the project concept and possible alternatives, focusing on strategic relevance, rationale, and long-run fiscal sustainability	Reviews justification for proceeding to project preparation, to identify nonstrategic projects and those likely to be nonviable economically or unaffordable (especially "white elephants") Advises decision makers accordingly	Decides if, on balance, there is a strong enough case for proceeding to project preparation, taking account of the pre-appraisal findings and reviewer's advice
Appraisal and selection	Initiates the preliminary design, feasibility study, and any necessary impact studies for the project Secures funding for detailed design and tender preparation if the decision is positive	Prepares a feasibility study to determine whether the risk-adjusted net social worth of the project is positive, if the social and environmental impacts are acceptable, and if the fiscal consequences are sustainable	Reviews the feasibility findings and tests their robustness, with an eye to identifying excessive optimism concerning costs and benefits and inattention to risks and deliverability	Decides if, in principle, the project represents good value for public money (that is, is likely to be efficient and effective) Decides if a major project is a priority for public funding, given competition from other projects Decides if a project may be proposed for budget funding
Capital budgeting	Prepares the capital budget proposal, including new projects that have been selected; ensures consistency with guidance from the finance ministry on financial constraints and government priorities	Analyzes the capital budget proposal to check that individual projects have all the necessary decisions and that none has circumvented earlier PIM stages; that new projects are deliverable in the planned time frame and within budgets; that proposed funding for new projects does not compromise the implementation of ongoing projects; and that the proposal supports the government's declared policy priorities, fitting within previously specified fiscal limits Identifies any competing claims for funding of new capital projects	Reviews capital budget proposals to verify alignment with government priorities, deliverability of new projects in the budgetary planning horizon, and aggregate fiscal sustainability, taking account of the appraisers' findings Prepares advice for the ultimate decision maker on resolving any competing claims for funding that cannot be resolved bilaterally	Approves capital budget proposals, having resolved all competing claims In so doing, decides to fund the full implementation of new projects included therein

<u>Source</u>: *World Bank (2020), Public Investment Management Reference Guide, chapter 4*

Appendix 3: Estimated Budget for the establishment, set-up and first two years of operations of the PIM Unit

Excel attached

References

Arabnet; Konrad Adenauer Foundation. (2022). *Braving the Storm: Safeguarding the Lebanese Innovation Economy.* Retrieved from https://www.kas.de/en/web/libanon/single-title/-/content/braving-the-storm-safeguarding-the-lebanese-innovation-economy

Atif, A., Flyvbjerg, B., Budzier, A., & Lunn, D. (2014, March). Should We Build More Large Dams? The Actual Costs of Hydropower Megaproject Development. pp. 1-14. doi:10.1016/j.enpol.2013.10.069

Cangiano, M., Curristine, T., & Lazare, M. (2013). *Public Financial Management and Its Emerging Architecture.* doi:https://www.elibrary.imf.org/display/book/9781475531091/9781475531091.xml

Central Administration of Statistics. (2022, 7 2). Key indicators. Retrieved from http://www.cas.gov.lb/index.php/key-indicators-en#:~:text=The%20average%20inflation%20rate%20in%202020%20is%2084.9%25.

Council of Ministers. (2022, 5 20). Financial Recovery Strategy and Memorandum of Economic and Fiscal Policies.

Couto&Gomide. (2022). *The Brazilian way of doing public administration - Chapter 1: Public Sector Planning, Retrieved from.* Retrieved from https://www.researchgate.net/publication/361292176_CHAPTER_1_-PUBLIC_SECTOR_PLANNING

ESCWA. (2021). *Multidimensional poverty in Lebanon (2019-2021) - Painful reality and uncertain prospects.* Retrieved from https://www.unescwa.org/sites/default/files/news/docs/21-00634-_multidimentional_poverty_in_lebanon_-policy_brief_-_en.pdf

EU, UNDP, WB. (2020). *Lebanon Reform, Recovery and Reconstruction Framework (3RF).*

Gherbal Initiative. (2022, 7 2). Loand and Grants. Retrieved from https://elgherbal.org/loans-grants

IMF. (2017). *Conflicts and Lebanon's Capital Stock - IMF Country Report 17/20.*

IMF. (2018). *Georgia Public Investment Management Assessment.* Retrieved from https://mof.ge/images/File/PIMA-2018-IMF.pdf

IMF. (2018). *Lebanon Public Investment Management Assessment .*

IMF. (2020, October 5). *Public Investment For The Recovery*. Retrieved from IMF Blog : https://www.imf.org/en/Blogs/Articles/2020/10/05/blog-public-investment-for-the-recovery

IMF. (2020). *Well Spent - How Strong Infrastructure Governance Can End Waste in Public Investment.* doi:https://doi.org/10.5089/9781513511818.071

IMF. (2022). *Congo 2022 Article IV Consultation and Second Review under the Extended Credit Facility Arrangement and Request for Modification of Performance Criteria and Financing Assurance Review.* Retrieved from https://www.imf.org/en/Publications/CR/Issues/2022/07/05/Democratic-Republic-of-the-Congo-Staff-Report-for-the-2022-Article-IV-Consultation-Second-520400

Institut des Finances Basil Fuleihan. (2022). *Hanging by a thread: Assessing the crisis' impact on Lebanese state institutions (2020-2021).*

Ministry of Finance. (2022). *Report on the Draft Budget Proposal for 2022.* Retrieved from http://finance.gov.lb/en-us/EventPdfs/English/Budget%202022.pdf

OECD . (2014). *Foreign Bribery Report.*

OECD. (2017). *Gaps and Governance Standards of Public Infrastructure in Chile.* doi:https://doi.org/10.1787/9789264278875-en

Policy and Management Consulting Group. (2019, 11 9). *Supporting MoF to Improve and Institutionalize Public Investment Management Methodology*. Retrieved from PMCG: https://pmcg-i.com/project/supporting-mof-to-improve-and-institutionalize-public-investment-management-methodology/

Rajaram, Anand, Le, T. M., Kaiser, K., Kim, J.-H., & Frank, a. J. (2014). *The Power of Public Investment: Transforming Resources into Assets for Growth.* The World Bank.

The Lebanese Center for Policy Studies. (2020). *Public Resource Allocation in Lebanon: How Uncompetitive is CDR's Procurement Process?* Retrieved from https://api.lcps-lebanon.org/content/uploads/files//1595575975-cdr_article_july2020.pdf

The Lebanese Center for Policy Studies. (2021). *Public infrastructure procurement in post-conflict power-sharing arrangements: Evidence from Lebanon's Council for Development and Reconstruction.*

UN. (2022). *Visit to Lebanon - Report of the Special Rapporteur on extreme poverty and human rights, Olivier De Schutter.* Human Rights Council . Retrieved from http://undocs.org/A/HRC/50/38

UNDP. (2020, 08 21). UN Geneva Twitter Account. Retrieved from https://twitter.com/ungeneva/status/1296847029037985792

World Bank . (2020). *Public Investment Management Reference Guide .*

World Bank . (Spring 2021). *Lebanon Economic Monitor, Lebanon Sinking (to the Top 3).*

World Bank. (2006). *Chile : appraisal of public investment.* Retrieved from https://documents1.worldbank.org/curated/en/666151468216003237/pdf/406180CL0Publi1b1OFFICIAL0USE0ONLY1.pdf

World Bank. (2018). *Jordan - 2018 Public Investment Management – Public Private Partnership Governance Framework.* Retrieved from https://documents1.worldbank.org/curated/en/479251538744462781/pdf/09a-JORDAN-Simplified-PIM-PPP-Governance-Framework-EN-19-May-2018.pdf

World Bank. (2020). *Public Investement Management Reference Guide.*

World Economic Forum. (2019). *The Global Competitiveness Report 2019.* Retrieved from https://www3.weforum.org/docs/WEF_TheGlobalCompetitivenessReport2019.pdf

Zein, F. E., & Sims, H. (2004). *Reforming war's administrative rubble in Lebanon.*