

**COMBINED PROJECT INFORMATION DOCUMENTS / INTEGRATED  
SAFEGUARDS DATA SHEET (PID/ISDS)  
CONCEPT STAGE**

**Report No.:** PIDISDSC16836

**Date Prepared/Updated:** 06-Jun-2016

**I. BASIC INFORMATION**

**A. Basic Project Data**

<b>Country:</b>	Kyrgyz Republic	<b>Project ID:</b>	P155148
		<b>Parent Project ID (if any):</b>	
<b>Project Name:</b>	Capacity Building in Public Financial Management 2 (P155148)		
<b>Region:</b>	EUROPE AND CENTRAL ASIA		
<b>Estimated Appraisal Date:</b>		<b>Estimated Board Date:</b>	21-Jun-2016
<b>Practice Area (Lead):</b>	Governance	<b>Lending Instrument:</b>	Investment Project Financing
<b>Sector(s):</b>	Central government administration (90%), Sub-national government administration (10%)		
<b>Theme(s):</b>	Public expenditure, financial management and procurement (100%)		
<b>Borrower(s):</b>	Ministry of Finance		
<b>Implementing Agency:</b>	Project Implementation Unit, Ministry of Finance		
<b>Financing (in USD Million)</b>			
	<b>Financing Source</b>	<b>Amount</b>	
	Borrower	0.00	
	Free-standing Single Purpose Trust Fund	6.00	
	Total Project Cost	6.00	
<b>Environmental Category:</b>	C - Not Required		
<b>Concept Review Decision:</b>	Track II - The review did authorize the preparation to continue		
<b>Is this a Repeater project?</b>	No		
<b>Other Decision (as needed):</b>			

## B. Introduction and Context

### Country Context

1. The Kyrgyz Republic is a lower-middle income country with a population estimated at 5.8 million people and a gross domestic product (GDP) of USD 7.4 billion. Its GNI per capita is USD 1,250 as of 2014. Almost two-thirds of the population live in isolated rural and mountainous areas. The Kyrgyz economy is characterized by significant informality, reliance on agriculture, extractives and remittances. GDP growth slowed to 3.6 percent in 2014 as higher investments were offset by weak external demand and a poor harvest. Construction increased by 24.9 percent driven by public investment growth and strong demand for residential buildings. Recession in the Russian Federation in 2015 undercut Kyrgyz trade and remittance flows. A modest increase in gold prices may provide some support to exports of gold. However, poor outlook for the Russian economy has led to a downward revision of Kyrgyz growth forecast to 2.5 percent (2015) and 3.3 percent (2016). Achievement of government forecasted growth rates of 5 percent or more will require sound macroeconomic policies, increased efficiency of public spending, increases in revenues from state owned enterprises and the development of a vibrant private sector.

### Sectoral and Institutional Context

2. Implementation of a modern public financial management system has been tracked through Public Expenditure and Financial Accountability (PEFA) assessments, with a baseline in 2009 and follow-up in 2014. PEFA highlights improvements in budget credibility, budget predictability, control over budget execution, accounting, and reporting, and in external scrutiny and audit over the period 2009 to 2014. Little progress is seen in budget comprehensiveness and transparency and policy alignment of budgets.

3. Budget credibility has improved for aggregate revenue and expenditure out-turn but remained weak for the composition of expenditure. Deviations of aggregate expenditure out-turn compared to the original approved budget have declined and revenue forecasting has improved. The extent of variance in the composition of expenditure by function has not declined, as the budget composition has still changed significantly during implementation. Consequently, budgets as presented to Parliament continue to lack credibility as an indication of the Government's resource allocation intentions.

4. Transparency in taxpayer obligations and effectiveness of tax administration have improved significantly. The updated Tax Code has reduced the number of taxes and required returns and simplified procedures for taxpayer compliance. Information for taxpayers is available at the State Tax Service (STS) website and at one-stop shops. The STS has unified taxpayer registers in one database which is linked to business and social contribution registration databases. STS has also started to conduct risk-based tax audits to more effectively target high risk taxpayers.

5. An automated Treasury Budget Information System has enabled improvements in budget predictability and execution through proper monitoring and cash planning. This system registers all expenditure and revenue transactions in real time and prevents the execution of any payment which is not provided for in the budget. The MOF has put in place arrangements for monitoring and control of public debt, with full monthly reporting of stocks and flows of both external and domestic debt. The Government undertakes borrowing now only on concessional terms and within a limit of 60 percent of GDP for the nominal value of outstanding external debt as stipulated in the law. Furthermore, the Government does not provide new guarantees for borrowing by SOEs or local governments. However, systems still need to be put in place to manage the public debt portfolio and keep track of payment arrears.

6. The timeliness and coverage of financial reporting have improved significantly. The

automated Treasury system generates two reports which, taken together, provide full information on revenues and expenditures of each individual budgetary organization including primary service delivery units such as schools and health clinics. Each budgetary organization produces a monthly expenditure report and submits it to the Treasury before end of the following month. The central Treasury generates a set of annual financial statements and relevant annexes covering the central government budget. The statements provide comprehensive information that includes revenues, expenditures, financial assets and liabilities, and non-financial assets.

7. The Chamber of Accounts has made progress in strengthening external audit. The 2012 and 2013 reports of the Chamber of Accounts provide evidence of the follow-up on audit recommendations. In particular, the 2013 report indicates that out of 1,447 recommendations arising from the 2012 audit 657 (45.4 percent) were fully implemented, 278 (19.2 percent) partially implemented, 157 (10.9 per cent) were not immediately applicable and 355 (24.5 per cent) were not implemented. The Parliament's Budget Committee and Finance Committee and specialized committees have strengthened their hearings on key findings resulting from this examination by the and in timeliness of the issuance of recommended actions. The executive has also implemented the recommendations issued by the legislature in a timely manner.

8. Significant improvements have been made in improving public procurement. In April 2015 the Parliament enacted a new Public Procurement Law (PPL) which was developed in line with international practice with the Bank support. The PPL has introduced modern procurement methods and enhanced disclosure of procurement information and data. The Government reorganized the Public Procurement Department (PPD) under the MOF into a regulatory body in 2014. The MOF developed e-procurement portal and e-Government Procurement (e-GP) with the support of the Asian Development Bank. The Bank together with the ADB and other development partners conducted a Country Procurement Status Review (CPSR) in Feb 2012. As a follow up to the CPSR, the Government has approved and implemented Public Procurement Strategy for 2012-14. Currently, the PPD is preparing a three year Public Procurement Strategy. Increasingly, the Chamber of Accounts has been increasingly involved in the audit of contracts.

9. The MOF has committed to the implementation of International Public Sector Accounting Standards (IPSAS). The Government has already reflected IPSAS reforms in legislation and regulations. The Bank team is assisting the Government to conduct Gap Analysis of the national accounting legislation and review of IPSAS practices in seven government and self-government entities. The Gap Assessment will inform development of the Strategy for implementation of simplified national accounting standards in public sector (KRPSAS) and of the outline KPRSAS and Chart of Accounts. Further implementation of KRPSAS reforms is a major challenge for the Government in the medium term.

10. The Open Budget Survey presents a somewhat more optimistic assessment of progress in the area of fiscal transparency than the PEFA assessment. The Kyrgyz Republic's OBI score increased from 20 in 2012 to 54 in 2014 which is slightly above a global average score of 45. The main factors that contributed to this improvement include publication of eight key budget documents tracked in the OBI and social accountability in the budget preparation. The Government regularly prepares a summary of the main elements of the budget for civil society and holds public hearings on the draft budget on an annual basis. In order to enhance transparency and ensure that citizens can exercise the right to access information held by public bodies, the MOF has launched a web site [www.okmot.kg](http://www.okmot.kg), which includes such portals as "Open Budget", "Electronic Public Procurement" and "Economic Map". Transparency could be further strengthened by simplifying budget materials and presenting them in a more user friendly format.

11. With the Bank and donor support, the Government has prepared a methodological and regulatory framework for program budgeting, including a roll-out of program classification for

expenditures and mechanisms for monitoring program performance. In particular, the Budget Circular covers program budgeting as well as other aspects of budget preparation. The MOF has issued instructions for setting performance indicators, which will potentially make possible the measurement of progress toward defined objectives. Coverage of government agencies involved in program budgeting was extended to twenty sectoral development strategies in the Medium Term Budgetary Framework (MTBF) for 2015-2017. However, program budgeting is still not used for budget decision making, budgets do not reflect program costs and their results orientation is still weak.

12. Medium-term fiscal planning has been at the core of PFM reforms since 2009 but with little sign of real progress. Ministries and agencies are required to provide detailed figures for the two out-years based on administrative, economic, functional, and sub-functional classifications. However, there is little evidence that forward estimates inform budget allocation when the budget is prepared the following year. Investment planning remains fragmented, with inadequate links to the planning of current expenditure. Furthermore, sector strategies lack objectives to be attained within specified timescales or resource allocations.

13. Stable fiscal planning has proved difficult because priority is given to protected expenditure (government employees' salaries, social benefits) rather than to public service priorities. The consequence has been continuing changes in the functional breakdown of government expenditure between budget estimates and actual out-turn. Large in-year changes in the composition of expenditure and the absence of any continuity in medium-term expenditure planning highlight difficulties in effective expenditure planning.

14. The regulatory framework for PFM reforms embodied in the Budget Code was approved in May, 2016. The Code replaces the Law on the Main Budget Principles and the Law on Treasury and is intended to establish a framework for budget management that reflects international practice.

15. Notwithstanding the improvements in financial reporting and accounting, the current automated financial management information system (FMIS) has a number of shortcomings. These include use of paper-based instructions from the Treasury to the National Bank of the Kyrgyz Republic (NBKR) for payments, lack of effective commitment controls and reporting on arrears and lack of centralized control of payroll. A long-running project to establish a Treasury Management Information System (TMIS) which would have linked budget preparation, budget execution, commitment control, payments and a Human Resources Management Information System was eventually cancelled in November 2013. Solutions currently under review include purchasing a new FMIS or further developing the current Treasury Budget Information System developed in-house by the MOF, which covers budget execution, reporting and accounting but lacks a budget preparation module and is not connected to the payments process. Currently, the MOF is looking for funds to procure the FMIS.

16. Development of technical and managerial skills needed to support the modern PFM system remains a long-term challenge. The MOF Training Center undertakes Government-wide training activities in support of the reforms. In recent years the Center has developed a Strategy for Distance Learning and implemented the 2013-2014 training plan. It has conducted training of MOF staff on an annual basis and at least 20 managers, 50 senior staff, and more than 2,000 PFM system personnel have been trained during 2010-2015. However, training needs of the Parliament, in particular of the Parliament Apparatus (e.g. Budget Committee), and of the Government Apparatus (e.g. Finance Division) have not been addressed systematically. Parliamentary discussions on the Budget Code and annual budgets indicate the need for technical training of all branches of power in the area of PFM. Similar concern arises about technical capacity of local governments and parliaments.

17. Since 2012 the Kyrgyz Republic has only two levels of government, each with its own budget. There are now 484 local authorities, made up of 453 essentially village governments and 31 urban authorities, including major cities of Bishkek and Osh. Local authorities receive 50% of the income tax and sales tax collected in their areas of jurisdiction. They also receive equalization grants, development grants and grants to cover unfunded mandates, which could emerge due to decisions made at the central level. The transfer of financial resources is essentially rules based. However, the formulae for equalization grants is complicated and development grants benefit relatively prosperous localities. In addition expenditure assignments are not clearly delineated and adequately reflected in legislation and instructions. The authorities plan to develop and implement medium term strategy for reform of intergovernmental fiscal relations.

### **Relationship to CAS/CPS/CPF**

18. Transparency and governance are at the center of the World Bank Group Country Partnership Strategy (CPS) for FY2014-2017 for the Kyrgyz Republic. The main objective of the CPS is to improve governance, largely focusing on three broad areas: public administration and public service delivery; the business environment and investment climate; and the management of natural resources and public infrastructure. The ongoing programmatic Development Policy Operation (DPO) series supports governance reforms in anticorruption, the judiciary, public financial management, energy, and trade and competitiveness, as governance improvements in these areas are crucial to the country's ability to move forward on this agenda. Policy dialogue under the DPO on PFM issues was supported by the Capacity Building in Public Financial Management Project series (CBPFM I from FY2009 to FY2015 and the proposed CBPFM II) and a number of smaller TFs .

19. CBPFM I, completed in May 2015 led to positive changes in PFM, although the pace of changes was slower than expected. Public procurement was the area that had shown the greatest improvement as a result of strengthening institutional, legal, and methodological frameworks as well as enhancing transparency in procedures. In addition capacity building of civil servants, improvements in regulatory framework and the general progress in PFM reforms were also important achievements of the project.

20. The Implementation Completion and Results Report for CBPFM I highlighted the following lessons learned: the need for TF contributors to synchronize the processes of signing Administrative Agreements to avoid delays in project implementation; project institutional arrangements should address coordination and implementation requirements within the implementing institutions; the project's results framework should be designed to support decision making during implementation as well as end-of-project evaluation; the results framework should not include results that are not within the scope of the project; the risks posed by frequent changes in the Government's core team should be made explicit and mitigation measures identified; and the project's flexibility to restructure project activities by responding to emerging opportunities was a design strength.

## **C. Proposed Development Objective(s)**

### **Proposed Development Objective(s) (From PCN)**

22. The Project Development Objective (PDO) is to improve budget predictability, control and transparency. Allocative efficiency entails the ability of government to prioritize public spending in accordance to economic and social needs. Thus allocative efficiency is directly linked to the composition of public expenditure, adequate flexibility of the budget to respond to spending priorities and the alignment of budget outturns with policy objectives as laid out in the budget and expenditure plans.

### Key Results (From PCN)

23. The following proposed results will allow tracking progress towards achievement of the PDO:

24. Decreased variance in the composition of expenditure out-turn (efficiency). The Project will support implementation of enhanced budget procedures for the preparation and execution of the annual budget and reforms pertaining to medium term fiscal planning and program budgeting. It is expected that these reform measures will contribute to the improvement in the composition of expenditure out-turn. According to the 2015 PEFA Assessment, variance in expenditure composition exceeded 15 percent in two of the last three years.

25. Diminished stock of expenditure payment arrears at the central government level (efficiency). As a result of enhancing the Treasury System and PFM processes, it is expected that the stock of outstanding expenditure payment arrears will decline. The 2015 PEFA assessment estimates that the arrears are in excess of 2 percent of total central government spending.

26. Reduced share of unreported extra-budgetary operations in central government expenditure (transparency). The Project will assist in expanding the coverage of the central government operations through incorporation of the Social Fund operations into Treasury Single Account (TSA). Hence, it is expected that the percentage of reported central government spending that enable an overall view of the central government finances increases. According to the 2015 PEFA Assessment, unreported extra-budgetary operations significantly exceed 10 percent of total central government spending.

Increased competence in management, administration, and technical functions and specifically in PFM in the MOF, Parliament's Budget Committee, Chamber of Accounts, Government Apparatus, local governments and parliaments (transparency). The project will support an ambitious capacity building program for legislative and executive branches of power in PFM area and TA on drafting PFM related legislation and instructions is expected to enhance Kyrgyz republic PFM. These achievements will be measured by improvements in PEFA scoring (PI- 6, PI- 11, PI- 12, PI-20, PI-21) on comprehensiveness of the budget, orderliness and participation in the annual budget process, multi-year perspective in fiscal planning, expenditure policy and budgeting, effectiveness of internal control and internal audit.

### D. Concept Description

27. The PFM Reform Action Plan approved by the President in 2009 initially covered the period 2009-2013. The Action Plan was updated for 2012-2015 and is currently undergoing further review and transformation into a more comprehensive document- PFM Reform Strategy for 2016-2025. An integral part of the Strategy is the PFM Action Plan for 2016-2019, which covers a wide range of measures aimed at strengthening budget preparation and execution, accounting, auditing and fiscal transparency, as well as improving public debt management, revenue administration, intergovernmental fiscal relations and transfers, public procurement procedures and public investment management. Complementing the PFM Action Plan, the Government has also adopted a Strategy for Developing Corporate Financial Reporting and Audit in the Kyrgyz Republic for 2014-2020. The project will support the PFM Reform Strategy for 2016-2025 and the PFM Action Plan for 2016-2019 and comprises six interrelated and mutually supportive components.

28. Component 1 Strengthening Fiscal Planning and Budget Preparation (USD 600,000). Component results include: approval of PFM related legislation; expansion of program budgeting; and an improvement in transparency. To achieve these results the component will finance technical assistance and capacity building related to:

Preparation of PFM related legislation/normative acts/instructions;  
Development of budget rules in order to increase predictability of the budget and to avoid unforeseen deviations within the fiscal year;

Strengthening medium-term forecasts and a Medium-Term Budgetary Framework (MTBF);

Implementation of program budgeting reforms, including improvements in program budget classification and sector level expenditure planning;

Improvements in budget transparency through improved coverage and quality of publicly disclosed fiscal information.

29. Component 2 Strengthening Public Expenditure, Debt Management, Public Procurement, Internal Control, Public Sector Accounting (USD 1,200,000). Component results include: treasury automation improved in line with international good practice; a fully operational payroll; an increased debt management system score on DEMPA analysis; implementation of national simplified accounting standards (KRPSAS). To achieve these results the component will finance technical assistance and capacity building related to:

Drafting legal and normative documents for incorporation of the Social Fund into the single treasury account;

Support to enhancement of the Treasury and a Financial Management Information System (FMIS), including: analysis of business processes and readiness of ICT infrastructure; drafting necessary legislation and normative acts, instructions; preparation of technical FMIS specifications; review of potential FMIS solutions and advice on an appropriate choice for an FMIS system; assistance in supporting interoperability of the FMIS with the existing management information systems (MIS);

Public debt management including implementation of an electronic database (debt recording system) and improvements in transparency of information on debt placement;

Payroll management, including monitoring and implementation of wage reform in the budgetary sector;

Development of Standard Bidding Documents (SBDs) and their incorporation into e-Government Procurement (e-GP); support e-GP development to include a framework agreement module and other methods such as e-reverse auction and e-catalogs, hardware strengthening and software improvement for framework agreements and the connection to the treasury system;

Support to implementation of the simplified national accounting standards (KRPSA) based on IPSAS and enhancement of a Chart of Accounts with supporting accounting manual and accounting certification;

Support to design and implementation of the government financial management and control system through drafting necessary legislation and underlying regulations, development of certification of the Internal Audit.

30. Component 3 Strengthening Intergovernmental Fiscal Relations and Sub-National PFM (USD 1,000,000). Component results include: approval of strategy on inter-governmental fiscal relations; publication of PFM assessments for sub-national governments; number of staff trained including managers. To achieve these results the component will finance technical assistance and capacity building related to:

Analysis of the system of intergovernmental fiscal relations, including sustainability and clarity of current expenditure assignments, equalization mechanisms, impact of budgetary loans and incentive grants on equalization;

Preparation of a medium-term strategic document on intergovernmental fiscal relations;

Simplification of equalization formulae and improvements in tax capacity assessments;

Preparation and implementation of a methodology for monitoring and evaluation of PFM

quality at the sub-national level;

Support to Communities of Practice created under the Scaling-Up the Peer-to-Peer Learning in Public Finance at the Local Self Government Level Project to continue capacity building of local budget officers, elected heads of local self-government units (Ayil Aymak), heads of budget commissions in the local legislature (Ayil Kenesh) through an innovative peer-to-peer learning approach.

31. Component 4 Strengthening Oversight by National Parliament, Capacity Building in Chamber of Accounts and Government Apparatus, Bank Supervision of the Project (USD 1,100,000). Component results include: an improvement in the OBI score for budget oversight and generation of reports on audit of public contracts. To achieve these results the component will finance technical assistance, capacity building and acquisition of equipment related to: Development of parliamentary staff and parliamentarians' capacity to exercise their oversight function;

Development of an analytical function in the National Parliament, possibly with the establishment of a specialized budget research office;

Implementation of public budget hearings;

Review of PFM related legislation;

For the Chamber of Accounts: improvement of a Public Procurement Audit Methodology and training materials and development of a Public Procurement Audit Methodology for e-Procurement Transactions; development of a software to conduct audit and monitoring; preparation of training materials and roll-out of training in Bishkek and at the regional level;

Development of Government Apparatus staff's capability to exercise their budget oversight function;

Project Supervision by the Bank.

32. Component 5 Strengthening Human Resource Management and Capacity Building in PFM (USD 1,100,000). Component results include: approval and implementation of a PFM strategy and a human resources strategy; core curriculum on PFM; capacity to deliver core curriculum; and change management activities to facilitate the Project implementation. To achieve these results the component will finance technical assistance, capacity building and acquisition of equipment related to:

Preparation of the Strategy for PFM System Development for 2016-2025;

Development and deployment of a change management program to support the new PFM Strategy and Treasury automation that will involve: a readiness for change assessment (including an analysis of business processes and readiness of ICT infrastructure as well as mapping of the main stakeholders); change management action plan; comprehensive communications strategy; and adaptive leadership and staff training;

Preparation and implementation of the Ministry of Finance Human Resource Strategy for 2016-2019;

Development and delivery of core training courses, including: evaluation of fiscal and investment risks; revenue forecasting; fiscal planning; program and performance budgeting; cash management; internal control and internal audit; accounting- IPSAS;

Development and delivery of distance-learning PFM modules;

Development of an analytical function in the MOF, possibly with the establishment of a specialized research office.

33. Component 6 Project Management (USD 400,000). This component will support implementation of the Recipient Executed part of the project and will finance technical assistance, capacity building and operational expenses, including project supervision, monitoring and evaluation, reporting, procurement, financial management activities of the Project Implementation



Unit (PIU).

## II. SAFEGUARDS

### A. Project location and salient physical characteristics relevant to the safeguard analysis (if known)

### B. Borrower's Institutional Capacity for Safeguard Policies

### C. Environmental and Social Safeguards Specialists on the Team

### D. POLICIES THAT MIGHT APPLY

Safeguard Policies	Triggered?	Explanation (Optional)
Environmental Assessment OP/BP 4.01	No	
Natural Habitats OP/BP 4.04	No	
Forests OP/BP 4.36	No	
Pest Management OP 4.09	No	
Physical Cultural Resources OP/BP 4.11	No	
Indigenous Peoples OP/BP 4.10	No	
Involuntary Resettlement OP/BP 4.12	No	
Safety of Dams OP/BP 4.37	No	
Projects on International Waterways OP/BP 7.50	No	
Projects in Disputed Areas OP/BP 7.60	No	

### E. Safeguard Preparation Plan

#### 1. Tentative target date for preparing the PAD Stage ISDS

20-Mar-2016

#### 2. Time frame for launching and completing the safeguard-related studies that may be needed. The specific studies and their timing should be specified in the PAD-stage ISDS.

Safeguard policies will not be triggered.

**III. Contact point****World Bank**

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**V. Approval**

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<b><i>Approved By</i></b>		
Safeguards Advisor:	Name: Agnes I. Kiss (SA)	Date: 01-Apr-2016
Practice Manager/ Manager:	Name: Adrian Fozzard (PMGR)	Date: 02-Apr-2016
Country Director:	Name: Jean-Michel Happi (CD)	Date: 08-Jun-2016

1 Reminder: The Bank's Disclosure Policy requires that safeguard-related documents be disclosed before appraisal (i) at the InfoShop and (ii) in country, at publicly accessible locations and in a form and language that are accessible to potentially affected persons.