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# Kyrgyz Republic

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Background Paper  
for the

## **Country Portfolio Review Mission**

(Joint Review by the Asian Development Bank, KfW Development Bank, the World Bank and the Islamic Development Bank)

*Kyrgyz Resident Mission*

*November 2004*

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## 2004 Country Portfolio Review Mission for the Kyrgyz Republic

### BACKGROUND PAPER

#### I. INTRODUCTION

1. The last year's portfolio review was conducted jointly with the World Bank in September 2003. The 2004 Country Portfolio Review Mission (CPRM) is scheduled to be fielded from 18-26 November 2004. This year the Islamic Development Bank (IsDB) and KfW Development Bank (KfW) agreed to join the portfolio review with ADB and the World Bank so that the common problems affecting the portfolios of the institutions could be taken up more effectively with the Government. Portfolio performance is an important determinant of resource allocation under the performance-based allocation formula. Therefore, poor portfolio performance not merely reduces project benefits and their development effectiveness, it could reduce future Asian Development Fund (ADF) allocations to the country which starting January 2005 would include a significant grant element. This year, CPRM will put greater effort to explain to the Government and other stake-holders and discuss ways to promote accountability through improved institutional arrangements. In addition, the following issues will also be taken up jointly with IsDB, KfW and WB: donor coordination, counterpart funding, prioritization of public investment program (PIP), harmonization of procedures, taxation of donor projects etc. Project-specific issues will be taken up by respective financing institution separately with the Government.

2. The overall objective of the CPRM is to assess the performance of the country portfolio based on the analysis of key performance indicators using information gathered during the review of individual projects. The Mission will present its findings to the Government and agree on an action plan to mitigate the implementation hurdles to improve portfolio performance. In doing so, the CPRM will work jointly with the World Bank and IsDB as required to: (i) review procedures and policies that cause implementation delays and underperformance, (ii) identify the major generic and cross sector issues in project implementation, and (iii) discuss ways to promote accountability for portfolio performance in the Ministry of Finance (MOF) and line ministries and agencies. CPRM findings will contribute to overall Kyrgyzstan's portfolio performance for determining the ADF resources allocation for the country in 2005.

#### II. OVERALL PORTFOLIO DESCRIPTION AND PERFORMANCE

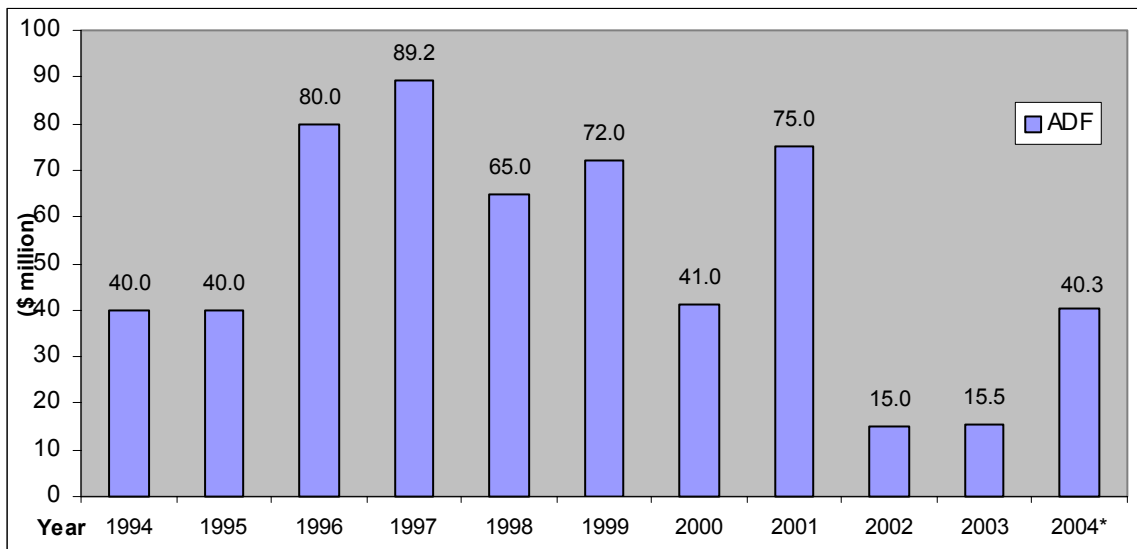
##### A. Portfolio Description

###### 1. Loans

3. **Size.** The Kyrgyz Republic became a member of the Asian Development Bank (ADB) in 1994 and began receiving assistance in the same year. As of 31 August 2004, the country has received 22 loans with a total amount of \$532.7 million equivalent. Of the total loans, nine loans have been closed and thirteen loans are ongoing, of these two are likely to be closed in 2004. Six out of the 22 loans are program loans totaling \$184.0 million for providing support to policy reforms to facilitate transition to market economy. The remaining 15 are project loans totaling \$348.7 million provided to support various physical investment activities. At present, 13 loans with a net loan amount of \$283.5 million are ongoing. These loans have an un-disbursed balance of \$126.6 million as of 31 August 2004. All these loans were provided on concessional terms from the Bank's special fund resources called ADF. Figures 1 and 2 show the volume of annual lending of ADB to the Kyrgyz Republic and the number of loans approved annually for the period 1994 to 2004. The list of approved loans by sector for the period 1994-2004 is provided in Appendix 1.

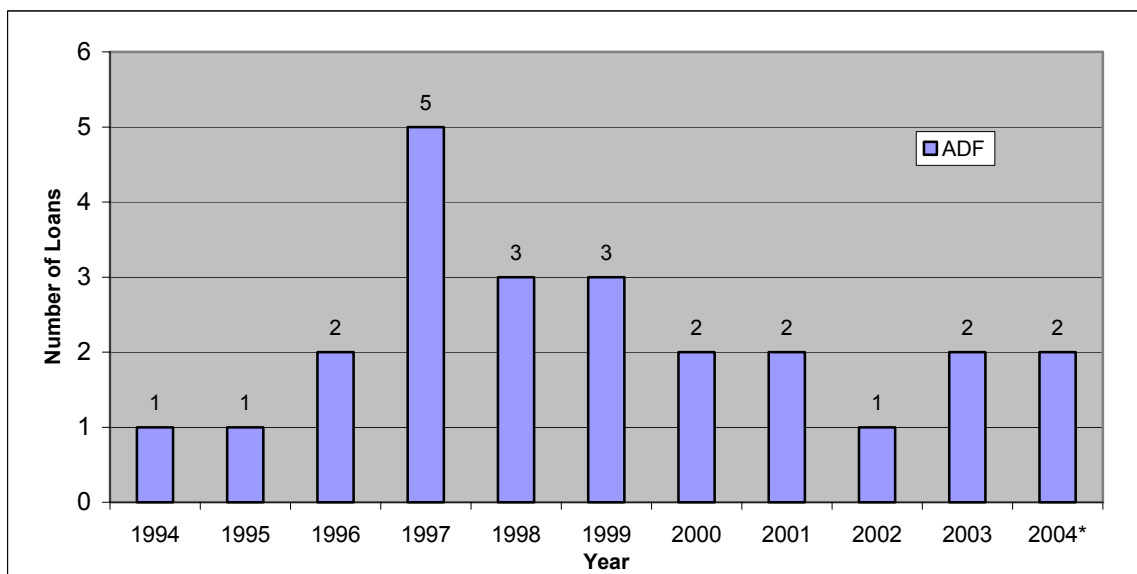
4. ADB's average annual lending level during 2002 and 2003 was \$15.25 million. This was much lower than the lending levels in the past largely due to the Government's policy of restrained borrowings as part of its debt reduction strategy. This strategy envisages a reduction in the size of largely externally funded PIP from about 6% of GDP in 2001 to about 3% of GDP by 2005. ADB's annual lending level began with \$40 million in 1994. It reached the peak level of \$89.2 million by 1997. Thereafter, the lending levels fell slightly and hovered between \$65 million and \$75 million till 2001. For 2005-2006 a \$40 million program was prepared but the indicated annual ADF allocations for the period is about \$31.5 million. Future lending levels will depend on the availability of ADF resources and the country's performance in promoting sound economic and social policies, good governance, and portfolio performance.

**Figure 1. ADB Lending to Kyrgyz Republic - Amount, 1994-2004<sup>1</sup>**



\* planned

**Figure 2. ADB Lending to Kyrgyz Republic- Number of Loans 1994-2004<sup>1</sup>**

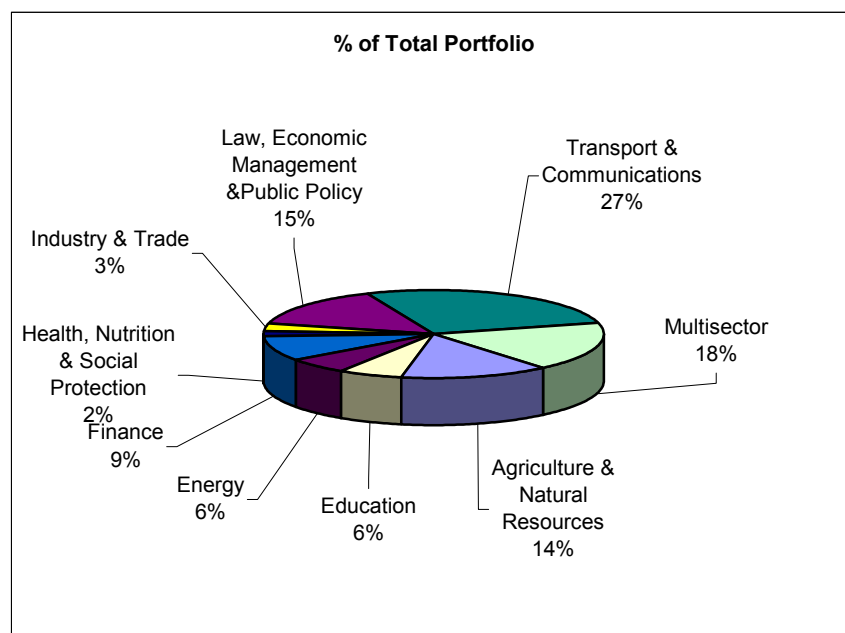


\* planned

<sup>1</sup> As of 31 August 2004

5. **Composition.** Appendix 1 provides the list of ADB loans approved from 1994-2004 while their sectoral composition as of 31 August 2004 is in Figure 3. The transport and communications sector continues to be the most important sector with a 27.2% share in ADB loans portfolio. Four loans were provided to the transport and communications sector in the amount of \$145 million three of which are (\$140 million) for rehabilitating the strategically and economically important Bishkek-Osh road. This road links the northern part of the country with the south which is separated by Ala-Too mountain range. The first two phases of this road are complete. Work on the third phase of Bishkek Osh road is underway. A \$5 million loan for rehabilitating the Kyrgyz segment of the regional Almaty-Bishkek road is also under implementation. Social infrastructure comprising education, health, water supply, and sanitation is the second largest recipient of ADB assistance accounting for 16.8%. Six loans were provided to improve social infrastructure with focus on basic education and its quality, management of the education sector, rehabilitation of schools and primary and secondary health facilities, promoting early childhood development, and provision/rehabilitation of potable water supply and sanitation facilities predominantly in rural areas. Some of the social sector projects cover more than one sector and hence classified under multi-sector. Promotion of capital markets and corporate governance, enforcement of contracts with minimum cost, and improving the legal and regulatory environment for the private sector is the third largest focus area absorbing \$79 million (14.8%) of ADB assistance. In the agriculture sector, which accounts for 14.3% of ADB portfolio, the focus is on rehabilitation of irrigation and other farm infrastructure, agricultural reforms, and institutional development. In the financial sector, ADB approved three loans (\$48.5 million) of which two supported the Government's efforts to improve regulation and management of the banking sector. The Rural Financial Institutions project is ongoing. ADB portfolio has one loan to promote regional cooperation among the Central Asian countries in the areas of regional transport and customs.

**Figure 3. Sectoral Distribution of Loans by Amount  
(as of 31 August 2004)**



**Table 1. Disbursements and Net Resource Transfers  
1999-2004**

Year	Amount in \$ Million		
	Loan Disbursement	Loan Service payment	Net Transfer of Resources
	A	B	(A-B)
1999	79.6	1.8	77.8
2000	21.4	2.4	19.0
2001	58.3	2.5	55.8
2002	27.2	3.0	24.2
2003	25.7	3.5	22.2
End-Aug 2004	37.3	2.3	35.0

6. The disbursements during the first eight months of 2004 exceeded total disbursements in 2003 by about 45% due to a sharp increase in the contract award ratio in 2003. As of 31 August 2004, the cumulative disbursement to the Kyrgyz Republic had reached \$404.9 million, or 76% of the total loan amount approved. As of the same date, the un-disbursed loan balance amounts to \$126.6 million.

7. The net inflow of resources to the country may fall modestly in the medium term for two reasons: the expiry of grace period of the loans taken before 1995, and a decline in the level of assistance from ADB during 2002 and 2003 which is expected to remain so for some more years. The payment of service charges has, however, been increasing (Table 1).

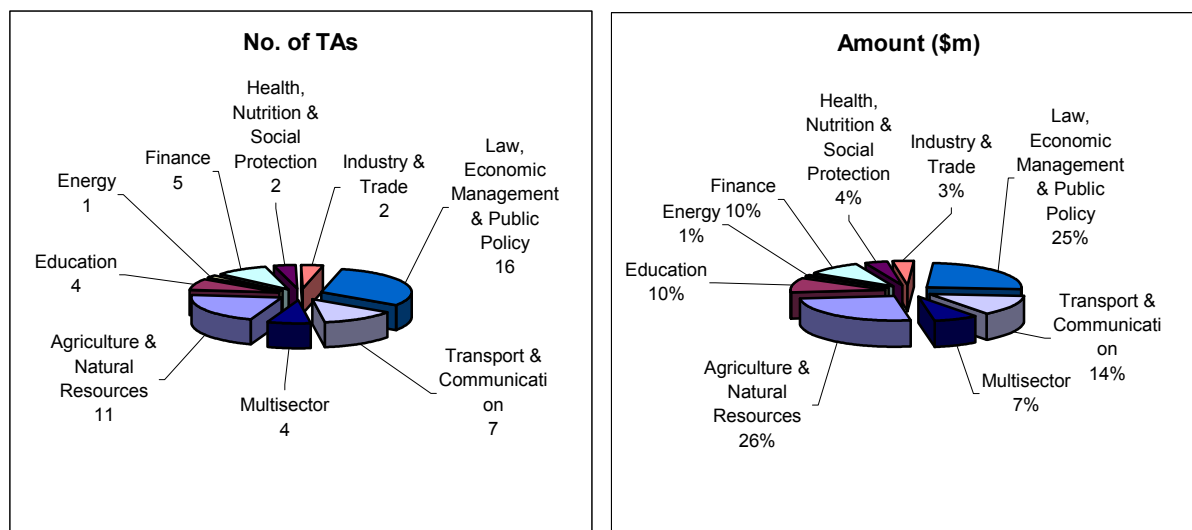
## 2. Technical Assistance

8. **Size.** As of 31 August 2004, ADB provided 52 technical assistance (TA) projects amounting to \$31.47 million. Of these 14 are project preparatory TAs amounting to \$9.69 million and the remaining 38 TAs for \$21.78 million are advisory TAs for capacity building, policy advise, institutional strengthening and training. The list of all approved TAs by sector is provided at Appendix 2. Twenty four of the 52 TAs were completed as of 31 August 2004. A list of all active TAs by sector is given at Appendix 6.

**Table 2. Sectoral Distribution of Approved TAs by Amount and Number  
(as of 31 August 2004)**

Sector	No. of		Amount	
	TAs	%	\$ Million	%
Agriculture & Natural Resources	11	21.2	8.254	26.2
Education	4	7.7	3.030	9.6
Energy	1	1.9	0.310	1.0
Finance	5	9.6	3.030	9.6
Health, Nutrition & Social Protection	2	3.8	1.200	3.8
Industry & Trade	2	3.8	1.100	3.5
Law, Economic Management & Public Policy	16	30.8	7.898	25.1
Transport & Communication	7	13.5	4.290	13.6
Multisector	4	7.7	2.360	7.5
<b>Total</b>	<b>52</b>	<b>100</b>	<b>31.472</b>	<b>100.0</b>

**Figure 4. Sectoral Distribution of TAs by Number and Amount (as of 31 August 2004)**



9. **Composition.** The sectoral composition of the approved TA portfolio is shown in Figures 4 and Table 2. The agriculture sector is the recipient of the largest amount of TA funds, \$8.25 million (26.2%), mainly for capacity building in the Ministry of Agriculture, institutional development (eg. water users associations), planning management of the sector, and environmental monitoring. About 25% of TA allocation amounting to \$7.9 million was provided for improving law, economic management and public policy activities mainly in the form of advisory TAs. Among these are strategically important TA projects to strengthen the economic policy making capacity in the Office of the President, and improving the capacity in Ministry of Finance to improve its project management and public investment prioritization capabilities. In addition, advisory support was provided to improve governance in the private sector, judicial reforms, support for the preparation of the National Poverty Reduction Strategy, and in a number of other areas. Social sector activities accounted for about 17.5% of TA support about half of which was for project preparation. The share of project preparatory TAs is generally larger in the assistance provided to specific sectors. Advisory TA in specific sectors is provided to support policy reform and assist in project implementation through capacity building in the respective line ministries. ADB's advisory TAs provided high quality technical inputs to assist the Government's policy and institutional reforms.

## B. Portfolio Performance

### 1. Loans

10. As of 31 August 2004, 13 projects are at various stages of implementation with an un-disbursed amount of \$126.6 million. A number of other indicators are used to assess portfolio performance such as time taken for loan effectiveness from approval, annual contract award ratio, disbursement ratio, and timely closure of loan accounts. The average time taken for approval to loan effectiveness for the ongoing Kyrgyz portfolio of 13 loans was 6.9 months in 2003 which was one month shorter than ADB average of 7.9 months. On average, the Kyrgyz Republic took 3.5 months for loan signing after approval, almost the same as ADB average, but after signing, loans became effective a month faster than ADB average.

**Table 3. Disbursement and Contract Award Performance**

Year	Contract Award Ratio %				Disbursement Ratio %			
	With Program Loans		Without Program Loans		With Program Loans		Without Program Loans	
	Kyrgyz	ADB	Kyrgyz	ADB	Kyrgyz	ADB	Kyrgyz	ADB
2000	6.6	20.0	7.5	17.7	11.9	20.5	13.1	18.3
2001	21.3	14.9	5.4	13.0	30.3	20.5	18.5	19.4
2002	13.3	22.6	10.8	17.9	15.2	22.2	13.4	16.3
2003	31.4	17.3	38.1	14.6	15.7	20.2	18.7	17.1
End-Aug 2004	14.7	10.7	17.5	10.5	22.4	9.3	12.6	8.8

11. The contract award ratio<sup>2</sup>, and the disbursement ratio<sup>3</sup> are key measures to gauge the portfolio implementation performance. These ratios are influenced by three sets of factors: the structural characteristics of the portfolio in terms of its age and composition; generic country specific factors such as the availability of counterpart funds, institutional capacity for project implementation, and project specific problems. Table 3 presents time series data on contract awards and disbursement ratios. The contracts award ratio (with program loans) improved sharply from 13.3% in 2002 to 31.4% in 2003 and was much better than ADB-wide performance. Excluding the program loans, this ratio was much higher in 2003 (38.1%) about 2.6 times ADB wide average. A significant acceleration in project implementation took place after the resolution of start-up problems in the road, waster supply and sanitation, and agriculture sectors and that contributed to a sharp increase in this ratio. Aggregate contract awards were \$51 million in 2003, 121.7% percent of target. As expected, the contract award ratio more than doubled in 2003 as the startup problems in social sector and agriculture sector projects and in two road sector projects were resolved. **Prognosis for 2004 is good with 84% percent of the projected contract awards of \$16.7 million (excluding program loans) has been accomplished till end-August 2004.**

12. Disbursement performance (with program loans) continued to be poor. In 2003 it was 15.7% which is less than ADB average of 20.2%. This improved in 2004 due to the release of the final tranches of both active program loans<sup>4</sup>. Disbursement ratio (excluding program loans) for the Kyrgyz Republic in 2003 was better 18.7% than the previous year and also ADB average (17.1%). However, preliminary trends for the first 8 months of 2004 show only a 55.3% accomplishment of the year's target for project loans. **Disbursement performance needs closer monitoring in the rest of 2004.**

13. A summary of project ratings is shown in Table 4 (Details are at Appendix 3). These rating are based on a Project Performance Report (PPR) system introduce by ADB in 1999 which assess project performance against two major parameters: (i) development objective (DO); and (ii) implementation progress (IP). Project performance under each of these parameters is rated into four categories, i.e. highly satisfactory (HS), satisfactory (S), partly satisfactory (PS), and unsatisfactory (US). Since introduction, PPR criteria have been refined continuously to minimize subjectivity in rating and to focus on the early identification of projects which are at risk. Implementation progress is assessed on the basis of timeliness in loan signing, effectiveness and implementation, timely availability of sufficient counterpart

<sup>2</sup> The ratio of contracts awarded/actual commitments during the year to the value available for the contract awards/commitments at the beginning of the year, plus the value of contract awards/commitments accrued during the year under new loans, minus cancellations of uncommitted loan balances during the year.

<sup>3</sup> The ratio of total disbursements in a given year over the net loan availability at the beginning of the year plus the new loan amounts that became effective during the year.

<sup>4</sup> Loan 3950-KGA: Customs Modernization and Infrastructure Development, and Loan 1860-KGZ: Corporate Governance & Enterprise Reform Program-Phase II.

funds, cost overruns, compliance with loan covenants, timeliness of consultants fielding, the number of staff-days fielded for project monitoring, etc. Given the increased focus of ADB on governance and anticorruption, timely submission of audited project accounts and agency financial statements (APA/AFS) is given a high weightage in project performance assessment.

**Table 4: Summary of Ratings of Ongoing Projects**

No	Loan No./Project Title	DO	IP
1	1529-KGZ(SF) Rural Financial Institutions	S	S
2	1547-KGZ(SF) Capacity Building in Corporate Governance and Insolvency	S	S
3	1555-KGZ(SF) Education Sector Development*	S	S
4	1630-KGZ(SF) Second Road Rehabilitation	S	S
5	1645-KGZ(SF) Social Services Delivery and Finance	S	S
6	1726-KGZ(SF) Agriculture Area Development	S	S
7	1742-KGZ(SF) Community-Based Infrastructure Services Sector	S	S
8	1775-KGZ(SF) Almaty-Bishkek Regional Road Rehabilitation	S	PS
9	1853-KGZ(SF) Third Road Rehabilitation	S	S
10	1860-KGZ(SF) Corporate Governance and Enterprise Reform Program II	S	S
11	1926-KGZ(SF) Regional Trade Facilitation and Customs Coop Program-Kyrgyz	S	S
12	2007-KGZ(SF) Community Based Early Childhood Development	S	S
13	2045-KGZ(SF) Emergency Rehabilitation	S	S

Notes:

DO – Development Objective, IP – Implementation Performance, S - Satisfactory, and PS - Partially Satisfactory

\* Closed on 30 September 2004

14. Key portfolio management indicators at Appendix 3 indicate an improvement in portfolio performance in 2003. The overall risk ratio of the portfolio improved marginally from 13.7% in 2002 to 10.4% in 2003 and was less than ADB average (13.2% in 2003). As was for the entire ADB portfolio, project implementation delays, significant disbursement delays and fielding of project missions constitute the three largest risk factors for the Kyrgyz portfolio. These three factors alone constitute 79% of the risk. Other important risk factors are delays in the establishment of project implementation units (PIUs) and fielding of consultants, environmental and social factors and poor compliance with covenants. There was a marginal increase in the overall portfolio risk during the first 8 months of 2004 mainly due to implementation delays, shortage of counterpart funds, and disbursement delays. Unlike last year when there was no project at risk, this year the Almaty-Bishkek Road Rehabilitation project (Loan 1775–KGZ) is rated at risk due to implementation delays caused by reasons beyond the Government's control<sup>5</sup>. As against 16 flags<sup>6</sup> in 2003, portfolio has one flag less in 2004 although there are two additional projects. There are two projects with a total of 3 flags each which need closer monitoring – Loan 1775-KGZ: Almaty-Bishkek Regional Road Rehabilitation, and Loan 1547-KGZ: Capacity Building in Corporate Governance and Insolvency. Of these, the latter loan is expected to be completed in 2004. One more loan with two flags Loan 1853-KGZ: Third Road Rehabilitation also needs special attention.

## 2. Technical Assistance

15. Of the total 52 approved TAs, 18 are ongoing totaling an approved outlay of around \$11.29 million. Six of these are complete but not financially closed. Four of the active TA are for preparing projects and the rest are advisory. The average age of ongoing TAs has increased considerably from 29.8 months in 2002 to 38.7 months as of 31 August 2004. In addition to qualitative assessment of accomplishment of project objectives, three quantitative

<sup>5</sup> The project was significantly delayed because of delay in ratification of the cross border transit agreement by the Kazakhstan Parliament.

<sup>6</sup> Flags are used to mark risk factors. This is explained in detail in Appendix 4.

indicators are used to assess TA portfolio performance: the time taken to sign the TA agreement, the time taken to field TA consultants, and the delays in submission of final report. Assessment of performance of ongoing TAs in terms of these quantitative indicators is given at Appendix 6.

16. The Government took an average of 1.8 months which is ranging between two weeks to 3.5 months in 2003 to sign TAs after they were approved, much better than ADB average of 3 months. As against the norm of 6 months, the time taken to field consultants after TA signing averaged about 8.8 months in 2003, which was even longer than in 2002. But this parameter looks much better if the transport sector is excluded. On average, the fielding of consultants took 26.3 months in the transport and communications sector. The average time taken to field consultants was the shortest (1.1 months) in the case of TA 4068 KGZ: Capacity Building in Savings and Credit Unions and Micro-finance Institutions. The delay was the highest (26.6 months) in the case of TA 3757–KGZ: Institutional Support in the Transport Sector (details at Appendix 6). There was an average of 5.6 months delay in the submission of final reports as of 31 August 2004. The reasons for late fielding of consultants and delayed submission of TA final reports need to be investigated.

17. TA completion reports (TCRs) for 14 out of the 34 completed TAs are available. These rate 9 TAs as successful in accomplishing their objectives. The remaining TAs are partially successful. Five TAs were post-evaluated in 2002, of these three were rated as successful and two partially successful. ADB provides substantial technical assistance to the Government for capacity building, institutional strengthening, and project preparation in a wide range of sectors. Frequent changes in senior officials in the ministries, reorganization of agencies, transferring of personnel trained under the TAs have had considerable adverse impact on the benefits of a number of the technical assistance projects. In particular, the above factors impacted adversely on the objectives of TA: 2473 – Strengthening the Ministry of Economy; TA: 2450 – Reorganization and Strengthening of the Ministry of Agriculture and Food Processing Industry; TA 2879 – Strengthening of Education Planning and Administration, and TA: 3234 - Strengthening Aid Coordination and Management. The ongoing efforts to reform the civil service is likely to reduce the high turnover of staff, a major cause for impeding the development impact of TAs.

### **III. PORTFOLIO PERFORMANCE AND MAJOR ISSUES**

#### **A. Introduction**

18. The last year's CPRM identified, jointly with the World Bank, a number of common problems affecting portfolio performance. These problems could be grouped under three broad themes: general institutional and policy environment, portfolio performance assessment, and sector policy issues. This section reviews the current status of key issues identified under these themes.

#### **B. General Institutional and Policy Environment**

19. There is not much of change in general policy and institutional environment compared to last year. The scarcity of funds for public investment, inadequate institutional capacities and deficiencies in administrative structures, and lack of understanding of policies and procedures of external aid agencies continue to affect project implementation. In addition, the project implementation units raised concerns about considerable delays in disbursements. Some of these problems are of managerial nature and should not be allowed to have an impact on project implementation performance. Others are structural in

nature and would take time and considerable effort to resolve them. Scarcity of public funds, and certain types of institutional and administrative deficiencies are structural in nature. Many aspects of institutional deficiencies and the lack of understanding of donor procedures could be addressed with capacity building and effective portfolio management. ADB has recently provided a TA to improve the capacity in the Ministry of Finance and line Ministries in this area<sup>7</sup>. Other ADB-supported investment projects and TAs need to address this pervasive problem of institutional deficiencies by focusing on capacity building and human resource development.

#### a. Scarcity of Budgetary Resources for Public Investment

20. **Public Investment Program.** The unsustainable level of public external debt forced the Government to adopt fiscal austerity as part of its debt reduction strategy<sup>8</sup>. An important element of this strategy is to limit external funding of PIP to a sustainable level, which is determined at about 3% of GDP from 2005 onwards. This has accentuated the scarcity of funds for PIP and also created difficulties in finding counterpart funds and affected the implementation of ongoing projects. The serious fiscal situation is unlikely to improve in the medium term unless the Government finds new sources of revenues and succeeds in obtaining debt relief on concessional terms from the Paris Club creditors to reduce the debt service burden. Even so, the limits placed on external funding of PIP are unlikely to be removed as those are determined by debt sustainability considerations with a view to reducing the stock of debt to a sustainable level. Easing of fiscal situation could however improve the Government's ability to provide counterpart funds and perhaps increase domestic resource support for PIP.

21. To comply with the imperatives of the debt reduction strategy, the Government considerably reduced its borrowings from all donors, including ADB and the World Bank, during the past three years and slashed the size of its future borrowing program. Consequently, disbursement requirements of the ongoing projects exceeding the PIP ceiling by a wide margin has been reduced to manageable limits. In fact, the disbursement requirements of PIP projects for the period 2005-2009 (of \$406.3 million) will be less than the Government could spend (up to \$426.5 million) under the PIP ceiling during the period. The forecasts show that the problem of excess disbursement requirements (about \$45 million) now exists mainly in 2005 and 2006. From 2007 onwards, the disbursement requirements of all ongoing and programmed projects will be below the IMF ceiling on PIP of 3% of GDP. In fact the shortfall could be even large considering the grant element in ADF IX assistance, which provided up to 50% in grant for Kyrgyzstan on program basis starting January 2005, and the grant element being not covered by the PIP limit. If the IMF shows some flexibility, the Government could spend above the PIP limit during 2005-2006 to complete the ongoing projects on time without violating the IMF's ceiling for the 2005-2009 period. Such an approach would facilitate timely completion of the ongoing projects, which is important not only for protecting project benefits but will also improve portfolio performance which in turn will facilitate larger allocation of highly concessional ADF and IDA resources. **CPRM will request the Government to seek flexible PIP limits from the IMF to harmonize fiscal adjustment with project funding requirements. It would be prudent to fix annual disbursement targets on the basis of implementation schedule of ongoing projects giving flexibility to allow disbursements to exceed the fiscal deficit targets in some years while maintaining long-term average.**

<sup>7</sup> ADB. 2002, TA 3996 –KGZ: Strengthening Capacity in the Government to Manage Externally-Assisted Projects. The consultants were fielded in May 2003.

<sup>8</sup> This program is supported by the IMF under its Poverty Reduction and Growth Facility (PRGF).

22. **Shortfalls in PIP Spending and Counterpart Financing.** Persistent shortfalls in spending on PIP below the limits set by the IMF is a major portfolio management and also a critical development issue. This primarily reflects the Government's policy to resort to the soft option of compressing development spending to meet its fiscal adjustment obligations under the PRGF. The objective of these spending limits is to bring down the level of PIP to sustainable levels over a period of time and also to provide the private sector adequate time to fill in the void left by PIP to the possible extent. Under this scheme, any short fall in PIP spending below the ceiling agreed with IMF would entail a deadweight loss to the economy because the future ceilings are not likely to be relaxed to offset shortfalls in past spending. Yet, the shortfall in spending has been recurrent since 2001<sup>9</sup>. **During 2001-2003, the Government did not utilize \$42.5 million available to it under the PRGF for public investment which is close to excess disbursement requirements of \$45 million forecasted for 2005-2006.** Thus, if the Government had met the PIP ceilings since 2001 the PIP constraint on disbursement requirements would have completely eased by 2005. The shortfall would cost the nation at least \$75 million in net project benefits by foregoing these investments<sup>10</sup>.

23. Another major consequence of the shortfalls in spending has been the delays in the release of counterpart funds for ongoing projects causing the building up of payment arrears and project implementation delays. This is adversely affecting potential benefits from development projects and their impact on economic growth and poverty reduction. ADB and the World Bank expressed serious concern on this matter in a joint letter to the Prime Minister in September 2002. This issue was raised in the 2003 CPRM and the Government agreed as part of the action plan<sup>11</sup> (See Attachment 2) to prepare a schedule for repayment of outstanding arrears in counterpart financing. Despite follow-up by ADB and the World Bank, the promised schedule has not been prepared nor the donors were informed on a quarterly basis about the counterpart financing situation.

24. One of the reasons behind the build up of arrears in counterpart funding is the mismatch between the quarterly disbursement ceilings and the heavy seasonality in project spending. Under the IMF's PRGF program, the ceiling on the PIP is being set on an annual basis with intermediate quarterly fiscal deficit targets. Consequently, the MOF monitors disbursements on a quarterly basis. These targets are fixed purely to limit the disbursements to meet the fiscal deficit benchmarks without taking into consideration the schedule of payments as determined by implementation timetable and strong seasonality in construction activities. Monitoring on quarterly basis is unnecessary and counterproductive as it would lead to building up of arrears and untimely release of funds which are major causes of project implementation delays. In particular, the impact of the untimely release of funds would be more pronounced in the Kyrgyz Republic because the construction period is short due to severe winters and could result in delays of one full year. This is also contrary to the GOSCOMINVEST decree (No 11) issued on July 24<sup>th</sup> 2002 which drew up an action plan to ensure adequate provision of counterpart funding in a timely manner without quarterly ceilings. This decree has also provided freedom to executing agencies to reallocate funds from one approved category to another within their approved PIP ceiling without prior permission of MOF. **CPRM will inform the Government about the adverse economic consequences of shortfalls in development spending. CPRM will press for the implementation of GOSCOMINVEST decree on timely release of funds without**

<sup>9</sup> The shortfall in 2001 was 22% on a PIP ceiling of \$84.7 million, in 2002 it was 8% against the permitted spending level of \$84 million. The shortfall was a massive 20% in 2003 as the Government spent only \$65.5 million on PIP as against a ceiling of \$82 million. Evidently, these shortfalls have occurred due to higher demands for current expenditure which the Government found inexpedient to compress.

<sup>10</sup> In net present value terms assuming a minimum economic internal rate of return of 12%.

<sup>11</sup> Action Plan of the Government of the Kyrgyz Republic for Elimination of Obstacles for Implementation of Projects Funded by the WB and the ADB (Approved by GOSCOMINVEST vide resolution NO. 12 dated 4 November 2003).

quarterly ceilings. The Mission will also bring to the notice of the Government about the delays in preparing the repayment schedule as agreed during the last years CPRM.

**b. Institutional Capacity and Deficiencies in Administrative and Implementation Structure**

25. The seasonality in construction creates a mismatch in the time profile of revenue and capital expenditure flows and puts considerable pressure on Government cash flows. Managing this requires a good fiscal and project management system to make information available on timely basis for effective planning. The fiscal reporting system of the Government at present is not amenable for proper cash flow planning both by the MOF and the line ministries. The present system facilitates submission of project financing requirements and its time profile at the time of preparation of the annual budget and does not easily lend itself to revision of expenditure requirements periodically during the year to reflect the actual pace of execution of projects. A comprehensive project management and aid coordination information system is being developed under an ADB technical assistance<sup>12</sup> to the MOF to streamline the Government's management information system relating to externally-aided projects and build capacity within MOF and the line ministries in project management and implementation. The project has developed monthly and quarterly reporting systems to collect information from different PIUs in line ministries for transmission to MOF. The TA also provided training to the PIU and line ministry staff on the basics of project management and monitoring. The GOSCOMINVEST endorsed the information system and the forms for collecting information on monthly and quarterly basis. **CPRM will request the Government to take steps to strengthen the project monitoring units in the line ministries to collect information from PIUs for their and MOF's use. The project management and aid coordination system should be made an integral part of the budgetary process to improve fiscal planning.**

26. At present there is no nodal unit exclusively and independently accountable for ensuring efficient implementation of externally-aided projects. Ideally, such a nodal unit should be created within the MOF to ensure that donor funds are effectively spent and project benefits are not eroded by poor portfolio management. This is particularly important because poor portfolio performance would impact adversely on country portfolio performance assessment, which could in turn lead to reduced allocation of ADF, IDA, and other highly concessional resources and their grant components. The absence of such a unit is evident from the non-accomplishment of many key actions agreed last year to eliminate impediments to project implementation. **The Mission will, therefore, request the Government to strengthen the portfolio management capacity within MOF and make it accountable for portfolio performance in general and for implementing the action plans agreed during the CPRM in particular.**

**c. Problems arising from the lack of Understanding and Experience with Policies and Procedures of External-Aid Agencies**

27. **Taxation of Project Purchases.** The TA framework agreement with the Government of Kyrgyz Republic and the loan agreements stipulate that ADB funds cannot be used for payment of local taxes and duties and the same should be born by the Government. The Government provides counterpart financing in the form of exemption of taxes. In the case of procurement under TAs, taxes are exempted. However, problems are

<sup>12</sup> TA 3996 –KGZ: Strengthening Capacity in the Government to Manage Externally-Assisted Projects. The consultants were fielded in May 2003.

being encountered by both TA and loan projects in complying with ADB rules pertaining to taxation. This is due to the fact that ADB TA projects are not included in the list of projects eligible for zero rating of VAT. In the case of loans, PIUs report two problems: (i) difficulties in obtaining VAT exemption, (ii) ambiguity in the computation of Government co-financing which is usually provided in the form of tax exemption, and (iii) ambiguities in the procedure for taxation of consultants (local as well as foreign) hired under loan projects.

28. The MOF administers tax exemption in two ways. First, through an annual notification, it announces the procedure to be followed for availing VAT and customs duty exemption for goods and services procured under donor-funded project. The notification also includes a list of projects eligible for tax-free purchase of goods<sup>13</sup> which are generally grant-funded projects. Yet ADB TAs projects are not included in these lists in spite of raising this issue during the previous CPRM. Second, in the case of projects that are not included in the notification, the MOF issues letters of authorization to enable PIUs purchase goods with VAT exemption on a case by case basis. This procedure, besides causing delay associated with obtaining the necessary tax exemption letters, is not working well because a number of key suppliers are refusing to supply goods with VAT exemption based on such letters. For the reasons elaborated in para 29 below, suppliers' reluctance is due to the fact that the tax exemption letter will not allow them to claim refund of VAT they already paid on their purchases of inputs and raw materials. This creates problems to civil works contractors. If the project purchases are made gross of tax, the contractor will find it difficult to get refund from the Government.

29. The MOF is providing only VAT "exemption", as written in most tax exemption agreements with donors and international agencies instead of "zero rating" which removes all taxation from the price of a good. VAT exemption procedure distinguishes between "exempted goods" and "zero rated goods". When donor purchases are only "exempted" from VAT, suppliers will not be eligible for refund of VAT they paid on their purchases connected with the supply of the good / service and will be obliged to charge higher prices to accommodate the tax they had paid on inputs. This makes it difficult for donors to determine tax element in project purchases to exclude the same from their financing. However, when donor purchases are "zero rated", the suppliers get refund of taxes paid by them on their purchases connected with the goods supplied to donors and can supply at competitive prices.

30. Besides causing difficulties to donors in determining the tax element in the project purchases, the policy is detrimental to the development domestic business. Since most countries "zero rate" their exports, this policy will put domestic suppliers/producers at a disadvantage when the procurement is under ICB. Even in the case of domestic procurement, in Kyrgyzstan this policy is most likely to encourage trade diversion because the international borders are quite close to the important economic centers like Bishkek city and Fergana valley. Thus, the current taxation policy besides causing project implementation difficulties, will create an incentive to import goods/services instead of sourcing them locally and could cause considerable loss to the economy. This issue was brought to the attention of the Government in joint letter in June 2003 by the World Bank and ADB and will also be raised during the CPRM.

31. The MOF was also asked to issue clear guidelines on the procedure for taxation of consultants funded under loan projects. The actions agreed for resolving this issue were not implemented purportedly. **CPRM will raise this issue with the Government and seek its assistance to put in place interim measures to mitigate the problem until the new tax code is brought into force.**

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<sup>13</sup> The most recent notification was issued on 12 March 2004 - Notification No. 15-3-11/22136 in the place of the previous notification No. 15-3-11/2487 dated 9 April 2003.

32. **Disbursement Delays.** A number of PIUs have reported considerable delays in processing their disbursement applications by the MOF and ADB. Such delays cause considerable financial hardship to contractors due to the high cost of funds and could eventually reflect as higher bid prices. A number of factors are responsible for these delays most of which are managerial and hence should be solved as soon as possible. The first source of delay is at the MOF which tends to accumulate claims till the beginning of the following quarter after hitting the quarterly disbursement ceiling. This could be avoided by dispensing with the quarterly ceiling on disbursements. The second source of delay is in ADB which is arising due to two factors: submission of incomplete and/or inaccurately prepared withdrawal applications (WAs), incomplete supporting documents, and communication delays due to remoteness of the country and low reliability of means of communication. Of these three factors, training in ADB procedures could minimize submission of incomplete and/or inaccurate WA, but cannot address the remaining two problems. **Pre-screening of WA at the resident mission could mitigate this problem in a cost effective manner. Since project administration is being transferred to KYRM in a phased manner, pre-screening of WA may be assigned to the resident mission on an experimental basis in 2005.**

### C. Portfolio Performance Analysis

33. ADB's standardized evaluation approach uses a combination of quantitative performance indicators and qualitative analysis of inputs, processes, and outputs. Standardization allows comparison of portfolio performance across projects as well as across borrowing member countries. This approach breaks down the analysis into (i) start-up performance; (ii) financial performance; and (iii) portfolio performance and supervision (see Appendix 5 for a summary of these performance indicators).

#### a. Start-up Performance

34. Three indicators are used to measure start-up performance, viz., the time taken for (i) loan effectiveness, (ii) establishing project implementation office, and (iii) recruiting consultants. The first two are analyzed by comparing actual and projected dates, and the last is measured by the time taken from project approval until the signing of the first consultant contract. Appendix 5 summarizes the start-up indicators for all 13 ongoing loans.

#### Loan Effectiveness

35. The average time taken for approval to loan effectiveness for the ongoing 13 loans was 6.9 months which is one month less than ADB average in 2003 of 7.9 months. The time taken for loan signing after approval was 3.6 months, almost the same as ADB average, but the time from loan signing to loan effectiveness was shorter. This indicates that the Kyrgyz loans are comparatively better planned in terms of detailed project scope, preparation of bidding documents, establishment of project implementation units, and compliance with conditions for loan effectivity. The average would have been even better but for the inordinate delay in the effectivity of Loan No 1775 for the Almaty-Bishkek Regional Road Rehabilitation. This loan took 19.0 months to become effective due to the delay in the ratification of the cross boarder agreement between the Kyrgyz Republic and Kazakhstan by the Kazakh Parliament. The effectivity of Loan 1855: Third Road Rehabilitation was delayed by 10.4 months due to the time taken to resolve the loan covenant on the establishment of a road fund which was in conflict with the conditions of IMF's PRGF program.

## **Establishment of Project Implementation Offices and Recruitment of Consultants**

36. Timely establishment of project implementation offices and recruitment of consultants is the first step in smooth implementation of projects. Consultants were hired in 10 projects of which one project in the past experience delays in recruiting consultants. These delays are often caused by the lack of familiarity with both Government and ADB guidelines, and the lack of experience in preparing invitation documents, evaluation criteria, and assessment of proposals. Another major problem was the delay in hiring local consultants again due to the lack of familiarity with ADB guidelines. Besides, inadequate staffing of PIUs and high turnover of staff continue to cause concern. Currently, this problem is manifesting in the Emergency Rehabilitation Project, where the delay in hiring local consultants is preventing the Government from efficient use of retroactive financing and taking advance procurement action. **CPRM will request the Government to take time-bound action to resolve this issue.**

### **b. Financial Performance**

37. Four indicators are used to measure financial performance: contract award ratio, disbursement ratio, imprest fund turnover, and timely submission of audited accounts.

#### **Contract Award Ratio and Other Indicators of Procurement Performance**

38. The contract award ratio is a comprehensive indicator to gauge physical progress in project implementation. This ratio is influenced by structural factors beyond the control of executing agencies and ADB, and poor implementation performance. For instance, this ratio tends to be low when the portfolio is young, and in the cases where the loans comprise of a large number of small sub-projects, or involve community mobilization/participation as in some social sector projects. Therefore, while analyzing this ratio one has to examine both these factors. The contracts award ratio (with program loans) increased from 13.3 in 2002 to 31.4 in 2003 but now has decreased to 14.7 in 2004. Excluding the program loans, this ratio was even more impressive, showing growth from 10.8% in 2002 to 38.1% and 17.5% in 2003 and 2004 respectively, which is much higher than the ADB's average of 14.6% and 10.5% for those respective years. Resolution of start up problems in several projects in the road and the social sectors accelerated their implementation and helped improve the contract award ratio. Aggregate contract awards (without program loans) reached \$51 million in 2003, about 209% percent of target (details at Appendix 7).

39. Aggregate contract awards (excluding program loans) are projected at a modest \$16.7 million in 2004 of this 88% has been accomplished by end-August 2004. The average delay in contract awards fell marginally from 9.8 months in 2003 to 9.3 months by end-August 2004. The lack of knowledge and familiarity of the executing agencies with the ADB procurement procedures as well as the low capacity of implementing agencies are the primary causes of procurement delays. Implementing agencies, particularly senior staff who constitutes members of tender committees in ministries, often do not understand ADB procedures and mix up with Government policies to support locally (oblast) based firms and to support national firms over foreign ones. This also leads to intrusive interference in procurement particularly by senior staff. The frequent changes in PIU staff is also a contributing factor<sup>14</sup>. **Contract award performance needs to be maintained by promoting greater awareness of ADB procedures among the executing agencies and addressing**

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<sup>14</sup> For example: In Loan No 1555 for the Education Development Sector Project there have been 4 changes of PIU Manager, seven changes of Project Director and 2 changes of Financial Officer.

**the high turnover of senior staff at PIUs. Simultaneously, there is a greater need to educate people about the virtues of community-based ownership and management of local assets to overcome the difficulties faced in social projects<sup>15</sup>.**

### **Loan Disbursement**

40. The disbursement performance continues to be tardy (details in Appendixes 3 and 8). The disbursement ratio (with program loans) was 15.7% in 2003 as against the ADB average of 20.2%. A 26% shortfall in accomplishing disbursement target was the main cause of low disbursement ratio. Prognosis for 2004 is better than last year as the Government has been able to accomplish 62% of the year's target of \$60.2 million. Disbursement ratio excluding program loans fell from 18.7% in 2003 to 12.6% in 2004. Preliminary trends for the first half of 2004 show slack disbursement performance in project loans, particularly in the road sector. Compression of PIP and the shortfall in public investment spending are the main contributing factor for the setback in disbursement performance. To be specific, serious problems in providing counterpart financing in a timely manner is the major project implementation issue. Arrears in counterpart funds continues to be a major problem particularly in the road sector. The Government repeatedly failed to comply with the agreed arrear payment schedules since February 2002 and did not prepare a schedule for payment of arrears as agreed during the 2003 CPRM. The payment arrears also contributed to delays in procurement of winter maintenance equipment, almost by one year, necessitating a second extension of the loan closing date of the Second Roads Rehabilitation Project (Loan 1630-KGZ) from 30 April 2002 to 30 October 2003, and, subsequently, a third extension to 31 October 2004. Now the Third Road Rehabilitation Project faces similar problems of arrears in payments to contractors which the Government addressed recently. Loan 1645 –KGZ: Social Services Delivery and Financing project continues encountering problems in counterpart financing. Though arrears could be small in magnitude, its impact on project implementation delays is considerable because the contractors involved are small entrepreneurs with weak financial endurance capacity. While the improvement in contract award performance may contribute to improved disbursement performance, the likelihood of PIP financing difficulties, delays in the resolution of taxation issue, delays in processing disbursement applications could have an adverse impact on disbursement ratio in 2005. **Portfolio disbursement performance could be improved if the Government could show some flexibility in PIP spending, and expeditiously resolves the problem of taxation of project purchases as envisaged in the relevant GOSCOMINVEST resolutions.**

### **Imprest Accounts**

41. Since the level of imprest fund balance is set to meet six months funding requirements of a project, ideally the imprest fund turnover ratio should be 2. The turnover ratio increased from 1.8 in 2002 to 3.5 in 2003 (ADB average 1.8). It was 3.3 in 2004 (details in Appendix 9). High turnover ratio could indicate, efficient use of imprest funds by PIUs, lower imprest fund limit, and even the use of imprest fund for unauthorized purposes such as temporarily meeting the counterpart fund requirements as was noticed in some World Bank projects. ADB, the World Bank, and the MOF conducted a joint review of commercial banks to determine their eligibility to hold imprest/special accounts. Results of the study are awaited. **Project review missions need to investigate the reasons for high imprest fund turnover and may consider raising the ceiling if warranted .**

### **Submission of Audited Accounts**

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<sup>15</sup> Loan 1742-KGZ: Community-Based Infrastructure Services Sector, and Loan 1645-KGZ: Social Services Delivery and Finance

42. The submission of audited project accounts and agency financial statements (APA/AFS) improved in 2003 but falls short of what can be considered good performance. The submission of audited project accounts by two road projects, Loan 1775: Almaty Bishkek Road; and Loan 1853: Third Road Rehabilitation, is now overdue. The submission of audited financial statements for 2002 by seven new energy companies, under the Loan 1143: Power and District Heating Rehabilitation, is still pending. **CPRM will reiterate the importance ADB attaches to timely submission of APA/AFS and request the Government to take steps necessary to improve the situation.**

### **c. Portfolio Supervision and Performance**

#### **Portfolio Risk Factors**

43. The average supervision intensity measured in terms of staff days per project of 17.8 days in 2003 is lower than ADB wide average of 25.4 days in 2003 (See Appendix 3). Of the 12 project risk factors monitored by ADB, Kyrgyz Republic fared better than ADB-wide average in 7 indicators in 2003. The performance was below average in the case of: establishment of project monitoring units, fielding of consultants, addressing environmental or social problems, shortage of counterpart financing, and disbursement delays. The overall portfolio risk ratio<sup>16</sup> of 10.4% is better than ADB wide average of 13.2% in 2003. Notably, this risk ratio fell sharply from 17.9% in 2001 due to improvement in the timely submission of APA/AFS, better compliance with other covenants, and improved project supervision.

#### **Loan Extension and Change of Scope**

44. Significant delay of 18 months in implementation of Almaty-Bishkek Road Rehabilitation Project (Loan 1775-KGZ) necessitated extension of loan closing date from 30 June 2004 to 31 October 2005. Similarly, the implementation of Third Road Rehabilitation Project is now delayed by 20 months (according to the July 2004 review mission). The EA proposed and the July 2004 review mission supported a request to extend the loan closing date from 30 April 2005 to 31 December 2006. The Government has requested ADB to extend the loan closing date of Loan 1529-KGZ: Rural Financial Institutions by two years from 30 September 2004 until December 2006 as the credit line component is still underutilized. ADB agreed to extend the loan closing date until December 2005 provided: (i) additional measures are taken to ensure satisfactory performance of apex union, and (ii) a partial reallocation of loan proceeds is made to support capacity building in the National Bank of Kyrgyz Republic for supervision of credit unions created under the project.

### **D. Sector Policy Issues and Compliance with Loan Covenants**

45. **Transport and Communications Sector.** A number of important policy issues are outstanding. The Government will have to establish of an effective and sustainable road maintenance system. This requires: (i) development of sustainable financing system for the sub-sector; (iii) prioritization of road maintenance, and (ii) commercialization of the sector. To address these issues, the Automobile Road Act and the Law on the Road Fund have been enacted. The Road Fund has been established but could not be operationalized due to IMF conditionalities. In lieu of this, sufficient level of budgetary allocations for road maintenance was agreed upon. But the government is experiencing serious difficulties for complying with financial loan covenants under the Third Road Rehabilitation Project (Loan

<sup>16</sup> Weighted average of 12 risk factor.

1853-KGZ) on the level of road maintenance financing. The first contracts for road maintenance was awarded in December 2001. But the progress in commercialization of road maintenance is slow and need to be carefully monitored. The Government needs to prioritize maintenance of roads and focus on strategically important roads. Further, institutional reforms need to be initiated to gradually raise funds for road maintenance from users. The law to impose user charges on heavy trucks has been approved by Parliament.

46. **Agriculture.** Implementation of Loan 1726-KGZ: Agricultural Area Development Project is being affected by non-compliance with environmental and social loan covenants and insufficient allocation resources for project implementation.

47. **Water Supply and Sanitation.** The pace of implementation of Loan 1742-KGZ: Community Based Infrastructure Services Sector Project has improved. The executing agency (EA) is taking active measures to have an integrated approach to project implementation. EA is also actively pursuing cost recovery and community mobilization of resources through continuous dialogue with the local leadership and oblast administration. However, the project steering committee has to become more active and involve other sectoral agencies in the implementation of the project. The project faces problem due to insufficient annual PIP allocations, which may stretch its implementation period.

48. **Rural Financial Institutions.** The loan agreement was amended to enforce stricter performance requirements and prudential norms for the credit unions (CUs). Specific measures have been taken to: (i) introduce new capital adequacy norms, a minimum capital requirement, and maximum borrowing limits, (ii) revise criteria for CUs to participate in the project, (iii) develop a strategic plan for the sustainability of the Financial Company for the Support and Development of Credit Unions (FCCU), and (iv) promote savings by CUs. The Government requested ADB to consider lowering the interest rate charged to FCCU and extend the loan period by 24 months. ADB, in principle, agreed to extend the loan till 31 December 2005 provided: (i) additional measures are taken to ensure satisfactory performance of FCCU, and (ii) a partial reallocation of loan proceeds to support capacity building in the National Bank of Kyrgyz Republic for supervision of savings and credit unions. A decrease in the interest rate charged to FCCU will be considered after the performance of FCCU reaches an accepted level. A review mission is planned during November 2004, to assess the performance of FCCU, determine the size of reallocation needed for capacity building in NBKR, and determine any other measures necessary to strengthen the CUs.

49. **Education.** Sector reforms are hindered by inadequacies in institutional capacity in the Ministry of Education (MOE). The existing policy and planning framework [Bilim Program (1996) and Education Training Master Plan (1996)] require revisions to reflect the need for: (i) greater private sector participation, (ii) mobilization of alternative financial sources, and (iii) decentralization of education management and administration. The issues of sustainability of the existing education system, low teacher pay and motivation, and poor quality of education also require urgent attention. While MOE is focused on addressing quantitative targets like textbooks and school equipment, greater emphasis also should be placed on improving qualitative aspect of educational system. From 2002, the performance of education sector project has improved notably. On MOE's initiative, the International Advisory Council on Education was established in 2003. The role of this Council will become important since the World Bank will also be providing significant support to the sector. This is expected to further improve donor coordination project implementation in the sector. The TA for developing Third Education Project has been commenced in 2004. The TA outputs will serve as a road map for other donors actively involved in the sector.

50. **Social Services Delivery and Finance.** Supplementary budgetary resource allocation to cover the incremental recurrent costs of the project need to be made. Such allocations shall not displace annual budgetary share for capital expenditures and

operational and maintenance expenditures in the health and education sectors. This project also suffers from outstanding arrears of counterpart funding.

51. **Corporate Governance and Enterprise Reforms (CGERP II).** The release of second tranche of the CGERP II of US\$17.5 million was originally scheduled for October 2003 but was delayed due to pending actions. The Government carried out bankruptcy procedures for two public sector companies and achieved satisfactory resolution of six financially and organizationally weak companies. The Parliament had approved amendments to the Law on Joint Stock Companies that are crucial for effectively enforcing corporate governance standards. Following these actions, the Government fully complied with all 8 final tranche release conditions. The tranche was released on 20 August 2004.

#### **Compliance with Loan Covenants.**

52. Five of the 13 ongoing projects complied with all covenants. Of the remaining eight, the status of compliance is satisfactory for seven and partially satisfactory for one – Loan 1630-KGZ: Second Road Rehabilitation Project. This loan is substantially complete and the status of compliance with sector policy covenants is deficient. A review of compliance with loan covenants of individual projects is at Attachment 1.

#### **IV. EVALUATION OF ACTION PLANS 2003**

53. The 2003 CPRM prepared two action plans; one to address common problems faced by ADB and World Bank and the other to address the project-specific problems faced by ADB-financed projects. The joint review identified 35 actions to address 11 common problems affecting the portfolios of ADB and WB. The Government complied with 14 actions, partially complied with 3, is complying with 4, did not comply with 10, and the status of compliance was not known for 4 (see Attachment 2 for status of compliance with the joint action plan). The non-complied actions are mainly in three areas: (i) provision of timely information by PIUs to the MOF regarding their financing plans, counterpart funds requirement, and status of arrears in payment; (ii) taxation; and (iii) rationalizing the intrusive and frequent PIU inspections by the Chamber of Accounts.

54. The project-specific action plan contains 33 actions to improve performance of 10 loans in ADB portfolio. Of these, 11 actions are related to loan covenants. As of end-September 2004, the Government fully complied with 22, partially complied with two, not complied with five, and compliance is underway for the remaining four. Most of the non-complied actions relate to financial loan covenants (Status of compliance with project specific action plan at Attachment 3).

55. Overall compliance with the joint action plan is mixed where as that of project-specific action plan is generally satisfactory

### Non-compliance of loan covenants in specific loans

**Loan 1529: Rural Financial Institutions Project** - Overall compliance is mixed as the following four loan covenants were either partly or not complied with:

- *FCSCU shall be responsible for determining whether a CU is eligible for participation in the Project on the basis of the criteria specified below [in (b)] and for monitoring performance of participating CUs with respect to such criteria and the use of Project funds. LA, Schedule 5, para. 5 (a).* FCCU findings on fraud in 21 credit unions were referred to prosecutors in 2002. Some individuals have been convicted already, but most cases are still pending. FCCU has strengthened licensing procedures and capital requirements for SCUs. FCCU has also shared its findings with ADB's Anticorruption Unit, which has ensured ADB completeness of administrative procedures regarding corruption and fraud. More recently, an NBKR on-site inspection found that FCCU had not been in compliance with regulations limiting single borrower exposure for a long time, and had not monitored credit performance adequately. **Partly complied with.**
- *The CUs shall make subloans to Sub-borrowers at market rates to be determined by the credit committee of each CU under the guidance of NBKR and FCSCU [LA, Schedule 5, para. 7 (a)].* Many credit unions continue to lend at rates that do not seem to be in line with market rates. Interest rates for SCU credits can diverge by as much as 18 percentage points across loans to customers in the same sector but different region. The same applies to customers in different sectors of the same region. It is not clear what level of guidance is given on loan pricing from FCCU and NBKR. However, efforts are being made by the GTZ project team to introduce more appropriate loan pricing procedures. **Not complied with.**
- *The CUs shall be required to report monthly to FCSCU, including financial statements, subloan classification, size and number, and size of member contributions. FCSCU staff shall regularly visit CUs to advise on managerial, procedural and financial matters, with the frequency of visits declining as CUs mature [LA, Schedule 5, para. 9 (c)].* The reporting is improving but accounting and management skills remain weak, which make reports unreliable. FCSCU capacity is still weak. An inventory of FCCU's loan documentation undertaken in October 2004 found that the documentation is – in part – missing. The new management of FCCU has dismissed responsible senior managers of FCCU. **Partly complied with.**
- *The draft Law on Credit Unions shall, among others, provide for: (i) mature CUs being allowed to accept savings deposits from their members; (ii) CUs being exempt from taxes as non-profit organizations; and (iii) a comprehensive framework for a credit union system, including an apex union [Loan Agreement, Schedule 5, para. 13(b)].* The current version of the law does not clearly provide the comprehensive framework for the credit union system, including an apex union. **Partly complied with.**

**Loan 1547: Capacity Building in Corporate Governance and Insolvency** - complied with loan covenants, which are due.

**Loan 1555: Education Sector Development Project** – one loan covenant on out-of-country training is not complied with. Since the Government was unwilling to utilize loan proceeds for international training of educational staff, these activities have been cancelled. However, pilot programs for in-country staff development were conducted on schedule. Project implementation was completed on 30 June 2004.

**Loan 1630: Second Road Rehabilitation Project** – Overall compliance was satisfactory, but the compliance with sector policy covenants was only partially satisfactory. Of the six loan covenants, five are complied with late and one is partially complied with.

- The late and partially complied with sector policy covenants refers to: (i) reassignment responsibilities between MOTC and Ministry of Architecture and Construction, and between the Vehicle Inspection Department and Ministry of Interior; (ii) strengthening of Bishkek-Osh road maintenance system; (iii) facilitation of private sector participation in road maintenance; (iv) development of a time-bound road safety program; (v) establishment of equipment pools; and (vi) establishment of a project benefits monitoring system.

**Loan 1645: Social Services Delivery and Finance Project** - Complied with all loan covenants, which are due.

**Loan 1726: Agriculture Area Development Project** – Unsatisfactory compliance with environmental and partly satisfactory compliance with social loan covenants.

- Three of total six environmental loan covenants are not complied with. The not complied loan covenants require monitoring of drainage and water logging problems, water quality and flow in Chui River, and also monitoring of the salinity, nitrates, and nitrates in the ground water.
- One of the two social loan covenants, requiring that women farmers are to be given full opportunity to participate in all project activities and report on such activities, is not complied with.

**Loan 1742: Community Based Infrastructure Services Sector Project** - Overall compliance is satisfactory. Out of 37 loan covenants eight are complied with and compliance with remaining 29 is underway.

**Loan 1775: Almaty-Bishkek Road Rehabilitation** - Overall compliance was satisfactory. Out of twenty loan covenants three are complied with, two are complied with late, eight are being complied with and seven are not yet due.

- An important loan covenant relating to signing of cross border agreement was accomplished after considerable delay which has resulted in considerable implementation delays.

**Loan 1853: Third Road Rehabilitation Project** - Overall compliance was satisfactory except for compliance with financial loan covenants.

- The Government constantly failed to comply with the financial covenant on raising the level for road maintenance financing to adequate levels, particularly, for the maintenance of federally administered roads.

**Loan 1860: Corporate Governance and Enterprise Reform Program-II.** The final tranche was released on 20 August 2004 after a delay of about 10 months. The release was held up pending compliance with two of the eight final tranche release conditions.

**Loan 1926: Trade Facilitation and Customs Cooperation Program** – All loan covenants for second and final tranche release were complied with and the tranche was released on 17 September 2004 after two months delay.

**Loan 2007: Community Based Early Childhood Development project** - Complied with all loan covenants that are due.

**Loan 2045: Emergency Rehabilitation Project** – A new project, compliance with loan covenants is underway.

Approved by:  
Resolution of GOSCOMINVEST  
Dated 4 November 2003. No. 12

**Action Plan of the Government of the Kyrgyz Republic for Elimination of Obstacles for  
Implementation of Projects Funded by the WB and the ADB**

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
	Allocation of counterpart funding and PIP funds by the Government of the Kyrgyz Republic	<p>Each year PIUs shall submit updated financial plans indicating the requirements in PIP funding and counterpart funds that will be used by the Ministry of Finance for allocating PIP funds and counterpart funds.</p> <p>Hold quarterly meetings with PIUs and the Executing Agencies for considering the status of utilization of allocated PIP funds and counterpart funds and bring annual plans in compliance accordingly. Revise and reallocate jointly with PIUs and the Executing Agencies their needs in counterpart funding for 2003. Ensure full utilization of allocated funds of external financing under PIP</p> <p>Ensure timely cofinancing of projects.</p> <p>Prepare a schedule for repayment of outstanding arrears in cofinancing</p>	<p>MF, PIUs, the Executing Agencies</p> <p>PIUs, the Executing Agencies</p> <p>MF, PIUs, the Executing Agencies</p> <p>MF, PIUs</p> <p>MF</p> <p>MF</p>	<p>According to the budget process, before the budget approval</p> <p>Every quarter</p> <p>By 1 December 2003</p> <p>Regularly</p> <p>Regularly</p> <p>By 1 December 2003</p>	<p><i>Being implemented</i></p> <p><i>Being held</i></p> <p><i>Being implemented</i></p> <p><i>Being implemented</i></p> <p><i>Being implemented</i></p> <p>Due to unforeseeable expenditures of the Government of the Kyrgyz Republic related to</p>	<p>Complied with</p> <p>Complied with</p> <p>Partially complied with</p> <p>Not complied with</p> <p>Not complied with</p> <p>Not complied with</p>

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
		Provide information on project cofinancing situation to donors on a quarterly basis	MF	On a quarterly basis	consequences of natural calamities in the Kyrgyz Republic, and also to uneven level of revenues collections to the budget and untimely receipt of program loans and grants, at present it is not possible to elaborate and further implement the schedule of repayment of the arrears on cofinancing of investment projects of PIP <i>Ministry of Finance of the Kyrgyz Republic is continually working on repayment of the accrued arrears on cofinancing and makes all possible efforts to ensure normal activity of PIP projects</i>	Not complied with
	Fulfillment of procedures of procurement of goods, works and services of a financing institution	Senior officials involved in procurement process must follow procedures of procurement of goods, works and services of a financing institution  Use only standard bidding documents of a financing institution	Heads of the Executing Agencies  PIUs, the Executing Agencies	Regularly  Regularly	  <i>As for the above mentioned subparagraphs,</i>	Complied with  Complied with

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
		<p>Stringently follow procedures of a financing institute for procurement of goods, works and service</p> <p>Introduce changes to bidding documents and other procurement documents only having agreed them with the financing institution</p> <p>Ensure openness in conducting all tenders and publication of announcements about the winners of all tenders</p> <p>Maintain accurate and updated records on procurement for further control</p> <p>Conduct workshops in procurement procedures for improving the knowledge of senior officials, staff of the Executing Agencies, PIUs and domestic consulting companies, contractors and suppliers.</p> <p>Study the possibilities for establishing an efficient procurement system</p>	<p>PIUs, the Executing Agencies</p> <p>PIUs, the Executing Agencies</p> <p>PIUs, the Executing Agencies</p> <p>PIUs, the Executing Agencies WB, ADB</p> <p>MF</p>	<p>Regularly</p> <p>Regularly</p> <p>Regularly</p> <p>Regularly</p> <p>4<sup>th</sup> quarter of 2003, and 2004</p> <p>4<sup>th</sup> quarter of 2003</p>	<p><i>Practically all PIUs observe donor' procedures</i></p> <p><i>WB conducted seminars in October 2003, and a regional seminar in June 2004, ADB conducted a workshop in June 2004. The Working Group at present has prepared a draft Strategy on Harmonization. Some of the directions of the Strategy are: 1) Harmonization of financial management; 2) Harmonization of procurement procedures; 3) Harmonization of PIUs</i></p>	<p>Complied with</p> <p>Complied with</p> <p>Compliance status is unknown</p> <p>Compliance status is unknown Complied with</p> <p>Complied with</p>

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
					<i>and project implementation groups.</i>	
	Civil works	<p>Ensure satisfactory quality of civil works.</p> <p>Ensure compliance with civil work schedules taking into account the procedures of approval and contract awards</p>	<p>PIUs, the Executing Agencies, State Commission on Architecture and Construction</p> <p>PIUs, the Executing Agencies, WB, ADB</p>	<p>Regularly</p> <p>Regularly</p>	<p><i>Not all the projects observe the work schedules. Big delays on completion of civil works are in such projects as emergency project, irrigation systems rehabilitation project, on-farm irrigation project, Clean water</i></p>	<p>Being complied with</p> <p>Being complied with</p>

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
		<p>Ensure qualified supervision of civil works and execution of contracts.</p> <p>Prepare final report on implementation of above sub-paragraphs of this para.</p>	<p>PIUs, the Executing Agencies, State Commission on Architecture and Construction</p> <p>MF, State Com. On Architecture and Construction, the Executing Agencies, PIUs</p>	<p>Regularly</p> <p>One month prior to the next portfolio review in 2004</p>	<p><i>Necessary personnel are being engaged for projects where civil work are carried out. In addition: In compliance with the Resolution No. 338 of May 4, 2004 it is mandatory for all the executive agencies to carry out the state architecture and construction control over the quality of construction of objects implemented with the use of foreign investments.</i></p>	<p>Being complied with</p> <p>Not complied with</p>
	Lack of competition while conducting small value procurement	<p>Conduct a market research under MF's coordination to identify the availability of sufficient number of suppliers.</p> <p>Ensure continuous publication of announcements on small value procurements in national mass media.</p>	<p>MF, the Executing Agencies, PIUs</p> <p>PIUs, the Executing Agencies</p>	<p>4<sup>th</sup> quarter of 2003</p> <p>Regularly</p>	<p><i>Each PIU has a certain database containing information about the key suppliers</i></p> <p><i>Being implemented.</i></p>	<p>Partially complied with</p> <p>Being complied with</p>

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
	Transfer of funds to a special account	Stop the practice of transferring the funds to a special account in the National Bank.	MF	Regularly	<i>Being implemented</i>	Complied with
	Inspections of PIUs activity by controlling bodies	Develop regulations for adjusting relationships between the Government and the Chamber of Accounts on auditing of PIUs	MF, WB, ADB, the Executing agencies, PIUs	Before 31 December 2003	<i>At present the Law "On the Chamber of Accounts of the Kyrgyz Republic" has been adopted. This Law reflects activity of the Chamber of Accounts on the audit of lawful, rational and effective utilization of foreign credits, loans and humanitarian aid received by the Government of the Kyrgyz Republic, and also by economic entities under guarantee of the Government of the Kyrgyz Republic. During consideration of the draft Regulations the Ministry of Finance raised an issue of limitation of the number of inspections of PIUs by the Chamber of Accounts. In addition the Ministry</i>	Not complied with

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
					<i>of Finance sent a letter to the Chamber of Accounts with request to stipulate in the new draft law for the number of inspections of PIUs not more than once a year.</i>	
	External Aid Coordination	Hold meetings with donors not less than once a quarter	MF, the Executing agencies, donors	Every quarter		Not complied with
		Enhance coordination of Ministries and agencies on attraction of external aid	MF, the Executing agencies	Regularly		Compliance status is unknown
		Strengthen the work on harmonization of external aid	MF, the Executing agencies	Regularly	<i>Being implemented. The Working Group on harmonization has prepared the draft Strategy on harmonization.</i>	Partially complied with
	Ensure timely audits of Projects	Appoint auditors in a timely manner and ensure timely submission of audit opinions and reports to financing institutions and the Ministry of Finance.	the Executing agencies, PIUs, MF	Regularly	<i>Being implemented</i>	Partially complied with
		Update and circulate a list of audit firms which comply with requirements of financing institutions.	WB	By 1 October 2003	<i>WB provided the list of auditors</i>	Complied with
	Project monitoring and evaluation	Review the systems of project monitoring and performance evaluation within each particular project and prepare a report	the Executing agencies, PIUs, MF	Before 31 March 2004	<i>ADB TA project "Strengthening the capacity of the Government of the</i>	Complied with

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
					<p><i>Kyrgyz Republic on project monitoring and management of externally assisted projects" is being implemented in the Ministry of Finance. Under this Technical Assistance an information system for monitoring and management of externally assisted projects was established, which was provided to line ministries, agencies and PIUs.</i></p> <p><i>On 20-21 May 2004 a seminar-presentation of the system was held with participation of the line ministries and agencies.</i></p> <p><i>According to the new system the new forms have been developed of quarterly and monthly reporting, which were approved by the Resolution of GOSCOMINVESTdated</i></p>	

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
					<i>25 August 2004, No. 19</i>	
	Issues of taxation	The Government of the KR shall develop an efficient strategy for resolving the issues of taxation of goods, works, services, taking into account various privileges and exemptions.	MF, PIUs	Before 31 March 2004	<i>At present the Ministry of Finance of the Kyrgyz Republic is working on drafting the new version of the Tax Code of the Kyrgyz Republic, which should be completed by the end of the current year. At the same time the work is carried out on bringing into order the taxation of goods, works and services of investment projects of the Public Investment Program. Due to limited time and amount of the work, the Ministry of Finance considers expedient to reconsider the deadline of this issue and to move them to the end September 2004.</i>	Not complied with
		The agreed strategy must be applied uniformly to all projects financed by international organizations and donor countries.	MF, the Executing Agencies, PIUs	Regularly		Not complied with
	Engagement of domestic consultants to the projects financed on a grant basis	Elaborate a clear policy and guidelines, which: comply with rules and procedures of WB and ADB;	MF, WB, ADB	Before 31 March 2004	<i>Being implemented. The Working Group at present has prepared a draft Strategy on Harmonization. Some of the directions of the</i>	Complied with
		comply with operational requirements for ensuring quality of TA				Complied with

No.	Generic issues	Activities	Responsible agency	By when	MOF comments	Status assessment by ADB
		is aimed at further development of domestic consultancy industry			<i>Strategy are: 1) Harmonization of financial management; 2) Harmonization of procurement procedures; 3) Harmonization of PIUs and project implementation groups.</i>	Complied with
	Problem projects	Ensure satisfactory implementation of the projects "Health Sector Reform –II" and Consolidated Structural Adjustment Credit (CSAC) and consider implementation of these projects at GOSCOMINVEST meeting.	MF, EAs, PIUs	By 31 December 2003	<i>Health project was considered in November 2003, CSAC program was considered in February 2004.</i>	Compliance status is unknown

## 2003 Action Plan for Project Specific Issues

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
1.	<b>Loan 1443: Power and District Heating Rehabilitation Project</b>	<p>(i) Delay in the submission of audited accounts of newly established energy companies.</p> <p>(ii) Installation of pipes under District Heating Component.</p> <p>(iii) Fulfilling ADB's conditions for changing the on-lending terms for JSC BDHC to support completion of civil works</p>	<p>(i) the outstanding audited accounts of all seven new energy companies to be submitted to ADB;</p> <p>(ii) commitment letters from the MOF and JSC Bishkek District Heating Company (BDHC) confirming that the freed up capital of \$3.4 million equivalent will be utilized for completing the district heating component</p>	<p>December 2003</p> <p>15 October 2003</p>	<p>MOF / Bishkek District Heating Company (BDHC)</p> <p>MOF / BDHC</p>	<p><b>Partially complied with</b></p> <p>On 31 March MOF sent the following audit reports to KYRM :</p> <p>1) Auditor's report of the JSC KyrgyzEnergO for 2000 (in Russian);</p> <p>2) Auditor's report of the JSC VostokElectro for 2002 (in Russian and English);</p> <p>3) Auditor's report of the JSC Electric Power Stations for 2002 (in Russian);</p> <p>4) Auditor's report of the JSC SeverElectro for 2002 (in Russian);</p> <p>5) Auditor's report of the JSC Bishkek District Heating Company for 2002 (in Russian and English).</p> <p>Submission of English versions of the above AFSS of JCS KyrgyzEnergO for 2000, JCS Electric Power Stations for 2002 and Severlectro for 2002 is still pending</p> <p>Submission of AFS for (i) JSC National Grid of Kyrgyzstan, (ii) JSCs OshElectro, and (iii) JSC JalalabadElectro for 2002, is also pending.</p> <p>MOF requested and ADB disagreed to provide assistance for translating pending AFSS into English.</p> <p>Submission of audit reports in English is pending</p> <p><b>Complied with</b></p> <p>Commitment letter has been submitted on 24.11.03</p>

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
			(iii) detailed time schedule and cost estimate for outstanding works, showing that the Project will be completed by 2008	15 October 2003	BDHC / MOF	<b>Complied with</b> Implementation schedule and cost estimates have been submitted to the review mission, which visited Bishkek from 13 to 19 November 2003
2.	<b>Loan 1529: Rural Financial Institutions</b>	(i) Alleged fraud detected in certain credit unions	Government to thoroughly investigate this issue and send detailed report on actions taken to address the fraud issue	Before November 2004 Steering Committee Meeting	NBKR / Finance Company for Support and Development of Credit Unions (FCCU)	<b>Complied with. The issue was discussed at the November 2004 Steering Committee.</b> The next meeting has been scheduled for April 2005. FCCU provides a detailed report on the fraud cases as part of its quarterly reporting. In addition, the FCCU management reports to KYRM CD on the fraud cases on a monthly basis. FCCU findings on fraud in 21 credit unions were referred to prosecutors, who so far have convicted 4 of the 41 individuals of wrongdoing. Cases were brought to the court against management of 18 CUs. Three CUs out of 21 have repaid their debts. FCCU tightened procedures for increasing capital of any credit union, and strengthened licensing procedures. FCCU shared its findings with ADB's Anticorruption Unit, which has ensured ADB completeness of administrative procedures regarding corruption and fraud.

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(ii) Interest rate to be charged to FCCU	(ii) Submit a report to ADB on the interest rate to be charged from MOF to FCCU in consultation with MOF	30 June 2004 (date has been revised on 4/2/04)	NBKR	<b>Complied with.</b> In March 2004, agreement was reached between the Government and ADB that FCCU's performance as measured against the agreed benchmarks will serve as a condition for considering to lower the interest rate charged to FCCU. According to ADB's preliminary calculations, at least three of the four benchmarks have been met. A decrease in the interest rate charged to FCCU will be re-considered as soon as satisfactory performance of FCCU has been ensured. During the review mission in November 2004, measures to ensure satisfactory performance of FCCU and Institutional framework for SCU supervision were discussed. Auditor has provided additional information on FCCU's performance. MOU is to be signed between the Government and ADB to fix all agreements reached. The issue will be discussed at the Steering Committee April 2005.
			ADB to provide comments on the report submitted by NBKR	Following compliance with above item (ii)	ADB	
3.	<b>Loan 1555: Education Sector Development Program (ESDP)</b>	(i) The delays in the fielding of international consultants.	(i) Government and ADB to decide on necessity of fielding of international consultants	(i) End-September 2003	Ministry of Education (MOE)	(i) <b>Complied with.</b> The issue was discussed during the last review mission from 8-16 December 2003. The option of recruiting an international textbook consultant under TA 2879 is being considered by ADB. Since a loan closing date is 30 June 2004, the need for project implementation consultant was dropped.

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(ii) Considerable delays in developing a benefit monitoring system.	(ii) Government to report on the development of a benefit monitoring system	(ii) End-September 2003	MOE	(ii) <b>Complied with.</b> The consultant report was submitted to ADB for comments. Comments have been sent to the consulting firm for finalizing the report. The report has been finalized and approved by the Government and ADB.
		(iii) Due to PIP limitations, the executing agency is unlikely to use all project funds.	(iii) The Government to provide sufficient loan and counterpart funds allocations for 2003 and 2004 to ensure the project utilization by the loan closing date. The Government will take a decision on allocation of additional funds	(iii) September – October 2003	MOF&MOE	(iii) <b>Complied with.</b> No further extension of loan closing date is envisaged. The approved PIP allocation for 2004 and the amount available in the imprest account of were sufficient to cover expenditures. By loan closing date 30 June 2004, the total loan utilization was \$12.1 million. Unutilized loan balance of \$1.8 million was cancelled on 14 June 2004. The loan closed on 30 June 2004.
4.	<b>Loan 1630: Second Road Rehabilitation Project</b>	(i) Implementation of safety measures has been delayed due to the payment arrears to the Contractor. The civil works for \$1 million have been partly rescheduled for 2004.	(i) MOTC will revise the implementation schedule	1 October 2003	MOTC	<b>Complied with</b> The implementation schedule has been revised and agreed with ADB
		(ii) Procurement of winter equipment is delayed due to the payment arrears to the Contractor. Unfavorable exchange rate between the \$ and the Euro prevented EA from signing the contract with supplier	(ii) EA is negotiating with supplier and is optimistic that a satisfactory resolution could be reached.	1 October 2003	MOTC	<b>Complied with</b> Negotiated contract has been signed in late August 2003

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(iii) Due to the above two delays, the amount of US\$ 0.7 million of the total budget of US\$ 5.7 million allocated under PIP for 2003 will not be utilized	(iii) EA and MOF will revise the budget for 2003 and discuss the possibility for reallocating these funds to other ADB-financed projects	1 October 2003	MOF/MOTC	<b>Complied with</b>
5.	<b>Loan 1645: Social Services Delivery and Finance</b>	(i) Integrated management information system for project performance monitoring and evaluation not established as required.	(i) Government to enhance the existing monitoring and evaluation system, in consultation with ADB.	(i) 15 February 2004 (date has been revised on 4/2/04)	MOF	<b>Being complied with.</b> The consulting firm engaged for developing the system has been requested to revise its report. The revised report will be submitted to ADB by December 2004. Meanwhile, the Government uses its own system to monitor project performance, and the outcomes of the consultants work will be incorporated accordingly into the existing monitoring system.

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(ii) Due to PIP limitations, the executing agency is unlikely to utilize all project funds.	(ii) The Government to provide sufficient loan and counterpart funds allocations for 2003 and 2004 to ensure the project utilization by the loan closing date.	(ii) 1 March2004 (date has been revised on 4/2/04)	MOF	<b>Not complied with.</b> The loan closing date has been extended to 31 December 2004. The MOF has allocated \$3.5 million for the project in 2004 PIP which is not sufficient to cover expenditures in 2004. According to the PIU estimation about \$3.9 million is required for 2004. At CPRM review on 4 Feb 2004, it was agreed that MOF would resolve the issue in consultation with PIU. According to MOF the amount will be revised based on 9 months performance results. By 17 November 2004, an undisbursed loan balance was \$613,687.4 of which about \$346,000 is an uncommitted balance after taking out pending claims (\$110,000) and anticipated expenditures of PIU and the consulting company (\$150,000). MOF has to decide on use of the uncommitted balance.
		(iii) There were arrears in payments to contractors due to insufficient counterpart funds release, which may result to delays in delivering works and services.	(iii) The Government to release sufficient counterpart funds to ensure that payments, which are overdue, are paid off.	(iii) 15 March 2004 (date has been revised on 4/2/04)	MOF	<b>Not complied with.</b> Delays in payment of counterpart funds have led to arrears in payments to contractors of <b>Som</b> 6.49 million.. According to MOF, the outstanding amount would be released by the end 2004.
6.	<b>Loan 1726: Agriculture Area Development Project</b>	(i) The EA will give appropriate attention to all components of the project.	The EA will ensure integrated execution of all project components of the project.	Regularly	MAWR PI, Chui Oblast Administration	<b>Being complied with</b> The EA is improving the integrity of project components.

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		Achieving the disbursement target for 2003	The EA will work closely with the supplier to ensure delivery of drainage and irrigation equipment in December. If the delivery is not possible in 2003, reallocate an appropriate amount to the KAFC credit line	15 November 2003	MAWR	<b>Complied with</b> 80% of total payment has been disbursed to the supplier upon shipment of equipment by the end December 2003
7.	<b>Loan 1742: Community Based Infrastructure Sector Services Project</b>	(i) EA needs to pay more attention to community mobilization, cost recovery and institutional capacity building.	(i) EA will strengthen its efforts in community mobilization and cost recovery particularly at community level as this may potentially erode the project benefits. These efforts could be monitored through improvement of community contribution and water tariffs collection.	Regularly	MAWR PI	<b>Being complied with</b>
		(ii) The Steering Committee is not functioning well	(ii) EA, MOF, MOH, KJKS will organize the Steering Committee meeting in September 2003 and ensure its proper functioning on a regular basis thereafter.	September 2003	MOF, MAWR PI, MOH, KJKS	<b>Complied with</b> Steering committee meeting has been held in April 2004.
		(iii) Implementation of sanitation, hygiene and health education and urban water supply and sanitation components are delayed	(iii) The Government will consider the status of implementation of the hygiene and sanitation component and urban water supply and sanitation component and adopt an implementation plan for these components	By January 2004	Goskominvest	<b>Complied with</b> The budget and project implementation plan for 2004 envisage implementation of these components
		(iv) Harmonize the differences between the design standards for water supply systems set by PMU and the national norms	EA and the Government will undertake necessary actions to legalize the project design standards	30 June 2004	MAWR/ Government	<b>Being complied with</b>

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(v) The current disbursement ceiling of US \$4.2 million for 2003 may impede the accelerated implementation of civil works.	The EA and MOF will discuss and agree an increase of disbursement ceiling for 2003	September – October 2003	MAWR PI, MOF	<b>Complied with</b> MOF allocated additional US\$3.3 mln for 2003. On 12 April 2004 EA sent a additional request to Prime Minister to increase the disbursement ceiling up to US\$ 12 mln in 2004.
8.	<b>Loan 1775: Almaty-Bishkek Regional Road Rehabilitation Project</b>	(i) The project implementation is behind schedule due to the delay in ratifying the cross border agreement. Therefore, the loan closing date needs to be revised.	EA will consider submission of request for extending the loan closing date	April 2004	MOTC	<b>Complied with</b> On 14 April ADB approved the request for extending the loan closing date by 16 months from 30 June 2004 to 31 October 2005.
		(ii) The planned disbursements for 2003 of \$2 million may not be achieved in full amount.	The EA and MOF will revise the disbursement plan for 2003	September – October 2003	MOF / MOTC	<b>Complied with</b> MOTC and MOF adjusted disbursement plan for 2003.  The final disbursement was \$0.594 million and did not reached to \$2 million. However, both contracts for civil works has been awarded within 2003. The construction works have been started early 2004.
9.	<b>Loan 1853: Third Road Rehabilitation Project</b>	(i) The budgetary allocation for maintenance of the Bishkek-Osh road has not reached the agreed amount of Som 60 million for 2003	(i) MOF to consider allocation of additional budget for 2003	October 2003	MOF	(i) <b>Complied with</b> Actual disbursement in 2003 reached the amount of Som 83.6 mln, including emergency works in summer 2003.

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		(ii) MOF shall ensure agreed level of budgetary allocation in the amount of Som 80 million for 2004 in accordance with Loan Agreement.	(ii) MOF will ensure the agreed level of budgetary allocation for maintenance of Bishkek-Osh road in the national budget for 2004	In accordance with 2004 budget preparation schedule	MOF	(ii) <b>Partially complied with</b> the amount of Som 40.3 mln has been allocated in the national budget for 2004. Actual financing in 2004 reached the amount of Som 84.47 mln, including special means (MOTC information as of 6.09.04)
		(iii) Contrary to the Loan Agreement, the budgetary allocation for maintenance of other MOTC-administered roads is below the agreed level of Som 196 million for 2003.	(iii) MOF will consider additional budgetary allocation to comply with the Loan Agreement.	October 2003	MOF	(iii) <b>Not complied with</b> Actual allocation for 2003 reached the amount of Som 161.9 mln, including the emergency works in summer.
			MOF will ensure the agreed budgetary allocation in the amount of Som 215.6 million for maintenance of other MOTC administered roads in the national budget for 2004	In accordance with 2004 budget preparation schedule	MOF	(iv) <b>Not complied with</b> The amount of Som 144.7 mln has been allocated in the national budget for 2004. Actual allocation for 2004 reached the amount of Som 177.87 mln, including special means (MOTC information as of 6.09.04)

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
10.	<b>Loan 1860: Corporate Governance and Enterprise Reform Program –II Phase</b>	All eight mandatory conditions for the release of the second tranche were complied with.	<p>Government to undertake the following key outstanding actions to comply with the remaining conditions:</p> <p>(i) to address remaining weaknesses in the Law on Joint Stock Companies enacted in April 2003 and to strengthen enforcement of regulation.</p> <p>(ii) to facilitate adoption of amendments to several laws that protect creditor rights, law on pledges which have been drafted but are pending in Parliament.</p> <p>(iii) to adopt an enterprise restructuring strategy of the Government.</p> <p>(iv) Ministry of Finance has to provide sufficient budgetary provisions as agreed with the loan review mission in August 2003 for employment counseling, retraining, and other active labor market measures, so that the Ministry of Labor can implement these remedial measures for the workers affected by enterprise restructuring.</p> <p>(v) Resolution of at least six weak enterprises</p>	2 <sup>nd</sup> Quarter of 2004	<p>CDC/SCSM</p> <p>MOJ</p> <p>METI/CDC</p> <p>MOF</p> <p>METI/SCSPFI</p>	<p><b>Complied with.</b></p> <p>All second tranche release conditions have been complied with by establishing a corporate governance rating mechanism, strengthening the selection of state representatives in state owned enterprises, enacting auditing and accounting laws in line with international standards, amending regulations to strengthen corporate governance in commercial banks, undertaking a comprehensive review of process related constraints and systemic weaknesses in the judiciary and disseminating the findings, and enacting relevant legislation to allow third-party arbitration and to render judgments of higher courts with finality, enacting legislation on joint stock companies and resolution of financially and organizationally weak companies..</p>

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
11.	<b>Loan 1926: Trade Facilitation and Customs Cooperation Program<sup>17</sup></b>	Timely compliance with conditions for second tranche release	9i) Parliament with approve the new Customs Code (ii) Government will revise the customs regulations in line with new Customs Code and submit drafts to ADB (iii)MOF will develop electronic links between DCS and DTS (iv) DCS will develop and ICT strategy and investment plan (iv) DCS will develop and submit to the Government for approval regulations on customs intermediaries (v) DCS will establish simplified transit procedures	1 July 2004	DCS	<b>Complied with</b> The new Customs Code was approved by Legislative Chamber on 13 April 2004 and by People's Representative Chamber on 13 June 2004, and will become effective on 1 January 2005. The agreed regulations have been revised and submitted to the government for approval . Second tranche has been released on 17 September 2004
12.	<b>Loan 2007: Community Based Early Childhood Development project<sup>1</sup></b>	Insufficient release of Government's counterpart funds in 2004.	MOF will ensure the agreed level of counterpart funding.	By 31 December 2004.	MOF	<b>Not complied with.</b> In 2004, a total amount to be disbursed by the Government was Som 2 million (equivalent to \$0.048million) to the project. However, only Som 1 million of counterpart funds have been released by 17 November 2004.
13.	<b>Loan 2045: Emergency Rehabilitation Project<sup>1</sup></b>	Fulfilling conditions for loan effectiveness:  Delay in hiring consultants.	(i) Establishment of Project Steering Committee, (ii) Appointment of Project Director  MEES/MOTC to hire local consultants immediately after approval advance procurement action and retroactive financing in October 2003	Within 3 months after loan signing  January 2004	Government / MEES  MEES/MOTC/MOF	<b>Complied with late.</b> Delayed by late start of selection process and long discussion between MOF and IAs on remuneration rates for consultants

<sup>17</sup> The section is not a part of originally agreed Action Plan and was inserted by ADB KYRM for monitoring purposes only

NN	Name of Project	Issues/Concerns	Actions(s) Agreed Upon	Target Date	Agency Responsible	Status as of 30.09.04
		Delay in utilizing retroactive financing	MEES / MOTC to submit withdrawal applications for retroactive financing immediately after loan effectiveness	June 2004	MEES/MOTC	<b>Complied with late.</b> Delayed by (i) late submission of necessary documents for existing contracts, (ii) late hiring of local consultants, (iii) pending submission of SIEE and resettlement framework
		Delays in procurement of civil works under advance procurement action	MEES/MOTC to submit draft bidding documents shortly after approval advance procurement action in October 2003	January 2004	MEES/MOTC	<b>Complied with late.</b> Delayed by late hiring of local consultants.

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