

ASIAN DEVELOPMENT BANK

TAR: OTH 36290

TECHNICAL ASSISTANCE

FOR

PROMOTING GOOD GOVERNANCE

IN EAST AND CENTRAL ASIA

August 2002

ABBREVIATIONS

ADB	–	Asian Development Bank
CARs	–	Central Asian republics
DMC	–	developing member countries
ECRD	–	East and Central Asia Department
GA	–	Governance assessment
GDP	–	gross domestic product
IMF	–	International Monetary Fund
LTSF	–	long-term strategic framework
PSA	–	private sector assessment
PSD	–	private sector development
TA	–	technical assistance
TE	–	transition economy

NOTES

- (i) In this report, "\$" refers to US dollars.

I. INTRODUCTION

1. The long-term strategic framework and poverty reduction strategy of the Asian Development Bank (ADB) require ADB to promote socially sustainable development across its member countries. Both documents focus on the need to strengthen governance, promote private sector development, and encourage effective financial management in line with international standards and best practices. To ensure effective operationalization of all its policies and strategies, and Asian Development Fund VIII commitments, ADB is required to undertake country thematic assessments including governance assessments (GA), private sector assessments (PSAs), and financial management studies.

2. The East and Central Asia Department (ECRD) has thus far launched eight thematic studies for selected economies of the Central Asian republics (CARs) and Mongolia (referred to hereafter as transition economies (TEs)).¹ Drawing on this ongoing work and experience gained, this technical assistance (TA)² will focus on conducting the remaining thematic assessments for economies covered by ECRD.³ The TA adopts an integrated approach as it launches assessments in different thematic areas simultaneously to undertake work in a coordinated and coherent manner to draw lessons across the region. Launching integrated work has the benefit of encouraging better interface and debate on common issues, and exploiting synergies between the thematic subject/areas and sharing the experience across the region, while adopting a cost-effective approach to conducting these studies. The thematic studies are designed to take stock of the state of development, issues and constraints, and policy initiatives taken in these areas; and develop an action plan for strengthening governance, the private sector, and financial management. The recommendations of these assessments are to be reflected in ADB's country strategies and operational programs. The TA framework is provided in Appendix 1.

II. ISSUES

3. Over the past decade, the TEs have launched wide-ranging economic reforms to move from centrally planned to market-based systems. Given their contiguous geographic grouping, the TEs have a common political and economic heritage, and face similar transition and development challenges despite certain differences emerging from diversity in size and location, ethnic composition, resource endowments, etc. As a result, the level of economic transformation of the TEs varies. For instance, while Uzbekistan has taken a gradual approach in liberalizing its economy, the smaller economies with a relatively weak resource base have adopted speedier measures toward liberalization. Yet, these economies face tough policy challenges. Despite the abolishment and disintegration of the economic and trade structures nurtured by the former Soviet Union, the region continues to exhibit interdependence and linkages as evidenced by the swift transmission of the Russian financial crisis in 1998, which adversely affected economic gains and introduced new vulnerabilities.

4. The TEs have adopted macroeconomic stabilization programs⁴ supported by the International Monetary Fund. In recent years, the CARs have managed to achieve positive real gross domestic product (GDP) growth, and somewhat curb the inflation rate. Public finances and external accounts exhibit inherent vulnerabilities in the CARs, resulting in high external debt ratios

¹ So far, ECRD has governance and private sector assessments in progress for the People's Republic of China (PRC), Kazakhstan, and Tajikistan. In the case of the Kyrgyz Republic and Mongolia, governance assessments have been launched, but private sector assessments have yet to be launched. In the case of Azerbaijan, Uzbekistan, and Turkmenistan, both governance and private sector assessments are required. Diagnostic studies for financial management have been completed for the Azerbaijan, PRC, Mongolia, and Uzbekistan.

² The TA was listed in the ADBBO on 25 June 2002. Management has approved the request to waive the three-month listing requirement.

³ See para. 15.

⁴ Uzbekistan, however, adopted a staff monitoring program only in January 2002.

in the Kyrgyz Republic,⁵ Mongolia, and Tajikistan. To ensure fiscal and external sustainability, the governments have resorted to cuts in public spending in relation to GDP, which will affect the region's long-term growth prospects. On the external front, the TEs exhibit varying degrees of openness. Except for Uzbekistan, foreign exchange and trade regimes across the CARs and Mongolia have been liberalized. Currencies remain weak after having depreciated by roughly half compared with the levels in the early 1990s. Progress with structural reforms has varied. Generally, price and trade liberalization has proceeded, while the process of economic restructuring has been slow and confined to small and service-related industries. Recurring banking crises have necessitated settlement of nonperforming portfolios through fiscal support. Despite frequent bank restructuring, inefficiencies in financial intermediation have persisted and inflationary pressures have prevented emergence of competitive interest rates. The growing economic difficulties have resulted in rising poverty and a fall in social indicators. Unless the implementation of an effective reform agenda is expedited, the transition of these economies will be protracted.

5. **The State of Governance.** An effective and well-functioning political and administrative governance structure at all levels is key to strengthening economic fundamentals of the TEs and their sustained recovery. After disintegration of the former Soviet Union, the TEs ended up with concentrated political regimes (one party or special interest groups). Often these groups protect old state structures and influence frequent changes within the bureaucracy, due to regional or clan rivalries. Such conditions have made economic and social transformation difficult. Civil services and other institutions are weak, competition is limited, and opaqueness of the regulatory framework allows room for discretion. Together this has encouraged rent seeking and corruption.

6. State governance in the TEs can be judged by their economic performance, the quality of life of the populace, and their access to basic rights and services. While the overall macroeconomic management record of the TEs has been mixed, the ability of the governments to reorient their roles has been a challenge. The state continues to perceive its role as a principal provider of public services and continues to allow enterprises access to budget, subsidies, directed low-cost credits, tax exemptions, and accumulation of interenterprise arrears. This has encouraged imprudent investments and financing decisions that have resulted in misallocation of resources, while complicating fiscal management and adversely affecting the health of the banking system.

7. Weak economic management further affects governance in the TEs. In the public sector, low revenues have affected fiscal management, and compressed public investment. Both have consequences for long-term growth and financial sustainability. While decentralization allows voters preferences to be incorporated into governance and investments decisions, weak financial and human resource capacities at subnational government levels impede satisfactory intergovernmental fiscal arrangements that would allow adequate revenue and expenditure balances. In the absence of sound center-local fiscal relations, fiscal management is complicated given competing pressures and ad hoc allowances. Although some core institutions are evolving in the TEs, the lawmaking process still suffers from weaknesses. The business practices of the legislative bodies are at times ad hoc and arbitrary in that the larger public interest is not effectively represented. Improvements are needed in this area to mediate effectively between differing interests, and establish policies, laws, and resource priorities. The judiciary lacks predictability and transparency, and is not independent of the executive branch, nor is it adequately equipped with the capacity to uphold the rule of law and settle disputes.

8. **Private Sector Development.** Private sector activity has gained momentum across the TEs, although the share of the private sector in GDP ranges from 20% in Tajikistan to 60% in Kazakhstan. The growth in the private sector is a direct result of privatization of small and service-related enterprises and housing implemented by auction sales, voucher schemes, privatization investment funds, and employee buyouts. New capital has primarily been directed in some

⁵ Given its unsustainable levels of external debts, creditors agreed to reschedule the external debt at the Paris Club in February 2002.

countries and in specific sectors such as oil and minerals. The state sector continues to dominate in large manufacturing and public utilities. Enterprises in these sectors have been transformed into joint stock companies, providing some clarity of ownership and mandated submission of financial statements. Progress in liquidation and operational and financial restructuring of state-owned enterprises has been slow because of the lack of political commitment, weak capacity of the state property committees, and issues of corporate governance of these companies.

9. Legal and regulatory frameworks are not conducive for private sector development (PSD) and impinge heavily on most sector activities. For instance: state orders (i) impose controls on the crop sector and industrial products through production and price controls (notably in Uzbekistan) as well as the sale and purchase of housing and industrial land, (ii) impose licensing and other requirements on the establishment of businesses and foreign investment, (iii) regulate wages and recruitment practices, and (iv) impose restrictions on foreign exchange. The legal deficiencies affect enforcement and guarantee of property rights and quick resolution of bankruptcies. Civil codes are outdated. Commercial disputes are rarely settled in the courts based upon inexperience with commercial contracts.

10. The TEs have introduced a number of measures to attract investments. The basic legal framework now in place for company, banking, taxation, and foreign investment laws includes guarantees for full repatriation of profits from foreign investment and offers tax incentives. Given the fundamental economic issues, the CARs have been able to attract cumulatively \$8.4 billion, of which three fourths has been to Kazakhstan largely to support the oil sector with limited flows to others. Access to finance has been a challenge for the TEs. Financial intermediation is largely bank based, while private equity flows are limited because of the small and weak capital markets and lack of institutional investment. Economies with stronger financial positions, such as Kazakhstan, have been able to issue sovereign eurobonds or raise funds for specific infrastructure projects through international syndicated loans.

11. Transforming the governments' role from being the exclusive financiers and providers of infrastructure services to becoming facilitators and regulators of services provided by private firms is essential for the TEs and critical to support fiscal and external debt management. Building public and private partnerships and more regional cooperation will help to build infrastructure. To channel the private initiative in socially useful directions, the TEs need to develop an enabling policy environment and regulatory framework. As the engine of productivity, growth, and job creation, the private sector has tremendous potential to contribute to growth and poverty reduction in the TEs.

12. **Financial Management.** As an integral part of governance and the PSD strategy, the state of financial management and policies being adopted by the TEs needs to be studied. Most of the TEs are adopting international accounting standards and international auditing standards, although local standards and practices do not yet conform to international best practices and suffer from weaknesses in institutional, regulatory, and legal frameworks for accounting and auditing practice. The problems constraining the adoption of international standards are the lack of skilled accounting and auditing personnel, absence of accounting education and training as well text books in this area in local languages, and lack of effective professional bodies to provide oversight of standards and their implementation.

13. The TA will launch assessment work simultaneously for each thematic area in a country to develop synergies between the three thematic subjects: governance, PSD, and financial management (para. 2). The three thematic areas being studied cover some common grounds, which needs to be reviewed and analyzed in a an integrated manner to avoid overlapping. For instance, GA involves discussions of political and economic management and rule of law that has implications for the PSAs, and similarly the PSAs cover issues of corporate governance and management, which is integral to governance matters. Aspects of both public and private sector financial management are a key component of the GA and PSAs. Adopting this approach will

enable ADB to design appropriate and focused assistance in response, while encouraging an effort to reduce costs as well as the potential overlap in conducting thematic work. The TA will identify the unique conditions, priorities, and approaches being adopted in the selected countries for governance, PSD support, and better financial management. The assessment work will be conducted based on the guidance provided in ADB's governance and private sector strategy and action plan papers.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

14. The objective of TA is to analyze the state of governance, PSD, and financial management in the TEs in an integrated manner, and to propose coherent strategies in these areas. The TA will support an in-depth review and assessment of the existing political and economic governance structures, and state of legal and regulatory policies and institutional frameworks to identify the issues and constraints facing governance, PSD, and financial management. Drawing on this work, the TA will help develop a strategy and action plan to promote improvements in these thematic areas and identify the role that ADB and other assistance agencies can play in encouraging economic development within the context of country strategies programs.

B. Methodology and Key Activities

15. The TA will undertake GA for Uzbekistan and Azerbaijan; PSA for Azerbaijan; Kyrgyz Republic, Mongolia, and Uzbekistan; and diagnostic work on financial management, where required.

16. **Governance Assessment.** Adopting the framework of ADB's governance policy, this component will include an assessment of governance structure by reviewing the effectiveness of (i) the political process to judge formulation and implementation of governance management and policies; (ii) the extent of public accountability, and quality of public administration and civil services function, while judging the level and effectiveness of the participation of civil society; (iii) the governments' public financial management with a focus on evaluating intergovernmental arrangements keeping in view merits of decentralization versus centralization, and implications for voter's choice, allocative efficiency, and the capacities of the subnational governments; and (iv) the rule of law by analyzing the capacity of the state's legal and regulatory framework, judicial system, and anticorruption policies. Drawing from this diagnostic analysis, a priority medium-term action plan for strengthening country governance and different sectors will be developed.

17. **Private Sector Assessments.** The PSA will provide an overview of the nature and scope of the private sector in the country concerned, and identify the strengths, weaknesses, and constraints of the whole or selected segments of the private sector. The PSA will also review the policy and regulatory framework and identify possible approaches and recommendations to catalyze PSD in light of the foregoing diagnosis and analysis, while identifying strategic initiatives for ADB assistance.

18. **Diagnosis of Financial Management.** Examining the state and quality of the accounting and auditing structure and systems in the public and private sectors, this study will analyze how standards and their applications differ from international best practices, and the capacities and professional agencies available to maintain these standards. The study will identify (i) a reform agenda to encourage adoption of international accounting and auditing standards and to improve transparency and accountability, and (ii) explore approaches and modalities to reduce corruption and enhance public confidence.

19. ADB staff will conduct assessment work based on standard templates drawing on country data and studies; reviews of ADB loan, TA, and economic and sector work; and consultation with all stakeholders. Special studies and surveys will be conducted with support of consultants as required. Each assessment will provide recommendations and an action plan that will be integrated into ADB's country strategy and program, recognizing ADB's experience and comparative advantage. The assessments will provide information on specific indicators that will serve to measure performance under ADB's performance-based allocation system. The findings of the assessments will be utilized for policy dialogue to enhance governance and financial management practices, and efforts will be launched to effectively create an environment for PSD. To encourage ownership of stakeholders as well as share experiences across the region, the TA will support dissemination of the findings of the assessment through national and regional workshops. Representatives of government agencies, professional bodies, educational institutions, assistance agencies, and other relevant interest groups will attend the workshops. Eventually this work will be consolidated and presented at ADB's annual meeting in 2003.

C. Cost and Financing

20. The cost of the TA is estimated at \$595,000 equivalent consisting entirely of foreign exchange. ADB will finance the TA on a grant basis from the ADB-funded TA program. The TA will finance the services of international (17 person-months) and domestic (19 person-months) consultants that will be used to support GAs for two countries and PSAs for four countries, and supportive work on financial managements for these assessments. The consultants will include governance specialists, private sector specialists, and certified public accountants with diagnostic accounting experience. The consultants will be recruited on need basis to support segments of assessment work where there is need to collect primary data and information or to interview/survey for example, the private sector, civil society, NGOs or accounting firms, and associated bodies. The TA budget includes \$75,000 equivalent to finance the costs of national and regional workshops to discuss the outline and findings of the studies as well as action plans developed through these studies. Detailed cost estimates are provided in Appendix 2.

D. Implementation Arrangements

21. ADB will be the Executing Agency for the TA. The TA implementation arrangements and allocation of total person-months will be kept flexible to ensure proper coverage of countries and topics. All of the consultants will be recruited on an individual basis but only to conduct specific studies where specialized skills are required, or where there are gaps in information or additional analysis is warranted within the overall TORs (see Appendix 3). Consultants will be recruited in accordance with *ADB's Guidelines on the Use of Consultants* and other arrangements acceptable to ADB on the engagement of domestic consultants. Assessments will be conducted on the basis of template provided in Appendix 3⁶ and Appendix 4 provides an outline of the final report. The TA will commence in September 2002 and be completed by June 2004. The Governance, Finance, and Trade Division of ECRD will administer and supervise the TA.

IV. THE PRESIDENT'S DECISION

22. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$595,000 on a grant basis for Promoting Good Governance in East and Central Asia, and hereby reports this action to the Board.

⁶ This could be somewhat modified by the *Private Sector Assessment Review Process*, being conducted by Regional and Sustainable Development Department in mid-2002.

TECHNICAL ASSISTANCE FRAMEWORK

A. Governance Assessment

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal Promote good governance.</p>	<p>Workshop to discuss with the governments recommendations of governance assessment and inclusion of the findings and recommendations in country strategy and program (CSP) for eventual implementation through lending and advisory support.</p>	<p>Country performance assessment of governance and sustainable economic growth to feed into performance-based allocation</p>	<p>Acceptance of the governance assessments by the governments</p> <p>Stable political and economic situation.</p>
<p>Purpose Assist the government in reviewing ongoing governance reforms, identify and prioritize governance reform needs, and recommend measures to implement reforms.</p>	<p>Successful completion of quality governance assessment report</p> <p>Agreed upon medium-term action plan for pro-poor governance</p> <p>Evidence that the governments commit to reforms that have been recommended</p>	<p>Policy consultation and workshop to discuss the findings and recommendations of the report</p>	<p>Governments are committed to the assessments and demonstrate buy-in.</p> <p>Governments are willing to involve other stakeholders in the preparation of governance action plans.</p>
<p>Outputs A quality governance assessment that provides a comprehensive overview of governance issues</p> <p>Governance action plan for incorporation into the CSP and ADB operations</p> <p>Increased understanding amongst government officials and civil society representatives of governance concepts and increase their dialogue on reform issues.</p>	<p>Agreement on ADB governance report and action plan</p> <p>Governance concepts increasingly utilized by various stakeholders and discussions are better informed</p>	<p>ADB staff review mission and consultations with governments agencies and other stakeholders</p>	<p>Governments provide adequate information and approve publication of the assessments</p> <p>Governments commitment to action plans</p> <p>Governments honor its commitment to second staff to workshops.</p>
<p>Activities Assess issues and challenges in promoting good governance</p>	<p>Satisfactory assessment and formulation of recommendations within the framework and time frame.</p>	<p>ADB staff review and monitoring of consultants' inputs within the time frame</p>	<p>Availability of adequate and reliable information</p>

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
Formulate recommendations to help practice good governance Workshops to disseminate findings	Discussions and deliberations at the workshops		Successful recruitment and fielding of qualified consultants and satisfactory inputs Constructive and free exchange of views at the workshops by participants
Inputs 2.5 person-months of international consulting services and 2.5 person-months of domestic consulting for each assessment			

TECHNICAL ASSISTANCE FRAMEWORK

B. Private Sector Assessment

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal Encourage development of a strong and dynamic private sector to accelerate economic growth and improve living standards</p>	Improved enabling environment for the private sector that encourages private sector activities and investments.	Economic and business reports	Political commitment for open and liberal private sector environment
<p>Purposes Promote broad-based private sector development (PSD) to increase private activities and integrate into the global economy. Assist government to develop the private sector strategies and action plan.</p>	Completion of private assessments (PSA) and strategies adopted by ADB and endorsed by the respective governments and private sector.	ADB staff hold consultation on the PSD strategy and action plan	<p>Availability of adequate and reliable information on all aspects of the private sector</p> <p>Governments' endorsement of, and commitment to the PSD strategy and action plans</p>
<p>Outputs PSA and private sector strategies in study countries to include</p> <p>(i) an overview of the private sector, (ii) review of the enabling environment, (iii) approaches to enhance PSD, and (iv) strategic initiatives for ADB assistance.</p>	PSA and private sector strategies prepared in line with the terms of reference of the TA, within the indicated time frame.	<p>Reports by ADB staff with consultants' inputs</p> <p>Participation in consultative meetings and feedback from participants and stakeholders</p>	Governments' support for the conduct of PSAs in the selected countries
<p>Activities Assess issues and challenges. Formulate strategic choices and options to help countries to successfully address identified impediments. Formulate recommendations for ADB's assistance plan.</p>	Satisfactory assessments of issues and challenges, formulation of strategic choices and recommendations for ADB's assistance	Reports by ADB staff and consultants	<p>Availability of adequate and reliable information</p> <p>Successful recruitment and fielding of qualified consultants and satisfactory inputs</p> <p>Constructive and free exchange of views at the workshops by participants</p>

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
Workshops to disseminate findings and recommendations.	ADB participation in workshops		
Inputs 2.5 person-months of International consulting services and 2.5 person-months of domestic consulting services per assessment.			

TECHNICAL ASSISTANCE FRAMEWORK

C. Financial Management Assessment

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal Strengthened financial management, accountability and transparency among government and private sector institutions</p>	<p>Implementation of recommendations to enhance financial management</p>	<p>Economic reports</p>	
<p>Purpose Assist the governments in assessing the current state of financial management, identify reform needs and recommend measures to implement reforms aimed at improving financial management and governance in line with international best practices and standards</p>	<p>Completion of financial management reports</p> <p>Agreed upon action plans to implement recommendations to improve policy and regulatory measures</p>	<p>ADB staff review missions and consultations with governments, professional bodies and other stakeholders</p>	<p>The governments are committed to and involved in improving financial management and governance.</p>
<p>Outputs Country reports that include</p> <ul style="list-style-type: none"> (i) a review of the existing accounting and auditing standards, and assessment of the degree of deviation from international accounting and auditing standards (IAAS) and international public sector accounting standards (IPSAS); (ii) an assessment of the capability and capacity to provide effective accounting support to meet international standards and best practices; and (iii) assessment of the level and type of assistance needed to provide acceptable accounting and auditing support. 	<p>Reports with quality assessments and recommendations and measures to implement these</p>	<p>ADB staff review and consultation with governments, professional bodies, educational institutions, and other stakeholders</p>	<p>Data availability</p> <p>Active involvement of governments' representatives and professional organizations</p> <p>Information will be shared with future accounting and auditing practitioners and other development agencies</p>

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
An action plan based on the assessments including recommendations to improve financial management	Recommended action plan for the governments and the role of the Asian Development Bank (ADB) in improving financial management	Feedback from governments, executing agencies, and professional organizations	Governments are committed to implementing action plans
<p>Activities Produce country reports and action plans by</p> <ul style="list-style-type: none"> (i) reviewing relevant documents on accounting and auditing regulatory framework. (ii) surveying and interviewing selected agencies and institutions. (iii) assessing existing accounting and auditing standards. (iv) developing recommendations for reforms and implementation (v) formulating an action plan <p>Assess the role of ADB and other development agencies in improving the financial management and governance situation in the country.</p>	Satisfactory assessments, surveys, and formulation of recommendations within the framework and time frame	<p>ADB staff review with inputs from consultants</p> <p>Feedback from government, agencies, and professional bodies</p> <p>Feedback from government, agencies, and professional bodies</p>	<p>Successful recruitment and fielding of consultants</p> <p>Availability of data and information</p>
<p>Inputs 2 person-months of international consulting services and 4 person-months of domestic consulting services</p>			

COST ESTIMATES AND FINANCING PLAN
(\\$)

Item	Foreign Exchange	Local Currency	Total Cost
Asian Development Bank Financing^a			
A. International Consulting			
1. Remuneration and Per Diem	391,000	0.0	391,000
2. Air Fare	30,000	0.0	30,000
3. Report preparation, translation	12,000	0.0	12,000
Subtotal (A)	433,000	0.0	433,000
B. Domestic Consulting			
1. Remuneration	42,750	0.0	42,750
2. Domestic Travel	2,000	0.0	2,000
Subtotal (B)	44,750	0.0	44,750
C. Workshops	75,000	0.0	75,000
D. Contingencies	42,250	0.0	42,250
Total	595,000	0.0	595,000

^a Financed by the Asian Development Bank-funded TA program.
Source: Asian Development Bank estimates.

OUTLINE OF TERMS OF REFERENCE FOR CONSULTING SERVICES

1. ADB staff will bear the primary responsibility for conducting the assessments based on the templates provided in A, B, and C sections below. These templates are consistent with the ADB's guidelines as provided in the *Framework for Preparation of Governance Assessments, July 2001*,⁷ the ADB's *Private Sector Strategy* and other guidelines issued by ADB for governance, private sector and financial management areas. ADB staff will take primary responsibility for preparing the assessment and will launch the work based on a review of the existing studies and documents and identify gaps and needs for additional work. Specialists will only be recruited on a need basis to conduct in-country fieldwork research in specific areas only where information or analysis is required and/or conduct interviews with the private sector representatives, nongovernment organizations (NGOs), and other relevant participatory groups and donors. For every assessment, the TA includes a pre-specified international and domestic consulting services and specific TORs for individual consultants will be developed based on the need for specific specialization to launch primary work or collate data/feedback of stakeholders within the broad outline of assessments specified below. ADB staff will be responsible for integrating the inputs of consultants to prepare the final assessments that will be disseminated widely to the governments and other stakeholders. ADB will structure workshops to allow a wider discussion on substantive matters arising from the report from a local and international perspective.

A. Governance Assessment (GA) (Total of 5 person-months of international and 5 person-month of domestic consulting services for GA of two countries – assuming 2.5 person months of international and 2.5 person months of domestic consultants per assessment)

2. The GA will be conducted by ADB staff with support of public administration specialists or institutional experts or legal and regulatory specialists, who have a proven track record and experience in governance area or have worked on institutional policy and development areas with experience in transition economies, preferably in the Central Asian republics (CARs). The consultants must have professional knowledge of governance elements, and ability to provide advice on policy reforms.

3. The report will contain an overview of the political, economic, and sector level of governance management, and identify issues and constraints faced by the country. The consultant will provide an overview and evaluation of the initiatives and programs launched by the Government to strengthen governance in the country and specific sectors, and assess the effectiveness of externally financed programs supporting governance. Based on this review, the consultants will identify areas where ADB can support or build on its past success, and provide perspectives on approaches and modalities of how governance can be strengthened for broader economic policy management and implementation, and specific interventions warranted to catalyze action at the macroeconomic and sector levels.

4. The following aspects will considered and assessed

- (i) **Governance—political and institutional structure.** Describe historical background; structure of governance: political structure, machinery of

⁷ This could be somewhat modified by the *Governance Assessment Review Process*, being conducted by RSDD in mid-2002.

government, and executive branch; and relationship between governance and social development management;

- (ii) **Decentralization and its impact on allocative and productive efficiency.** Describe public resource and expenditure management of central government, intergovernmental relationship—level of autonomy and fiscal independence, and state of subnational Government in terms of governance and financial management;
- (iii) **Public accountability.** Describe as pertains to the civil service, institutional mechanism for dealing with corruption, and civil society (including NGO, media, and professional associations);
- (iv) **Rule of Law.** Describe the legal and regulatory framework, and judicial system;
- (v) **External Assistance to Strengthen Governance; and**
- (vi) **Promotion of Governance—An Action Plan.** Include actions for promotion of poverty-focused governance reforms, medium-term action plan, identification strategic Initiatives for ADB, and how ADB can, with its various instruments and modalities, support programs to enhance governance.

B. Private Sector Assessment (Total of 10 person months of international and 10 person months of domestic consultants for PSAs of four countries – assuming 2.5 person-months of international and 2.5 person- months of domestic consulting services per assessment)

5. ADB staff will be responsible for the assessment and recruit private sector development specialists as needed to undertake specific analyses and surveys. The consultants hired should have proven track record of analytical work in private sector policy work and broad familiarity of approaches and modalities of promoting private sector development (PSD), small and medium enterprises, privatization and state-owned enterprise reform, finance and banking, and regulatory framework and legislative reform in transition economies.

6. The assessment will contain a profile of the private sector, its size and dimensions; the enabling policy, legal, and regulatory environment; and issues and constraints facing entry and exit of the private sector and foreign direct investment. Successes and failure of government policy and programs that have had implications for private sector development will be discussed; and multilateral and bilateral initiatives to promote the private sector will be evaluated.

7. The following will be assessed:

8. **Macroeconomic and Private Sector Policy Context.** Describe the Government's policy stance regarding the private sector, macroeconomic management and its role in restoring private sector confidence, state of infrastructure, and performance and problems of different segments of the private sector.

9. **Contribution of the Private Sector to the Economy.** Provide an overview of the size and different aspects of the private sector: its definition with specific details on private sector contribution to GDP and employment, and significance of small and medium enterprises and foreign direct investment. The study should in particular dwell on the

- (i) share of the private and public sectors in output, employment, and investment;
- (ii) share of private sector involvement in the large- and small-scale manufacturing sector;
- (iii) significance of private sector involvement by the industry sector or region, as appropriate;
- (iv) level of foreign direct investment and its location;
- (v) domestic vs. foreign ownership and investment by sector
- (vi) relative importance of different types of advocacy bodies for private sector promotion including the role of SMEs, cooperatives, NGOs, etc.

10. **Major Impediments to PSD.** Analyze strengths and weaknesses of the enabling policy, legal, and regulatory environment for the private sector, and specify how they encourage or impede the role of the private sector based on the launching of a firm survey or reliance on secondary surveys. Identify the

- (i) administrative licensing and regulatory regime affecting investment, ownership, output, pricing, distribution, access to technology, information and other inputs, financing, and taxation and employment; and assess their impact on the private sector;
- (ii) legal and regulatory constraints facing the private sector: entry and exit legal framework, perspective on state of crucial laws and their key elements such as related to property rights, contractual rights, law of associations, labor laws, cost and delays in legal redress, etc.;
- (iii) financing;
- (iv) marketing;
- (v) entrepreneurship;
- (vi) costs of doing business and transactions due to extent of bureaucratic procedures; and
- (vii) the capacity and quality of the public institutions responsible for planning and implementing the policy, laws, and regulations.

11. **The Role of the Private Sector in Industry.** Analyze the extent of the private sector's involvement in all key sectors of the economy including financial, infrastructure, social, and agriculture. Address the following: industry review and development; extent of private ownership, contribution, investment, and opportunities; policy environment that encourages/discourages private sector development; and recommendations.

12. **The Government and MDB's Role in PSD.** Prepare an inventory and review of programs supporting private sector development the assistance of other multilateral and bilateral external aid agencies, as well as any domestic initiatives of the Government and the private sector. Include a discussion of foreign direct investment promotion and the overall status of the privatization effort undertaken by the government.

13. **An Action Plan for PSD.** Develop an action plan for PSD identifying policy, legal, and regulatory changes required to promote PSD and areas for promotion of public and private partnerships. Provide perspective on how ADB can play a role in this area to create an enabling policy environment, supporting transformation of specific organizations dealing with PSD, support investment to create business and employment opportunities, and catalyze equity and debt required for critical infrastructure.

C. Diagnosis of Financial Management (DFM) (2 person-months of international consulting services and 4 person-months of domestic consulting services)

14. ADB staff will be responsible for the diagnosis with the assistance of consultants as needed. The consultants should be chartered accountants or certified public accountants with equivalent qualifications and extensive experience in the diagnostic analysis of accounting, auditing, and corporate governance matters, particularly of developing countries.

15. The financial management diagnosis will include the following

- (i) **Legal and regulatory framework.** Describe governing laws and regulations for accounting, auditing, and internal control systems in the public and private sectors; existing accounting and auditing capabilities in the public and private sectors, including the related enforcement issues; differences between the local standards and international accounting standards and international standards of auditing; governing laws for budgeting and reporting in public sector; and legal framework for accounting institutes including reporting structures and independence.
- (ii) **Professional infrastructure and institutions.** Describe professional infrastructure for the accountancy and auditing profession, continuing professional education arrangements of certified public accountants, organizational structure of the accounting institutes, institutional capability of accounting institutes and their accounting standards committee, and operational status of domestic and international accounting and auditing firms.
- (iii) **Financial reporting arrangements and disclosure requirements.** Describe financial reporting and disclosure requirements for financial institutions (particularly for banks, insurance companies, securities companies, and other nonbank financial institutions) and publicly listed companies, and transparency in comparison with accepted international regulatory and reporting standards.
- (iv) **Role of external assistance in strengthening financial management.** Prepare an inventory and review of programs of other assistance agencies assisting in developing accounting and auditing capabilities; if such assistance is available, assess the level of the assistance and any gaps that exist; and describe the role that ADB can play in collaborating with other agencies to improve the situation.
- (v) **Promoting financial management- an action plan.** Include actions for promotion of better financial management to support good governance with a focus on transparent reporting and budgeting; medium-term action Plan; strategic initiatives for ADB; and how ADB can provide assistance through various instruments to enhance governance through better financial management and transparent reporting?

REPORT OUTLINES

A. Generic Outline of Governance Assessment Report⁸

FOREWORD

ACKNOWLEDGMENT

BACKGROUND

Executive Summary (5–7 pages summarizing the key findings and recommendations)

I. INTRODUCTION AND OVERVIEW

II. DETAILED DISCUSSION OF SELECTED GOVERNANCE ISSUES

A. Public Administration

1. Core Government Functions and Public Sector
 - a. Constitution and Legislature
 - b. Machinery of Government
 - c. Participation in Policymaking and Legislative Process
 - d. Public Accountability—Corruption
2. Civil Service
 - a. Legality and Accountability of Civil Servants
 - b. Impartiality and Independence of the Public Service
 - c. Human Resource Management
3. Improving Governance at Subnational Levels of Government – National/Local
 - a. Legal Foundation
 - b. Public Finances
 - c. Decentralization and Intergovernmental Fiscal Reforms

B. Public Financial Management

1. Revenue Administration
 - a. Internal Revenue
 - b. Customs
2. Public Expenditure Management
 - a. Budget Formulation
 - b. Budget Approval
 - c. Budget Execution
 - d. Procurement
3. Public Sector Accounting
4. Public Sector Auditing
5. Intergovernmental Fiscal Relations
6. Specific Anticorruption Measures

⁸ Outline is based upon the Framework for the Preparation of Country Governance Assessments, Governance and Capacity Building Unit, Strategy and Policy Department, June 2001 and is customized to country circumstances and to highlight priority issues.

C. Legal and Regulatory Framework

1. Legal Framework
2. Regulatory Regimes
 - a. Organizational Issues
 - b. Transparency and Accountability
 - c. Redress Mechanisms
 - d. Effectiveness and Efficiency

D. Judicial System

1. Organization of the Court System
2. Budget, Finances, and Accountability
3. Appointments and Remuneration of Judges
4. Efficiency and Effectiveness

E. Civil Society and Governance

1. Freedom of Election
2. Freedom of Speech
3. Organizational Arrangements

III. CONCLUSIONS: ACTION PLAN

A. Government

B. External Assistance

C. ADB Action Plan

Appendixes: Aid Matrix
Government Organizational Chart

B. Generic Outline of Financial Management Assessment Report

EXECUTIVE SUMMARY

I. INTRODUCTION

- A. Study Background
- B. Objectives
- C. Scope
- D. Country Case Studies and Workshops
- E. ADB Focus on Financial Governance _____
- F. _____ (country)
- G. Project for Improving Financial Reporting and Auditing

II. ACCOUNTING AND AUDITING IN (Name of Country)

A. Accounting

- 1. Introduction
- 2. Public Sector Accounting
- 3. Private Sector Accounting
- 4. Financial Reporting Requirements

B. Auditing

- 1. Introduction
- 2. Auditor-General
- 3. Public Accounts Committee
- 4. Private Sector Auditing
- 5. International and Domestic Accounting and Auditing Firms

III. PROFESSIONAL INFRASTRUCTURE

- A. Introduction
- B. The Institute of Chartered Accountants of (Name of Country)
- C. Institute of Cost and Management Accountants
- D. The (Name of Country) Institute of Public Finance Accountants

IV. ACCOUNTING AND AUDITING STANDARDS

- A. Introduction
- B. Deviations from International Accounting Standards
- C. Public Sector Accounting Standards Board Establishment
- D. (Name of Country) Standards on Auditing

V. ACCOUNTING AND AUDITING TRAINING

- A. Introduction
- B. Public Sector Training
- C. Institutional Training
- D. Continuing Professional Education

VI. GOVERNMENT BUDGETING AND ACCOUNTING

- A. Introduction
- B. Project for Improving Financial Reporting and Auditing
- C. Budget Procedures
- D. Corruption Issues in the Public Service

VII. EXTERNAL ASSISTANCE

- A. Overview
- B. Aid Activities and Coordination
- C. Project for Improving Financial Reporting and Auditing

VIII. ISSUES AND RECOMMENDATIONS

- A. Where External Assistance Might be Appropriate
 1. (Name of Country) Accounts and Audit Academy
 2. Accounting Training
 3. Training for Accounting Lecturers and Professors
 4. Security and Control of Noncurrent Assets
 5. Review of Commercial Laws

- B. Where External Assistance Is Not Required
1. Separation of the Accounts and Audit Function
 2. Amalgamation of Accounting Bodies
 3. Public Relations—National Accounting Bodies
 4. Independent _____ Accounting Standards Board
 5. Public Sector Accounting Standards Board
 6. _____ Public Sector Accounting Standards Board
 7. Application of IAS for Unlisted Companies
 8. Public Accounts Committees
 9. Additional Recommendation by a Senior Staff Member of Auditor-General's Department
 10. Establishment of Internal Audit Function
 11. Joining the Institute of Internal Auditors
 12. ADB Anticorruption Policy

IX. MAIN DEFICIENCIES AND ACTION PLAN

REFERENCES

C. Generic Outline of Private Sector Assessment Report

EXECUTIVE SUMMARY

I. MACROECONOMIC ENVIRONMENT

A. Macroeconomic Overview

B. Profile of the Private Sector

II. GOVERNMENT POLICY FOR PRIVATE SECTOR DEVELOPMENT (PSD)

A. The Private Sector in the Constitution and Recent Policy Documents

B. Privatization

C. Small and Medium Enterprises (SMEs)

D. Competition

E. Trade and Investment Liberalization

III. ENABLING ENVIRONMENT, MAJOR CONSTRAINTS FOR PSD, AND RECOMMENDATIONS

A. Laws and Regulations

B. Access to Land

C. Access to Credit

D. Licensing and Registration

E. Taxation

F. Trade, Customs, and Duties

G. Dispute Resolution Mechanisms

H. Public Administration and Corruption

I. Labor Issues

J. Competition and Access to Markets

K. Information Exchange and Technology

- IV. PRIVATE SECTOR ACTIVITIES, SECTOR SPECIFIC CONSTRAINTS, AND RECOMMENDATIONS
 - A. Financial Sector
 - B. Natural Resources
 - C. Infrastructure
 - D. Social Sectors
 - E. Agriculture and Forestry
 - F. Other
- V. PSD ACTIVITIES OF OTHER AID AGENCIES
- VI. CONCLUSIONS AND RECOMMENDATIONS FOR ADB STRATEGY