



# Validation Report

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Reference Number: PVR-433  
Project Number: 39015-042  
Grant Number: 0077  
November 2015

## Kyrgyz Republic: Tax Administration Reform and Modernization Project

Independent Evaluation Department  
**Asian Development Bank**

## ABBREVIATIONS

ADB	–	Asian Development Bank
CAPE	–	country assistance program evaluation
GDP	–	gross domestic product
ICT	–	information and communication technology
ITAS	–	Integrated Tax Administration System
KITIS	–	Kyrgyzstan Integrated Tax Information System
MIS	–	management information system
PCR	–	project completion report
PMO	–	project management office
STS	–	State Tax Service
TA	–	technical assistance

## NOTE

In this report, “\$” refers to US dollars.

### Key Words

adb, asian development bank, information and communication technology, kyrgyz republic, public governance, tax administration, tax reform and modernization, validation

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## PROJECT BASIC DATA

<b>Project Number:</b>	39015-042	<b>PCR Circulation Date:</b>	Mar 2015	
<b>Grant Number:</b>	0077	<b>PCR Validation Date:</b>	Nov 2015	
<b>Project Name:</b>	<b>Tax Administration Reform and Modernization Project</b>			
<b>Country:</b>	Kyrgyz Republic		<b>Approved</b> (\$ million)	<b>Actual</b> (\$ million)
<b>Sector:</b>	Public Sector Management	<b>Total Project Costs:</b>	12.50	12.06
<b>ADB Financing:</b> (\$ million)	<b>ADF:</b> 10.00	<b>Grant:</b>	10.00	9.38
		<b>Borrower:</b>	2.50	2.68
	<b>OCR:</b> 0.00	<b>Beneficiaries:</b>	0.00	0.00
		<b>Others:</b>	0.00	0.00
<b>Cofinancier:</b>		<b>Total Cofinancing:</b>	0.00	0.00
<b>Approval Date:</b>	14 Jun 2007	<b>Effectiveness Date:</b>	5 Nov 2007	20 Nov 2007
<b>Signing Date:</b>	7 Aug 2007	<b>Closing Date:</b>	30 Sep 2012	30 Sep 2013
<b>Project Officers:</b>	S. Shrestha J. A. Tan III R. Barreto	<b>Location:</b> ADB headquarters ADB headquarters ADB headquarters	<b>From</b> Jun 2007 Oct 2009 Sep 2011	<b>To</b> Sep 2009 Sep 2011 Sep 2013
<b>Initial Reviewers:</b>	C. Narayanasuwami, Consultant M. J. Dimayuga, Senior Evaluation Officer, IED1	<b>Peer Reviewer:</b>	H. van Rijn, Principal Evaluation Specialist, IEOD	
<b>Quality Reviewer:</b>	F. Ahmed, Lead Evaluation Specialist, IED1	<b>Director:</b>	W. Kolkma, IED1	

ADB = Asian Development Bank; ADF = Asian Development Fund; IED1 = Independent Evaluation Department, Division 1; IEOD = Independent Evaluation Department; OCR = ordinary capital resources; PCR = project completion report.

## I. PROJECT DESCRIPTION

### A. Rationale

1. The Tax Administration Reform and Modernization Project was one of a series of projects supported by the Asian Development Bank (ADB) in the Kyrgyz Republic to foster economic growth and public governance by increasing tax and customs revenues and improving tax administration. The project was well aligned with the government objectives outlined in the Joint Country Support Strategy to introduce modern technology in tax administration, improve operations, and reduce corruption.<sup>1</sup> During project design, fiscal consolidation was considered vital to maintain the good performance of the economy and sustaining its achievements.

<sup>1</sup> ADB. 2007. *Joint Country Support Strategy: Kyrgyz Republic, 2007–2010*. Manila. The strategy focused on four pillars: economic development, governance and transparency in public administration, human development, and environmental sustainability.

## **B. Expected Impact**

2. The project was expected to help increase the effectiveness of tax administration to sustain fiscal consolidation and macroeconomic stability. The performance indicator was for state tax revenues to increase from 14.6% of gross domestic product (GDP) in 2005 to at least 16.0% of GDP by 2012. Two sectors were expected to benefit from tax reform and modernization: first, the taxpayers through more efficient procedures, which would reduce compliance costs and improve governance that would reduce the costs of corruption; and second, to the extent that increased revenues were channeled to social and economic expenditures directly benefiting the poor, to improve growth, job creation, and poverty reduction.

## **C. Objectives or Expected Outcome**

3. The project aimed to develop an effective, modernized, and efficient State Tax Service (STS),<sup>2</sup> which was to be measured by the following performance indicators: (i) large tax unit tax collections to increase by at least 17% per year during 2007–2012, (ii) number of new registrations to increase by 5.0% per year during 2008–2012 from a baseline of 1,884 in 2006, (iii) the average time required for firms to prepare tax returns is reduced to 170–195 hours in 2012 from 204 hours in 2006, and (iv) the average number of days firms spent in meetings with tax officials cut from 3.2 in 2005 to 2.8 by 2012.

## **D. Outputs**

4. Institutional strengthening, human resources development, and change management were key components of the project and these were supported by the two accompanying technical assistance (TA) projects.<sup>3</sup> Three outputs were targeted under the project: (i) an established central database and management information system (MIS), (ii) communication infrastructure developed for tax offices, and (iii) modernized central operations to improve taxpayer services.

## **E. Provision of Inputs**

5. Tax administration reform and modernization were addressed by installing information and communication technology (ICT); upgrading facilities; and institutional strengthening, including capacity building through TA. The two TA projects accompanying the project sought to strengthen (i) institutional capacities for tax administration reform, and (ii) help modernize tax administration through business process reengineering and change management. While the first TA project was successful, the second TA project achieved its objectives only partially because of time constraints. At appraisal, project cost was estimated at \$12.50 million equivalent, to be financed by a \$10.00 million ADB grant and by \$2.50 million from the government. The actual project cost at completion was \$12.06 million or 96.0% of the originally anticipated amount. ADB's actual expenditures amounted to \$9.38 million while the government's expenditures amounted to \$2.68 million—about 7.0% more than the original estimates.

## **F. Implementation Arrangements**

6. The Office of the Government was the executing agency and the STS was the implementing agency. A project steering committee headed by a representative from the

<sup>2</sup> The STS was previously known as the State Committee for Taxes and Collections.

<sup>3</sup> ADB. 2011. *Technical Assistance Completion Report: Institutional Strengthening and Capacity Building for Tax Administration Reform in the Kyrgyz Republic*. Manila; and ADB. 2011. *Technical Assistance Completion Report: Business Process Reengineering and Change Management for Tax Modernization in the Kyrgyz Republic*. Manila.

Office of the Government was set up to oversee and coordinate the establishment of the project, which was managed by a project management office (PMO). The PMO was headed by a project manager who was responsible for day-to-day project implementation. Delays in establishing a competent PMO, among others, led to the extension of the project until September 2013 (project completion report [PCR], para. 20).

## II. EVALUATION OF PERFORMANCE AND RATINGS

### A. Relevance of Design and Formulation

7. The PCR rated the project *relevant*. It was well aligned with the government's Country Development Strategy 2007-2010 and the subsequent National Sustainable Development Strategy for 2013–2017.<sup>4</sup> Both recognized the need to improve the fiscal space and reduce dependence on debt financing. Since 2002, the Kyrgyz Republic had been receiving assistance from multi-donors, such as the International Monetary Fund, to improve tax policy and administration and to modernize the tax code. The ADB project provided substantial assistance to improve tax administration and tax receipts, and modernize tax collection processes; this was closely supported by other development partners. Increasing tax revenues was considered essential to deal with high external public debt and reduce dependence on external partners. The project was included in the Joint Country Support Strategy, 2007–2010<sup>5</sup> and ADB's 2005 Country Strategy and Program Update.<sup>6</sup>

8. At appraisal, STS staff manually carried out a significant part of tax administration work. The design team determined that ICT could be introduced to reengineer business processes and improve revenue performance. Various measures were taken to develop appropriate software and improve the existing electronic database system initially used by 16 of the 64 tax offices. It was not until June 2009 that an Integrated Tax Administration System (ITAS) was developed to replace the previous one that was found to have deficient application processes.<sup>7</sup> New software solutions subsequently helped ensure that STS staff would fully accept and use ITAS, thereby reinforcing the relevance of project initiatives. The PCR stated that the project's relevance was improved through changes in system development and modernization of tax offices and less direct contact with taxpayers. This is further confirmed by the 2012 country assistance program evaluation (CAPE) findings.<sup>8</sup> This validation assesses the project *relevant*.

### B. Effectiveness in Achieving Project Outcomes and Outputs

9. The PCR rated the project *effective* based on the achievement of outcome and output indicator targets, as stated in the design and monitoring framework. On project outcomes, tax collections per year increased by 22.1% from 2007 to 2013 compared with 17.0% expected at project appraisal. Similarly, the number of new registrations in the STS electronic database increased by 60.4% per year from 2007 to 2013 compared with the 5.0% increases originally anticipated. Although not identified as an outcome indicator, this validation notes that tax

<sup>4</sup> Government of the Kyrgyz Republic. 2013. *National Sustainable Development Strategy for the Kyrgyz Republic, 2013–2017*. Bishkek.

<sup>5</sup> The Joint Country Support Strategy 2007–2010 was prepared by ADB, Swiss Cooperation, Department for International Development of the United Kingdom, United Nations agencies, and the World Bank Group and was closely aligned with the government's development goals.

<sup>6</sup> ADB. 2005. *Country Strategy and Program Update: Kyrgyz Republic, 2006–2008*. Manila.

<sup>7</sup> The PCR noted that the quality of the project preparatory TA, including the quality of TA consultants under this technical assistance, was less than satisfactory as it failed to identify correctly the deficiencies in the previous KITIS, which did not lend itself for upgrading.

<sup>8</sup> A 2012 CAPE rated ADB's country strategies and assistance programs in the Kyrgyz Republic *successful*. ADB's strategic positioning was rated *satisfactory*, its programs *relevant* and *effective*, and its resource use *efficient*.

administration expenses were reduced from 1.4% of net revenue collection in 2010 to 1.2% in 2011, indicating a more efficient use of resources by the STS. In addition, the use of ITAS by STS staff and the public showed steady improvement. However, due to less than anticipated improvements in the automation of tax declarations, expected improvements in average time spent preparing tax payments and in transacting business with tax officials fell short.

10. There were significant achievements on the three planned outputs stated in para. 4. On the first output, the project established the central tax database and MIS based on ITAS, which receives electronic information from all 61 STS tax offices. With the introduction of ITAS, the STS improved its automation level to a score of 2.6 in the overall range of 1–4,<sup>9</sup> suggesting that some of the STS functions and taxpayer services were still not fully automated. Nevertheless, “major improvements included faster report generation, a strong audit case selection process, and enhanced capacity for business intelligence.”<sup>10</sup> The second output, development of communication network for tax offices, was achieved with the financing of communication and network equipment for all STS offices and the modernization of 22 tax offices to install a communication and network infrastructure. The third output, establishment of modern central operations to improve taxpayer services, was largely achieved. An additional fourth and unplanned output was also achieved—project savings were utilized to establish 22 one-stop shops with no-contact windows—primarily to minimize corruption through open-plan offices, which lessened opportunities for rent-seeking through private discussions between tax administrators and tax officials. There were some elements of underperformance with the less-than-expected achievement in automation, the slow and gradual progress in the use of ITAS by STS staff, as well as the slow pace of electronic filing of taxpayer declarations. Nevertheless, as the achievements far outweighed the latter, this validation assesses the project *effective* in achieving the intended outcome of an effective, efficient, and a modernized STS.

### C. Efficiency of Resource Use in Achieving Outcomes and Outputs

11. The PCR rated the project *efficient*. The project had no cost overruns and delivered the expected outputs within budget—the total expenditure was \$12.06 million as against the approved amount of \$12.50 million. The savings were used efficiently to finance additional items such as the construction of one-stop shops. There were, however, delays in developing the central database and the MIS because of inefficient procurement and project management at the early stages of the project. Changes in software development from the Kyrgyzstan Integrated Tax Information System (KITIS) to ITAS also contributed to delayed implementation (PCR, paras. 20 and 39). Neither the project design nor the PCR included an estimation of the project’s EIRR; and efficiency was assessed from the perspective of process efficiency. This validation notes, however, that the increase in revenue collection and the reduction in government debt provide ample evidence to assume a calculation above the necessary threshold levels for the EIRR. This validation assesses the project *efficient* in achieving its outcomes and outputs.

### D. Preliminary Assessment of Sustainability

12. The PCR rated the project *likely sustainable*. The sustainability of outcomes in a project of this nature is largely dependent on the extent of the government’s commitment to build a strong in-house ICT capability and provide funding for the maintenance of communication infrastructure, servicing of software requirements, and upgrading staff capacity. At completion,

<sup>9</sup> ADB. 2013. *Toolkit for Tax Administration Management Information Systems*. Manila.

<sup>10</sup> Barreto, R. and R. Sinha. 2014. Implementing a Tax Administration System in the Kyrgyz Republic. *ADB Brief*. No. 29. Manila.

the share of tax administration expenditures allocated to ICT was low at 2.9% of total expenditures in 2011, and staff capabilities still needed to be enhanced.<sup>11</sup> Of the two accompanying TA projects, the capacity-building TA was rated sustainable but the business process reengineering TA was rated less sustainable because of complex software system issues identified during implementation. Government allocations are expected to increase because in 2015, the STS approved a new development strategy for 2015–2017, which aims to further modernize STS operations.<sup>12</sup> The government's commitment to improve funding and governance, develop social accountability, and enhance human resources development activities is further reflected in the development agenda in various policy documents such as ADB's Second Investment Climate Improvement Program; the National Sustainable Development Strategy (NSDS) for the Kyrgyz Republic, 2013–2017; ADB's country partnership strategy for the Kyrgyz Republic, 2013–2017; and the country partnership strategy of the World Bank Group, 2013–2017. Although sustainability on the surface may appear to be borderline likely/less likely sustainable, a more studied analysis of the development initiatives reflected in these policy documents and the actions taken since the PCR was written suggests that project outputs and outcomes will be sustained.<sup>13</sup> It is also significant that ADB and the STS continue after project completion to remain engaged in tax administration issues and in improving services to taxpayers through new initiatives. For these reasons, this validation assesses the project *likely sustainable*.

## E. Impact

13. The PCR rated the overall impact of the project *significant*. The expected impact from the project was “increased contribution of tax administration to fiscal consolidation and macroeconomic stability” (report and recommendation of the President, Appendix 3). This was achieved by increasing revenue, from 14.6% of GDP in 2005 to 18.1% of GDP in 2012. During the same period, external debt also declined from 69.8% of GDP in 2006 to 45.9% of GDP in 2012 (PCR, para. 42). The fiscal position would have been improved through these results, and it would be reasonable to infer that increased fiscal space would indirectly contribute to economic growth and poverty reduction through increased macroeconomic stability, minimized corruption, and reduced compliance costs. On this basis, this validation assesses the impact of the project *significant*.

## III. OTHER PERFORMANCE ASSESSMENTS

### A. Performance of the Borrower and Executing Agency

14. The PCR rated the performance of the STS *satisfactory*. The STS managed project implementation well despite some inadequacies in implementing the TA on business process

<sup>11</sup> ADB. 2014. *A Comparative Analysis of Tax Administration in Asia and the Pacific*. Manila. A study undertaken by Satoru Araki and Iris Claus found that the Kyrgyz Republic ranked low in the share of tax administration expenditures allocated to ICT.

<sup>12</sup> State Tax Service. 2014. *Development Strategy of the State Tax Service under the Government of the Kyrgyz Republic, 2015–2017*. Bishkek.

<sup>13</sup> The NSDS, Chapter 8, Section 8.2 states, “The major goal of the tax policy should be fostering economic development through improvement of business and investment climate by means of simplifying taxation, under the auspices of the Medium Term 2013–2017 Fiscal Policy Concept, which is now being finalized. This goal shall be achieved through a number of objectives: (i) equalization of the tax burden and improvement of the investment climate, (ii) ensuring completeness of tax collection; (iii) modernization of tax and customs services; and (iv) improvement in and automation of tax reporting.” In addition, ADB's Central and West Asia Department has since confirmed that the state enterprise responsible for maintaining the STS ICT systems (PCR, para. 40) has been established and is fully operational.

reengineering and change management for tax modernization.<sup>14</sup> In the first year, problems were encountered because the English proficiency of PMO staff was inadequate. This was overcome subsequently by recruiting English-proficient staff. Overall, the STS maintained stable performance despite the lack of full automation hindering effective taxpayer services, partly a result of the partially completed reengineering business processes TA at project completion. Nonetheless, this validation concurs with the PCR and considers the performance of the STS *satisfactory*.

## B. Performance of the Asian Development Bank

15. The PCR rated ADB performance *satisfactory*. ADB kept its supervision levels high as reflected by the number of review missions fielded and loan review mission reports produced. Constant monitoring and review appear to have paid off—technical issues arising from ICT and software development were addressed during review missions and prompt remedial measures were pursued. However, the PCR noted (para. 32) the minor disagreements with the STS regarding ADB's long review processes for replenishing the imprest account, but these were subsequently resolved. Overall, this validation considers ADB performance *satisfactory*.

## IV. OVERALL ASSESSMENT, LESSONS, AND RECOMMENDATIONS

### A. Overall Assessment and Ratings

16. This validation found the project *relevant, effective, efficient, and likely sustainable*, and its impact *significant* (see table). The project's major achievements could be summarized as follows: the project (i) helped increase tax revenues, which in turn contributed to fiscal consolidation and macroeconomic stability; (ii) strengthened and modernized central operations and the STS's capacity to plan, implement, and monitor taxpayer services and compliance programs; (iii) made use of the accompanying technical assistance to build staff capacities, prepare manuals, and strengthen skills, albeit with limitations due to shortcomings in implementing the business process reengineering TA; and (iv) helped increase efficiency in tax collection. Changes in project design during implementation, especially the development of ITAS in lieu of KITIS, laid the foundation for improvements in outcomes.

17. The project encountered delays initially due to language and procurement difficulties. By the very nature of their technological implications, ICT projects are also known to face time constraints and implementation delays. However, largely due to the determination of the government and the commitment of ADB, the project progressed satisfactorily and was successful in achieving its objectives. Overall, this validation assesses the project *successful*.

#### Overall Ratings

Criteria	PCR	IED Review	Reason for Disagreement and/or Comments
Relevance	Relevant	Relevant	
Effectiveness in achieving outcome	Effective	Effective	
Efficiency in achieving outcome and outputs	Efficient	Efficient	

<sup>14</sup> The project design could not have anticipated the difficulties associated with implementing KITIS, which had certain technical limitations as well as issues arising from software development with the changeover of systems from KITIS to ITAS.



Preliminary assessment of sustainability	Likely sustainable	Likely sustainable	Sustainability appeared to be borderline as stated by the PCR, but various initiatives of the government and ADB to push through with tax and governance reforms and remain engaged in pursuing further reforms post PCR makes the <i>likely sustainable</i> rating appropriate (para. 12).
<b>Overall assessment</b>	<b>Successful</b>	<b>Successful</b>	
Impact	Significant	Significant	
Borrower and executing agency	Satisfactory	Satisfactory	
Performance of ADB	Satisfactory	Satisfactory	
Quality of PCR		Satisfactory	See para. 25.

ADB = Asian Development Bank, IED = Independent Evaluation Department, PCR = project completion report.

Source: ADB Independent Evaluation Department.

## B. Lessons

18. Effective tax administration requires an effective automated registration, payment, collection, and monitoring system. Sharing the experience of other neighboring countries in implementing similar tax reforms and modernization will be helpful in further improving such systems.

19. As automation, information technology systems, and business process improvements take time, particularly in developing countries, considerable pre-project initiatives should be advanced to educate, train, and improve skills of intended beneficiaries, mainly implementing and executing agencies.

20. In introducing technological changes, business processes should be appropriately modified to suit emerging changes. The cooperation of business entities, including government agencies, should be solicited to streamline systems and procedures. The need to upgrade procedure manuals and expand ICT capability has been stressed in the PCR with which this validation concurs.

21. Project experience suggests that TA completion reports for the TA projects associated with the loans should be reviewed to derive lessons learned.

22. Projects that require substantial pre-project awareness of new technological interventions and arrangements to include capacity-building elements into project preparatory technical assistance should be considered essential and built into project documents.

## C. Recommendations for Follow-Up

23. This validation concurs with the PCR's recommendations and suggests that the following also be considered: a sustainable and robust tax system requires (i) a good and responsible tax administration that is independent and autonomous; (ii) an effective human resources management with people as the key movers of change; (iii) an adequate level of staffing and motivated, well-trained professionals with a high sense of duty and integrity; and (iv) a level of ownership of systems and procedures that confer legitimacy to changes in the tax administration system.

## V. OTHER CONSIDERATIONS AND FOLLOW-UP

### A. Monitoring and Evaluation Design, Implementation, and Utilization

24. The design and monitoring framework at project appraisal set achievable targets and identified assumptions and risks associated with implementation. However, in projects with high technological and innovative components, it is not always possible to anticipate the level of technical know-how required of government entities. Some of the issues encountered during implementation arose from the STS's lack of knowledge of systems and processes associated with implementing KITIS, which was subsequently changed to ITAS. Notwithstanding these learning difficulties, no major issues were encountered during project monitoring activities largely because ADB played an active role, keeping abreast of implementation bottlenecks through its review missions. Some of the targets set at appraisal were not reached because of inadequacies in the quality of staff and skill development programs, which were not completed on time.

### B. Comments on Project Completion Report Quality

25. The PCR has endeavored to be candid in presenting its findings and is of good quality. Technical issues are clearly outlined and the reader is given a perspective of the advantages of applying electronic systems for tax administration. The ratings are in line with the findings except with regard to sustainability where more information could have been provided on the steps being pursued by ADB to remain engaged with the STS and the proactive measures being adopted by the government to ensure continued funding and logistical support to tax reforms. On the whole, this validation assesses the quality of the PCR *satisfactory*.

### C. Data Sources for Validation

26. In addition to the PCR, the following documents were consulted: (i) the report and recommendation of the President; (ii) loan review mission reports; (iii) Joint Country Support Strategy: Kyrgyz Republic, 2007–2010; (iv) the World Bank's new country partnership strategy for the Kyrgyz Republic, 2013–2017;<sup>15</sup> (v) ADB's country partnership strategy for the Kyrgyz Republic, 2013–2017; (vi) the NSDS for the Kyrgyz Republic, 2013–2017; (vii) ADB Brief No. 29: Implementing a Tax Administration System in the Kyrgyz Republic (December 2014); (viii) A Comparative Analysis of Tax Administration in Asia and the Pacific, April 2014; (ix) Development Strategy of the State Tax Service under the Government of the Kyrgyz Republic, 2015–2017; and the (x) ADB CAPE 2012.

### D. Recommendation for Independent Evaluation Department Follow-Up

27. None.

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<sup>15</sup> World Bank/International Finance Corporation. 2013. *Country Partnership Strategy for the Kyrgyz Republic, 2013–2017*. Washington, DC.