ADB

# Completion Report

Project Number: 36168
Loan Numbers: 2130/2131/2132
November 2012

# Sri Lanka: Fiscal Management Reform Program

Asian Development Bank

## CURRENCY EQUIVALENTS

Currency Unit – Sri Lanka rupee/s (SLRe/SLRs)

| | | At Appraisal | At Program Completion |
|---|---|---|---|
| | | 19 November 2000 | 31 December 2011 |
| SLRe1.00 | = | $0.01 | $0.01 |
| $1.00 | = | SLRs104.90 | SLRs114.93 |

## ABBREVIATIONS

| | | |
|---|---|---|
| ADB | – | Asian Development Bank |
| CDS | – | central depository system |
| FMEP | – | Fiscal Management Efficiency Project |
| FMRP | – | Fiscal Management Reform Program |
| GDP | – | gross domestic product |
| IICC | – | interagency implementation and coordination committee |
| IMF | – | International Monetary Fund |
| IRD | – | Inland Revenue Department |
| IT | – | information technology |
| ITMIS | | Integrated Treasury Management Information System |
| MOFP | – | Ministry of Finance and Planning |
| PAFMIS | – | public accounting and financial management information system |
| PSC | – | Public Service Commission |
| RAMIS | – | revenue administration management system |
| SDR | – | special drawing right |
| TA | – | technical assistance |
| TIN | – | taxpayer identification number |

## NOTES

(i) The fiscal year (FY) of the government and its agencies ends on 31 December. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2010 began on 1 January 2010 and ended on 31 December 2010.

(ii) In this report, "$" refers to US dollars.

| | |
|---|---|
| **Vice-President** | X. Zhao, Operations 1 |
| **Director General** | J. Miranda, South Asia Department (SARD) |
| **Director** | B. Carrasco, Public Management, Financial Sector and Trade Division, SARD |
| | |
| **Team leader** | S. Shah, Senior Financial Sector Specialist, SARD |
| **Team members** | A. Alipio, Associate Project Officer, SARD |
| | K. Formanes, Operations Assistant, SARD |

## CONTENTS

# BASIC DATA

## A. Loan Identification

| | | |
|---|---|---|
| 1. | Country | Sri Lanka |
| 2. | Loan Numbers | 2130, 2131, 2132 |
| 3. | Program and Project Title | Fiscal Management Reform Program |
| 4. | Borrower | Democratic Socialist Republic of Sri Lanka |
| 5. | Executing Agency | Ministry of Finance and Planning |
| 6. | Amount of Loans | |
| | 2130 | $45,000,000 |
| | 2131 | SDR6,672,000 |
| | 2132 | $15,000,000 |
| 7. | Program Completion Report Number | 1365 |

## B. Loan Data

| | | |
|---|---|---|
| 1. | Appraisal | |
| | – Date started | 20 October 2003 |
| | – Date completed | 30 October 2003 |
| 2. | Loan Negotiations | |
| | – Date started | 8 November 2004 |
| | – Date completed | 9 November 2004 |
| 3. | Date of Board Approval | 14 December 2004 |
| 4. | Date of Loan Agreement | 20 December 2004 |
| 5. | Date of Loan Effectiveness | |
| | – In loan agreement | 21 March 2005 |
| | – Actual | 21 December 2004 |
| | – Number of extensions | 0 |
| 6. | Closing Date | |
| | – In loan agreement | 30 June 2008 |

| | 2130 | 2131 | 2132 |
|---|---|---|---|
| – Actual | 11 Jun 2008 | TBD | TBD |
| – Number of Extensions | 0 | 2 | 3 |

7. Terms of loan

| | 2130 | 2131 | 2132 |
|---|---|---|---|
| – Interest rate during grace period | Libor-Based | Fixed | Libor-Based |
| – Interest rate during amortization | | | |
| – Maturity (number of years) | 15 | 32 | 25 |
| – Grace period (number of years) | 3 | 8 | 5 |

8. Terms of relending (if any) — None
   – Interest rate
   – Maturity (number of years)
   – Grace period (number of years)
   – Second-step borrower

9. Disbursements[a]
   a. Dates

| Loan 2130 | Initial Disbursement | Final Disbursement | Time Interval |
|---|---|---|---|
| | 22 December 2004 | 11 June 2008 | 42 months |
| | **Effective Date** | **Original Closing Date** | **Time Interval** |
| | 21 December 2004 | 30 June 2008 | 42 months |

| Loan 2131 | Initial Disbursement | Final Disbursement | Time Interval |
|---|---|---|---|
| | 5 May 2005 | 12 July 2012 | 87 months |
| | **Effective Date** | **Original Closing Date** | **Time Interval** |
| | 21 December 2004 | 30 June 2008 | 42 months |

| Loan 2132 | Initial Disbursement | Final Disbursement | Time Interval |
|---|---|---|---|
| | 1 June 2005 | 26 July 2012 | 86 months |
| | **Effective Date** | **Original Closing Date** | **Time Interval** |
| | 21 December 2004 | 30 June 2008 | 42 months |

TBD = to be determined.
[a] For Loans 2131 and 2132, final disbursement dates, amount cancelled, amount disbursed, and undisbursed balance are subject to change after finalization of liquidation of imprest account.

b. Amount

**Loan 2130** $45,000,000

**Program Loan Tranche Releases (in $ million)**

| Currency | Tranche 1 | Date | Tranche 2 | Date | Tranche 3 | Date | Total |
|---|---|---|---|---|---|---|---|
| $ | 15,000 | 22 Dec 2004 | 15,000 | 22 Dec 2006 | 15,000 | 11 Jun 2008 | 45,000 |

**Loan 2131 (in $ million)** SDR6,672,000 $10,294,986

| Category/Name | | Original Allocation | Last Revised Allocation | Amount Canceled | Net Amount Available | Amount Disbursed | Undis-bursed Balance |
|---|---|---|---|---|---|---|---|
| 01 Consulting | SDR | 5.938 | 5.938 | 0 | 5.938 | 4.557 | 1.381 |
| Services and Training | $ | 8.200 | 9.074 | | 9.074 | 6.946 | 2.128 |
| 02 Interest | SDR | 0.200 | 0.200 | 0 | 0.200 | 0.147 | 0.053 |
| Charge | $ | 0.300 | 0.308 | | 0.308 | 0.227 | 0.081 |
| 03 Unallocated | SDR | 0.534 | 0.534 | 0 | 0.534 | 0.000 | 0.534 |
| | $ | 1.500 | 0.823 | | 0.823 | 0.000 | 0.823 |
| 99 Imprest Account | $ | | | | 0.152 | 0.152 | 0.051 |
| **Total (SDR)** | | **6.672** | **6.672** | **0** | **6.672** | **4.807** | 1.968 |
| **Total $ equivalent** | | **10.000** | **10.295** | **TBD** | **10.357** | **7.325** | 3.031 |

| Loan 2132 (in $ million) | | SDR4,742,000 | | $6,000,000 | | |
|---|---|---|---|---|---|---|
| **Category** | **Original Allocation** | **Last Revised Allocation** | **Amount Canceled** | **Net Amount Available** | **Amount Disbursed** | **Undisbursed Balance** |
| 01-Equipment | 13.200 | 13.200 | 0 | 13.200 | 10.545 | 2.655 |
| 02-Civil Works | 0.000 | 0.070 | 0 | 0.070 | 0.034 | .0.036 |
| 03A-IRD-Training and Call Center | 0.000 | 0.210 | 0 | 0.210 | 0.066 | 0.144 |
| 03B-MOF-Training Center | 0.000 | 0.140 | 0 | 0.140 | 0.021 | 0.119 |
| 04-IDC | 0.800 | 0.800 | 0 | 0.800 | 0.615 | 0.185 |
| 05-Unallocated | 1.000 | 0.580 | 0 | 0.580 | 0.000 | 0.580 |
| 99-Imprest Acct | | | | | 0.007 | |
| **Total** | 15.000 | 15.000 | | 15.000 | 11.288 | 3.719 |

IDC = interest during construction, IRD = Inland Revenue Department, MOF = Ministry of Finance, TBD = to be determined.

10. Local Costs (financed)

| | 2131 | 2132 |
|---|---|---|
| - Amount ($) | 268,490 | 242,292 |
| - Percent of Local Costs | 9.43% | 115.00% |
| - Percent of Total Cost | 2.61% | 1.61% |

## C. Program and Project Data

1. Program and Project Costs ($ millions)

| Cost | Appraisal Estimate | | | Actual | | |
|---|---|---|---|---|---|---|
| | **2130** | **2131** | **2132** | **2130** | **2131** | **2132** |
| Foreign Exchange Cost | 45.000 | 7.400 | 15.000 | 45.000 | 7.618 | 14.790 |
| Local Currency Cost | 0.000 | 2.600 | 0.000 | 0.000 | 2.677 | 0.210 |
| **Total** | **45.000** | **10.000** | **15.000** | **45.000** | **10.295** | **15.000** |

2. Financing Plan ($ million)

| Cost | Appraisal Estimate | | | Actual | | |
|---|---|---|---|---|---|---|
| | **2130** | **2131** | **2132** | **2130** | **2131** | **2132** |
| Implementation Costs | | | | | | |
| Borrower Financed | | | | | | |
| ADB Financed | 45.000 | 9.700 | 14.200 | 45.000 | 9.984 | 14.200 |
| Other External Financing | | | | | | |
| **Total** | **45.000** | **9.700** | **14.200** | **45.000** | **9.984** | **14.200** |
| IDC costs | | | | | | |
| Borrower Financed | | | | | | |
| ADB Financed | 0.000 | 0.300 | 0.800 | 0.000 | 0.311 | 0.800 |
| Other External Financing | | | | | | |
| **Total** | **0.000** | **0.300** | **0.800** | **0.000** | **0.311** | **0.800** |

ADB = Asian Development Bank, IDC = interest during construction.

3. Cost Breakdown by Program and Project Components ($ million)

| Component | Appraisal Estimate | Actual |
|---|---|---|
| A. Policy Loan | 45.000 | 45.000 |
| B. Capacity Building, Training and Project Administration | 8.200 | 7.225 |
| C. Revenue Administration Management Information System | 13.200 | 10.545 |
| D. Contingencies | 2.500 | 0.000 |
| E. Financing Charges | 1.100 | 0.842 |
| **Total** | 70.000 | 63.612 |

4. Project Schedule

| Item | Appraisal Estimate | Actual |
|---|---|---|
| Date of Contract with Consultants | | |
| R. de Vera | January 2005 | September 2005 |
| PricewaterhouseCoopers | January 2005 | November 2005 |
| S. Saxena | | December 2005 |
| B. Pollock | | January 2007 |
| C. Perera | | November 2007 |
| Equipment and Supplies | | |
| Dates | | |
| First Procurement | January 2005 | April 2007 |
| Last Procurement | June 2007 | December 2010 |
| Completion of Equipment Installation | December 2007 | December 2011 |

5. Program and Project Performance Report Ratings

| | Ratings | |
|---|---|---|
| **Implementation Period** | **Development Objectives** | **Implementation Progress** |
| **Loan 2130** | | |
| From 14 December 2004 to 11 June 2008 | Satisfactory | Satisfactory |
| **Loan 2131** | | |
| From 14 December 2004 to 31 December 2010 | Satisfactory | Satisfactory |
| **Loan 2132** | | |
| From 14 December 2004 to 31 December 2010 | Satisfactory | Satisfactory |

| As of October 2012 | Project Indicators |
|---|---|
| Project Rating | On Track |
| Technical | Yes |
| Contract Awards | 86.697% |
| Disbursement | 90.617% |
| Financial Management | Yes |
| Safeguard | Satisfactory |

### D. Data on Asian Development Bank Missions

| Name of Mission | Date | No. of Persons | No. of Person-Days | Specialization of Members[a] |
|---|---|---|---|---|
| Inception | 24–26 February 2005 | 4 | 12 | a, b, c, e |
| Review 1 | 12,13 May 2005 | 2 | 4 | a, b |
| Review 2 | 20–22 July 2005 | 1 | 3 | a |
| Review 3 | 24–30 August 2005 | 4 | 28 | a, b, c |
| Review 4 | 24–26 November 2005 | 2 | 6 | a |
| Review 5 | 25–28 January 2006 | 3 | 12 | a, c |
| Review 6 | 24–26 April 2006 | 1 | 3 | a |
| Review 7 | 1–3 August 2006 | 1 | 3 | a |
| Review 8 | 31 October–3 November 2006 | 1 | 4 | a |
| Review 9 | 7–9 March 2007 | 2 | 6 | a |
| Review 10 | 21–25 May 2007 | 1 | 5 | a |
| Review 11 | 3–7 December 2007 | 3 | 15 | a, b, e |
| Review 12 | 30 April–2 May 2008 | 2 | 6 | a, d |
| Review 13 | 25–26 May 2010 | 1 | 2 | a |
| Review 14 | 16–18 January 2012 | 2 | 4 | a, e |
| **Total** | | | **113** | |

[a] a = economist, b = financial specialist, c = public management specialist, d = young professional, e = project analyst

# I. PROGRAM DESCRIPTION

1. On 14 December 2004, the Asian Development Bank (ADB) approved the Fiscal Management Reform Program (FMRP)[1] for the equivalent of $70 million to the Democratic Socialist Republic of Sri Lanka. As a sector development program, the FMRP comprised three loans: (i) a program loan of $45 million to support fiscal management policy reforms; (ii) a project loan of $15 million for the Modernization of the Revenue Administration Project, mainly for procurement of the Revenue Administration Management Information System (RAMIS); and (iii) a technical assistance (TA) loan of SDR6,672,000 ($10 million equivalent) from ADB's Special Funds Resources, for the Institutional Strengthening of Fiscal Management Institutions through capacity building, including implementation of the FMRP. The FMRP was prepared on the basis of findings of project preparatory TA.[2]

2. The program loan's longer-term goal was to strengthen public finance in Sri Lanka and place public finances on a sustainable path. The program's medium-term objective was to create an enabling environment to foster mobilization of tax revenues and improve effectiveness of public expenditures. To meet this objective, the FMRP aimed to support improvements in five core areas: (i) effectiveness of tax collection through the creation of a modernized revenue administration, (ii) the budget framework, (iii) public expenditure management and control systems, (iv) fiscal discipline, and (v) fiscal coordination including through fiscal decentralization. The program became effective on 21 December 2004. The program framework is in Appendix 1.

# II. EVALUATION OF DESIGN AND IMPLEMENTATION

## A. Relevance of Design and Formulation

3. At the time of program design, Sri Lanka's unsustainable fiscal deficits—8.9% of gross domestic product (GDP) in 2002, excluding grants and privatization receipts, and caused primarily by impaired revenue collection and a concomitant large public debt—constituted the most critical challenge to the country's sustained growth and macroeconomic stability. Unsustainable current expenditures were increasingly eroding public physical and social capital expenditures and affecting poverty reduction, while also crowding out private investment. Revenue collection was constrained by a weak, underfunded tax administration whose weaknesses were exacerbated by institutional segmentation across tax departments. These problems were aggravated by a complex tax policy regime with distortions (e.g., exemptions, tax holidays, and amnesties) that discouraged taxpayer compliance. At the same time, there was increased pressure on scarce public resources, in particular resulting from subsidies to loss-making public enterprises and oil subsidies not fully reflected in the budget, military and election-induced spending, and ballooning debt service payments. Weak expenditure controls and insufficient linkages between fiscal objectives and the budget framework compromised the government's ability to prioritize expenditures and institute a sustainable fiscal approach. The sector development program was relevant to augmenting fiscal space, preserving macroeconomic stability, and ensuring greater investment and sustained growth. It judiciously combined policy reforms, institutional modernization, and capacity development to support strengthening of revenue departments and expenditure rationalization. It also laid the foundation for creation of more coherent and integrated administrative structures, more effective public service delivery and an enhanced ability on the part of the government to attract private sector participation.

---

[1] ADB. 2004. *Report and Recommendation of the President to the Board of Directors: Proposed Loans to the Democratic Socialist Republic of Sri Lanka for the Fiscal Management Reform Program.* Manila.

[2] ADB. 2002. *Technical Assistance (Financed by Japan Special Fund) to the Democratic Socialist Republic of Sri Lanka for Preparing the Public Sector Resource Management Project.* Manila.

4. During program preparation, the government, ADB, and development partners agreed that the program would focus primarily on supporting in-depth institutional reforms. ADB's support for enhanced revenue mobilization was intended to complement support for tax policy reforms from the International Monetary Fund (IMF). ADB's support for expenditure management reforms under the program would also complement the public expenditure review conducted by the World Bank and increase the chances of meeting the Poverty Reduction and Growth Facility fiscal target. The construction of a management information system for linking provincial councils with the finance commission under a United Nations Development Programme project would supplement ADB's actions on decentralization. The 2003 workshop jointly organized by ADB and the IMF as well as the January 2004 workshop provided opportunities for building understanding and reform ownership.

5. The program was in line with the government's objectives in the Fiscal Management (Responsibility) Act, which was approved by Parliament in 2003 and required the government to (i) reduce the overall budget deficit to 5% of GDP and total debt to 85% of GDP by the end of 2006, and (ii) enhance fiscal transparency and accountability.[3] The program was also consistent with the strategic priority of ADB's country strategy and program,[4] which sought to create greater fiscal space and contain Sri Lanka's public debt by (i) rationalizing spending and strengthening central and local governments; (ii) widening the revenue base; and (iii) enhancing fiscal management, while boosting the overall efficiency of government. The program built on past ADB assistance, including TA to strengthen the public expenditure management system,[5] and the Small and Medium Enterprise Sector Development Program Loan,[6] which partially addressed the issue of revenue. The program's components are summarized in Table 1.

**Table 1: Overview of the Sector Development Program**

| Assistance Area | Program Components | ADB Assistance |
|---|---|---|
| 1. Assist in improving public resource and expenditure management systems, promoting fiscal discipline, and supporting fiscal decentralization | **1.1 Revenue Collection**<br>Component 1: Creation of a Revenue Board<br>Component 2: HR and IT development strategies for MRA<br>Component 3: Implement taxpayer identity number<br>Component 4: Introduce risk management system for cargo clearance at Customs Dept.<br>Component 5: Introduce electronic tax filing for LTU taxpayers<br>**1.2 Budgeting and Expenditure Control**<br>Component 6: Establish MTBF<br>Component 7: Introduce expenditure ceilings<br>Component 8: Restructure key ministries<br>Component 9: Consolidate non statutory funds and bring into budget<br>Component 10: Introduce output indicators and eventually performance indicators<br>**1.3 Fiscal Decentralization**<br>Component 11: Improve coordination<br>Component 12: Institutional strengthening of FC<br>Component 13: Review criteria for inter-governmental transfers | Loan No. 2130–SRI: Fiscal Management Reform Program |
| 2. Capacity building support for the institutional development of the | Component 1: Consulting services and training<br>**Finance Commission**<br>Component 2: Capacity building for the strengthening of systems and procedures of fiscal decentralization | TA Loan No. 2131–SRI: Strengthening of the Fiscal Management |

3 *Gazette of the Democratic Socialist Republic of Sri Lanka*, 10 January 2003; and *Annual Report 2002 of the Central Bank of Sri Lanka*.
4 ADB. 2003. *Country Strategy and Program 2004–2008, Sri Lanka*. Colombo; and ADB. 2004. *Country Strategy and Program Update 2005–2006, Sri Lanka. Colombo.*
5 ADB. 1999. *Technical Assistance to* the *Democratic Socialist Republic of Sri Lanka for Strengthening Public Expenditure Management Systems.* Manila (TA 3301-SRI, completed in October 2003).
6 ADB. 2001. *Report and Recommendation of the President to the Board of Directors on Proposed Loans, Partial Credit Guarantee, and Technical Assistance to the Democratic Socialist Republic of Sri Lanka for Small and Medium Enterprise Sector Development Program*. Manila (Loans 1894/1895/1896).

| Assistance Area | Program Components | ADB Assistance |
|---|---|---|
| fiscal management institutions | **National Budget Department**<br>Component 3: Capacity building for the strengthening of systems and procedures of budget preparation, implementation, and evaluation<br>**State Accounts Department**<br>Component 4: Capacity building for the strengthening of systems and procedures of cash management and accounting reports<br>**Fiscal Analysis and Debt Management**<br>Component 5: Preparation of an actuarial balance analysis to identify stock of un-funded government liabilities, and develop of a liability management system<br>Component 6: Design and implement an effective foreign aid counterpart fund management system | Institutions Project |
| 3. Support institutional strengthening focusing primarily on the procurement of equipment for the modernization of revenue administration | Component 1: Provision of equipment for MRA<br>Component 2: Applications and technology to support a comprehensive, integrated, electronically enabled revenue administration management information system<br>Component 3: Provision of equipment for FC for the purpose of network linkage with provincial councils<br>Component 4: Training | Loan No. 2132–SRI: Modernization of the Revenue Administration Project |

ADB = Asian Development Bank, FC = Finance Commission, HR = human resources, ICT = information and communication technology, IT = information technology, LTU = large taxpayer unit, MOF = Ministry of Finance, MRA = modernized revenue administration, MTBF = Medium Term Budget Framework, TA = technical assistance.
Source: ADB. 2004. *Report and Recommendation of the President to the Board of Directors: Proposed Loans to the Democratic Socialist Republic of Sri Lanka for the Fiscal Management Reform Program.* Manila.

6. Although the overall goal of the program was ambitious in Sri Lanka's post-conflict context, the integrated approach—which combined institutional strengthening though policy reforms, provision of information technology (IT) equipment for modernization, and extensive capacity building—proved to be critical for building reform commitments across a broad range of stakeholders by providing demonstrable benefits and overcoming capacity weaknesses of the executing and implementing agencies.

## B. Program Outputs

7. In 2003, Sri Lanka was emerging from two decades of civil conflict, which had reduced the level of resources available. In evaluating the program, it is important to be aware of the external factors that severely affected Sri Lanka during the implementation period. Program implementation and the process of fiscal consolidation it sought to support, were disrupted by the impact of the December 2004 tsunami on an already stretched civil service, floods, high oil and food prices, fragile political coalitions, ongoing internal conflict in the country, and violations of the ceasefire agreement between the government and Liberation Tigers of Tamil Eelam. Presidential elections in November 2005 were held against this backdrop. A change in the project director in December 2005 caused further delays in the release of the second and third tranches.[7] Instability and turnover in the senior leadership of key government agencies also contributed to unpredictability in the decision-making process. Despite these setbacks, the program effectively supported the government in its bid to transform and modernize public finance institutions in Sri Lanka. The government made a deliberate and successful effort to institutionalize reforms by complying with 51 of the program's 55 policy actions. The program aimed to support a range of outputs under five broad components, as listed below.

[7] ADB. 2006. *Progress Report on Tranche Release for Sri Lanka: Fiscal Management Reform Program.* Manila; and ADB. 2008. *Progress Report on Release of Third Tranche for Loan 2130-SRI: Fiscal Management Reform Program*. Manila.

### 1. Component 1: More Effective Tax Administration

#### a. Creation of a Modernized Revenue Administration

8. The program supported the establishment of a more efficient administration structure and a more transparent, objective, and accountable incentives system in the revenue departments. The establishment of the revenue board was instrumental to overcoming fragmentation of revenue administration and improving coordination across the Inland Revenue Department (IRD), Customs Department, and Excise Department. The strategic plans for the three revenue departments helped mobilize support for achieving revenue collection targets consistent with the objectives of the Fiscal Responsibility Act. The program also helped strengthen reporting requirements and build greater accountability to Parliament and the public. A tax ombudsman was appointed and internal audit units were created.

9. The TA loan has fostered functional integration through human resource management reforms, including implementation of competency-acquired and merit-based employment systems and training programs. The human resource management plans prepared by each of the three revenue departments were vetted by the Public Service Commission (PSC), after some delays due to weak PSC capacity. The commitment to merit-based appointment, appraisal and promotion schemes, and the introduction of effective grievance reporting systems have strengthened staff morale and performance. An estimated 1,700 new staff were recruited in 2007 and early 2008 by IRD and the Customs Department as part of their skill upgrading drive.

10. The subcomponent financed under the Modernization of the Revenue Administration Project (Loan 2132) envisaged developing an integrated RAMIS to enhance the timeliness, reliability, and efficiency of information sharing across departments. However, capacity limitations in IT proved more severe than anticipated, and delayed implementation of the information development plan, despite support by consultants to the government in reviewing IT options. In March 2007, an agreement was reached to undertake a phased approach to automation, starting with enhancement of the existing computerized system, including (i) replacement of servers at IRD (effectively installed from the second quarter of 2008), (ii) database cleansing, (iii) e-filing improvements, (iv) development of automatic risk-based audit selection, and (v) automation of a stop-filer program.[8] A local and wide area network infrastructure contract was awarded in 2008 and implemented in 2009−2011. The procurement contract for RAMIS will be finalized during 2012–2013. Installation of RAMIS will be completed during 2013–2014, while operationalization of RAMIS is expected during 2014–2015. For the Customs Department, an automated system for customs data was upgraded and an automated risk-based cargo clearance system put in place that includes improvements in the electronic interchange system. Simpler customs clearance processes were also introduced for low-risk importers. In view of staffing constraints, the excise special provision unit was kept under the Customs Department rather than being transferred to the Excise Department as initially envisaged.

#### b. Strengthened Tax Collection and Compliance

11. In updating the Inland Revenue Act (No. 10 of 2006), incentives were included relating to income tax exemptions as well as tax rate relief and concessions offered under the Board of Investment Act, to ensure consistency between these laws. A Taxpayer Charter was published to strengthen awareness about the rights and obligations of taxpayers and tax collectors. Tax compliance has improved due to the establishment of a unique and unified taxpayer identification number (TIN), enforced in IRD and Customs Department tax filing operations, and the requirement that TINs be submitted for banking transactions. The benefits have been initially constrained,

[8] Registered tax payers who stop submitting tax returns to the Revenue Department.

however, as a result of delays in implementation of the stop-filer program caused by unanticipated IRD computer data server capacity limitations.

### 2. Component 2: Improving the Budget Framework

#### a. Streamlined Budget Procedures

12. This output aimed to support lower expenditures by implementing restructuring plans in five key ministries. Expenditures were to be limited and efficiency enhanced through internal reorganization, devolution of responsibilities to sub-national governments and across ministries, and outsourcing. Important progress has been achieved in two ministries. The independent ministries of finance and planning have been merged into a Ministry of Finance and Planning (MOFP), which integrates planning and budgeting under one authority. MOFP restructuring has additionally strengthened administrative efficiency and coordination. Monitoring of the implementation of large projects has improved following establishment of an operational and review unit, while the oversight functions of IRD and the customs and excise departments has been strengthened through creation of a revenue administrative unit. Restructuring of the Ministry of Education has strengthened aid coordination, project implementation, and policy formulation and clarified the allocation of responsibility and accountability between the central and other levels of government. Changes have not taken place in other departments, however, despite the findings of earlier public expenditure reviews.

13. Moreover, the program fostered additional reforms based on synergies. In its 2007 budget, the government introduced a rolling medium-term budget framework to anchor budget estimates over the coming 3 years and rationalize expenditures. In addition, important actions supporting a strengthening of fiscal decentralization included (i) the president's appointment of a high-level committee to formulate a medium-term program to strengthen fiscal devolution; (ii) the creation in 2006 of the all-party review committee to review issues relating to administrative and fiscal intergovernmental relations, including fiscal devolution; and (iii) biannual meetings, beginning in May 2005, that brought together the national and provincial ministers of finance to discuss intergovernmental finances.

### 3. Component 3: Improved Public Expenditure Management and Control

14. This component aimed to enhance the capabilities and accountability of government and public agencies in setting policies and strengthening effectiveness in the allocation and use of public resources.

#### a. Strengthened Management of Off-Budget Expenditures and Borrowings

15. Off-budget expenditures financed through independent ministerial funds and contingent liabilities such as guarantees tend to obscure budgetary planning and undermine expenditure control. To enhance public accountability, an inventory of non-statutory funds was prepared in 2006. Two of the seven funds identified were closed (the railway fine fund of the Ministry of Transport and the benevolent fund of the Ministry of Posts and Telecommunication), and three funds were regularized through their own statutes.

16. The amount of outstanding government guarantees was assessed at about $350 million (1.3% of GDP as of September 2007), and information on government guarantees, liabilities of government-owned enterprises, and a tentative computation of pension liabilities was reported in the Fiscal Management Report 2008. As of May 2008, 25 government-owned enterprises had been liquidated. A government asset management system was introduced as a monitoring mechanism for disbursement and recovery of government lending activities. Furthermore, the Treasury Department's website is posting information on an annual basis with regard to arrears by ministry

spending unit. However, an actuarial analysis to assess the magnitude of pension liabilities, to be followed by a funding plan, has not been undertaken.

#### b. Improved Cash and Asset Management Systems

17. The introduction of a computerized and fully integrated public accounting and financial management information system (PAFMIS) was expected to be undertaken with direct funding and support of operations from the Government of Korea. However, despite initial agreements the project was cancelled. Although ADB agreed to provide support for the PAFMIS under the program, the government's preference for a phased approach to automation resulted in delaying the procurement of the PAFMIS, now referred as the Integrated Treasury Management Information System (ITMIS), to 2012–2013. Nevertheless, the adoption of a centrally managed Treasury Fund Transfer System—in which the government's bank accounts are consolidated into two main accounts with a direct interface between the banks and the Treasury Department—helped to strengthen the Treasury Department's cash management, and enhanced resource allocation efficiency. The reduction in the number of idle accounts and unnecessary overdrafts also resulted in substantial savings.

### 4. Component 4: Strengthened Fiscal Discipline

18. This component aimed to improve budget planning and execution processes for enhancing budget predictability and improving budget performance. It sought to develop monitoring mechanisms to better manage commitments and ensure improved disclosure.

#### a. Improved Budget Estimates

19. Budget planning was to be made more effective by anchoring it on more reliable budget estimate procedures and strengthening of MOFP. Improved budget preparation consultation and better coordination across fiscal management institutions were integral to reaching an agreement on more realistic and credible annual and medium-term revenue estimates. Also, more rigorous analysis of the assumptions underlying the determination of expenditure ceilings and the preparation of alternative scenarios contributed to greater consistency between the budget and the macroeconomic framework. Transparency has also improved, with biannual reporting to Parliament of fiscal performance as well as provision of key estimates and assumptions for the current and next 2 fiscal years, website posting of detailed information on monthly expenditures and revenues, and more timely auditing. For some time, it appeared that the program had helped increase the ratio of actual total revenue collected relative to the original estimate (98.6% of the budget estimate in 2006, versus 91.5% in 2004) and contain expenditure within budget allocations (at 98.6% of the budget estimate in 2006). However, revenue performance was weaker in 2009 when actual revenue was only 83% of budget estimates, causing a large revenue deficit and significant underfunding of public investments.[9]

#### b. Reduced Distortions

20. This subcomponent sought to overcome the major obstacles for tax collection. Important progress has to be made by curtailing the discretionary powers of the Board of Investment to grant income tax incentives and setting a time limit for tax holidays (except investments in lagging regions and low-income housing). The legal framework was revised in 2008, tightening the process for approving tax exemptions to strategic development projects. In addition, the tax base was broadened significantly as a result of enhanced enforcement of the Revenue Act and the removal of tax exemption privileges for government employees, which was a strategically important action that signaled the government's serious commitment to tax reform.

---

[9] Government of the Democratic Socialist Republic of Sri Lanka, General Treasury. 2010. *Financial Statements for the Year ended 31December 2009.* Colombo.

### 5. Component 5: Improving Fiscal Coordination

#### a. Stronger Fiscal and Macroeconomic Coordination

21. Under the program, a stakeholder consultation system was initiated for preparing budget estimates, which included various government departments, the central bank, and chambers of commerce. The preparation of the development budget now integrates information from the national budget, and planning and external resources departments (discussed in the Fiscal Policy Committee meetings), while funding of the government's strategic development plan is determined under a medium-term budget programming and expenditure framework. An additional benefit of improved coordination has been improved treasury cash management to estimate borrowing requirements and the timing of bond issuance.

#### b. Enhanced Fiscal Decentralization

22. This output aimed to support the establishment of a structure for improving sub-national service delivery by clarifying central–provincial government relations, assessing capacity improvement, and increasing accountability at the provincial level. Political indecision has delayed establishment of a new Finance Commission Act, but other progress includes (i) development of a system of result-based indicators by the Finance Commission; (ii) its implementation in three ministries; and (iii) guidelines on extending its use for all provincial activities, which are expected to facilitate monitoring and foster better performance. In addition, the Finance Commission proposed reforms, based on the consultants' analysis, to enhance efficiency, transparency, simplicity, equity, and predictability of the intergovernmental transfer system, including by focusing transfer allocations on major sub-national spending categories such as education and health, and integrating various sources of funding for province-specific development into the medium-term expenditure framework.

## C. Program and Project Costs

23. Program and project costs are summarized in Table 2.

**Table 2: Program and Project Costs Financed by ADB**

| Allocation and Withdrawal of Loan Proceeds | | |
|---|---|---|
| | **At Approval** | **At Closure** |
| **Item** | **Amount Allocated** ($'000) | **Disbursed** ($'000) |
| **1. Program loan** | | |
| **Total program cost (Loan 2130)** | **45,000** | **45,000** |
| **2. Project loans** | | |
| 2.a Strengthening Fiscal Management Institutions: Capacity Building | | |
| Equipment, material and software | 0 | 0 |
| Consulting services, training | 8,200 | 6,946 |
| Financing charges | 300 | 227 |
| Unallocated | 1,500 | 0 |
| Imprest account | 0 | 152 |
| **Total cost (Loan 2131)** | **10,000** | **7,325** |
| 2.b.Modernization of the Revue Administration: Procurement | | |
| Equipment, material and software | 13,200 | 10,545 |
| Civil works | 0 | 34 |
| IRD/MOF training | 0 | 87 |
| Financing charges | 800 | 615 |
| Unallocated | 1,000 | 0 |
| Imprest account | 0 | 7 |
| **Total cost (Loan 2132)** | **15,000** | **11,288** |
| **Total projects costs (Loans 2131, 2132)** | **25,000** | **18,613** |

ADB = Asian Development Bank, IRD = Inland Revenue Department, MOF = Ministry of Finance.
Source: Loan Financial Information Services records.

## D. Disbursements

24. The government established the imprest account in December 2004. It was projected that disbursements for Loans 2130, 2131, and 2132 would be completed by 31 December 2007. The first tranche of the program loan was released on 22 December 2004. The release of the second tranche, initially targeted for June 2006, was delayed until December 2006. This resulted in a 6-month delay in disbursement of the third tranche as well (from December 2007 to 11 June 2008).

25. Total disbursements under Loan 2131 amounted to $7.3 million, compared to about $10.0 million anticipated at loan approval. An initial advance of $812,000 was provided for the Loan 2131 imprest account in May 2005.[10] The first disbursement took place in September 2005, 9 months after loan effectiveness. The final disbursement took place in October 2012.[11] Total disbursements under Loan 2132 were $11.2 million, compared with $15 million estimated at loan approval. An initial advance of $250,000 was provided for the imprest account of loan 2132 in November 2007. As of October 2012, the imprest account is expected to be fully liquidated. The first disbursement took place in June 2005, 6 months after loan effectiveness, and the last disbursement in October 2012. Although significant delays were encountered for Loan 2132 during first half of the project's implementation, about 60% of projected loan disbursements nevertheless took place before loan closing. A breakdown of actual disbursements by year is in Table 3.

**Table 3: Disbursement by Year**
($'000)

| Item | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Loan 2130 | 15,000 | 0 | 15,000 | 0 | 15,000 | 0 | 0 | 0 | 0 | 45,000 |
| Loan 2131 | | 340 | 1,200 | 1,606 | 1,741 | 704 | 1,555 | (61) | 240 | 7,325 |
| Interest charge (included above) | | 5 | 16 | 30 | 48 | 62 | 66 | 0 | 0 | 227 |
| Loan 2132[a] | | 13 | 45 | 134 | 253 | 195 | 1,221 | 1,946 | 7,481 | 11,288 |
| Interest charge (included above) | | 13 | 45 | 90 | 125 | 121 | 112 | 109 | 0 | 615 |
| **Total** | **15,000** | **371** | **16,306** | **1,860** | **17,167** | **1,082** | **2954** | **1,994** | **7,721** | **64,445** |

() = negative.
[a] As of 18 October, withdrawal application 0006 (for $2,800) is being processed by ADB Controller's Department.
Source: Asian Development Bank

## E. Program and Project Schedule

26. The reforms under the program were to be implemented over 3 years from December 2004 to December 2007. The original closing date for the program loan was 30 June 2008, with an actual closing date for Loan 2130 of 15 June 2008. This was achieved despite disruptions in program implementation caused by (i) the impact of the December 2004 tsunami on an already stretched civil service; (ii) presidential elections in November 2005; and (iii) a change in the program director (para. 29) in December 2005, which caused delays in the release of the second tranche.

27. Implementation of both the RAMIS procurement project and the TA was delayed. A terrorist attack in February 2009 on the IRD building where the program office was located caused damage and unavoidable delays in implementation of the training programs. There were two extensions for Loan 2131 (it was originally expected to be completed by 31 December 2007, with an initial extension to 30 June 2009, and a second extension to 31 December 2010), and three extensions for Loan 2132 (it was initially extended to 30 June 2009, with a second extension to 31 December 2010,

[10] As of 18 October, withdrawal application 00023 for $104,000 to liquidate the imprest account is being processed by ADB Controller's Department.
[11] To be updated upon full liquidation of loan.

and a third and final extension to 31 December 2011). The project loans are to be closed after full liquidation of the imprest accounts.

## F. Implementation Arrangements

28. As the executing agency, MOFP was responsible for overseeing, coordinating, and reporting on the implementation of both the program and project components of the FMRP through delegation to the interagency implementation and coordination committee (IICC), headed by the secretary to the Treasury, as well as a project implementation unit for the modernizing revenue administration project, headed by a program manager. Detailed implementation arrangements are in Appendix 3. In addition, the program steering committee—chaired by the secretary to the Treasury, and the highest MOFP body overseeing the program—discussed and approved the strategic plans. The program manager was recruited as part of the consulting services, and assisted by a deputy program manager funded by the government. At the request of the government, ADB agreed to a reversal of the positions.

29. This arrangement worked well initially, but personnel mobility disrupted both program and project implementation. The program manager was replaced in January 2006 due to a promotion, and the deputy secretary to the Treasury, who had been overseeing the FMRP, was reassigned. Nevertheless, the program steering committee—whose members include those under the IICC as well as union representatives from the revenue departments, and which is under the leadership of the secretary to the Treasury—played a more active role in program management and decision making regarding implementation.

30. Implementation arrangements were adequate in that the executing agency and interagency implementation and coordination committee were appropriately selected. The implementation arrangements—which were carefully designed and ensured representation by a broad range of stakeholders and facilitated consensus building as well as strong, high-level government ownership—were critical to overcoming the challenges to project implementation (paras. 26–29).

## G. Conditions and Covenants

31. There were no delays in meeting the conditions of effectiveness. All loans became effective on 21 December 2004, 1 day after the date of the loan agreement. The loan covenants were relevant and in line with the project requirements. Details on the status of compliance with loan covenants are in Appendix 4.

## H. Related Technical Assistance

32. Loan 2131 for the equivalent of $10 million from ADB's special funds resources was approved as part of the program to support institutional strengthening of fiscal management institutions through capacity building initiatives. At the initial stage of project implementation, a consultant assisted the program manager with procurement and consulting services inputs, and technical oversight of the program. PricewaterhouseCoopers' consultants worked until February 2008 to provide support with the implementation of the three loans under the program. With the help of the training consultant, capacity development programs were organized for the officials of IRD, the Customs and Excise Tax departments, Census and Statistics, MOFP, Finance Commission and provincial councils. Foreign training opportunities within and outside Asia were given to about 2,600 officers at various levels of management. These covered matters such as (i) comparative and international tax policy and administration, (ii) accounting and auditing techniques using computers, (iii) budgeting and financial management, (iv) fiscal decentralization, (v) customs management and control, and (vi) ITC skill development.

33. Project preparatory TA amounting to $500,000 was approved in August 2002, made effective in September 2002 and closed in October 2005 (footnote 2). The TA supported program formulation to assist the government lower the fiscal deficit by establishing a more effective and efficient fiscal administration through strengthening institutional capacity for revenue mobilization and expenditure management. The project preparatory TA adapted international tax reform experience to the Sri Lankan context. A consulting firm, BearingPoint, was recruited in accordance with ADB's Guidelines on the Use of Consultants and provided expertise in tax administration, human resource management, and IT systems. The project preparatory TA's major outputs were in general successfully implemented, and led to the approval and successful implementation of the ensuing program and project loans.

### I. Recruitment and Performance of Consultants, Contractors, and Suppliers

34. Upon loan approval, project loan 2131 called for inputs of 160 person-months of international and 270 person-months of national consulting services to strengthen the skills and knowhow of the inland revenue, customs and excise departments, national budget department, state account department, finance commission and other government institutions. Consultant performance is rated *satisfactory*. For project loan 2131, the largest contract for $2.74 million, was awarded to Price Waterhouse Coopers. The consultants of PricewaterhouseCoopers and, the National Institute of Public Finance and Policy, as well as individually recruited consultants (Sanjay Saxena, B. Pollock and C. Perera) worked closely with the project implementation unit and relevant government institutions. These consultants submitted their reports in a timely manner and the quality of their outputs was satisfactory. The recruitment of the consultants was done in accordance with Guidelines on the Use of Consultants by ADB and its borrowers.

35. Under project loan 2132, procurement methods available under the loan were international competitive bidding, national competitive bidding and shopping. The major procurement under project loan 2132 was the automation of the IRD and installation of local area network/wide area network. After an initial delay, disbursements under this contract amounted to about $9.9 million, or 90% of the total disbursement. Other items procured under the loan for MOFP and IRD included computer equipment, upgrade of servers, upgrade of existing database software, and wireless local area network.

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

36. The government and MOFP's performance are rated *satisfactory*. Very good progress was made in implementing a complex set of reforms under the program, especially in view of the many challenges faced by the country such as internal conflict, fragile political coalitions, and a stretched civil service (para. 7). Implementation of the task list on the modernization of revenue administration, which covered an estimated 150 measures, is a tribute to the dedication and effort of the revenue departments to the reform agenda. High-level leadership played a critical role in keeping the program on track. The government gained credibility by improving security conditions, and a wide range of stakeholders supported the generally effective use of resources, increased transparency and consultation, and broad gains. The government demonstrated strong ownership and was actively involved in project supervision. The steering committee met frequently, on average once per quarter, which facilitated consensus building, especially in the face of unforeseen difficulties, and close oversight of the implementing agencies and consultants. Moreover, the government demonstrated adequate flexibility to overcome weak capacity and regulatory hurdles. MOFP submitted the audited project accounts and prepared the quarterly progress reports and project completion report as required. The government complied with all loan covenants and made budget funds available for institutions supported by the projects as required. However, with regard to the two project loans, implementation timelines were adversely affected due to limited IT and management

information system capacity at MOFP and the various government departments that constituted the interagency implementation and coordination committee.

### K. Performance of the Asian Development Bank

37. ADB's performance was *satisfactory*. Following loan effectiveness, ADB fielded 14 review missions for a total of 113 person-days. The review missions were effective in providing technical inputs, monitoring implementation progress, and coordinating with other development partners. Likewise, staff from the Sri Lanka Resident Mission provided valuable assistance in facilitating policy dialogue and evaluating bid documents. ADB helped settle the outstanding claims of the consulting firms.

38. ADB continued to pursue some subcomponents even after it became clear that, under the original design, they would not succeed as a result of technical problems or capacity constraints. The project scope was revised on a few occasions in a timely and systematic manner, enabling flexible adaptation to new technical information and implementation capacity assessments. This flexible approach, and close consultations to identify emerging government priorities, greatly contributed to good program and project outcomes.

## III. EVALUATION OF PERFORMANCE

### A. Relevance

39. The program is rated *relevant*. The overall thrust of the program—improving public resource and expenditure management systems, promoting fiscal discipline and supporting fiscal decentralization—was relevant. The program was also closely aligned with the government's development and fiscal consolidation objectives and ADB's medium-term operations strategy for Sri Lanka. Moreover, the Strengthening of Fiscal Management Institutions project helped promote the development of relevant skills and knowhow for fiscal institutions through capacity building support.

40. The design of the program and projects, which were processed and implemented jointly, made it possible to address highly complex and interlinked issues and set objectives that were sufficiently ambitious for fiscal consolidation. At the same time, the design enabled ADB to address the weak capacity of the implementing agencies. Both the TA loan and the procurement project for the modernization of revenue administration enhanced program implementation capacity and reinforced the government's ownership of reform.

41. While some of the activities were reprioritized, rescheduled, or dropped altogether—including those related to the restructuring of key ministries, implementation of human resource management plans, and establishment of the information technology plan—these changes did not significantly reduce the scope and the ultimate achievement of the program and projects.

### B. Effectiveness in Achieving Outcome

42. The program was *effective* in transforming and modernizing public finance institutions in Sri Lanka, and laid the foundation for strengthening public financial management and revenue management through necessary interventions in policy, institutional structures, and related processes. The greatest achievement under the program has been the transformation of the revenue administration into a more professional and effective tax administration, which is an outcome conducive to increased revenue collection. Important steps were taken towards the consolidation and restructuring of key ministries; this objective was not fully achieved, however, because it was diverted in the interest of seeking a more stable coalition in Parliament. At the same time, the government remained committed to restructuring institutions, rationalizing expenditures and

improving service delivery, and requested that ADB support such reforms under the Fiscal Management Efficiency Project (FMEP).[12] The FMRP has had several accomplishments that go beyond the projected deliverables, including: (i) increased awareness of the importance of human resource management in building the capacity of staff and raising their motivation to achieve the departmental goals of revenue collection, enforcement and customer services; (ii) incorporation of performance-based career progression and compensation into national policies of the PSC and National Salaries and Cadres Commission; (iii) agreement on participatory and transparent performance management processes and their link to incentives and promotion; (iv) agreement on merit-based criteria for promotion; and (v) demonstration of the advantages of including union representatives in departmental human resource committees. While the program provided the necessary impetus to institute reforms needed to create fiscal space, implementation of the information systems and capacity building measures supported under the FMEP will enable the government to consolidate efforts to improve central government public financial management and revenue administration.

## C. Efficiency in Achieving Outcome and Outputs

43. The project was *efficient* in achieving the outcome and outputs envisaged during appraisal. The program loan was entirely disbursed within the original implementation schedule. Although automation was delayed, important actions have been taken to upgrade the IT system, which have helped mitigate shortfalls (in term of effectiveness and efficiency) in increasing revenue. For both project loans, $18.613 million (approximately 74% of the total loan amount of $25.295 million equivalent) was disbursed. The project implementation period had to be extended by 2.5 years for project loan 2131 and 3.5 years for project loan 2132.

44. The key outcome has been the improvement—albeit slower than initially envisaged—in fiscal performance, as evidenced by a reduced primary fiscal deficit (from 2.1% of GDP in 2005 to 1.8% in 2007), and a reduced current account deficit (from 2.6% of GDP in 2005 to 1.6% in 2007). The result has been lower outstanding debt against the backdrop of increased public infrastructure investment, with total government debt declining from 90.6% of GDP in 2005 to 81.4% of GDP in 2008.

## D. Preliminary Assessment of Sustainability

45. The sustainability of project outcomes is *likely*. The extension of the TA loan facilitated further institutionalization of the changes. After delays with regard to RAMIS and PAFMIS (now referred as ITMIS), the procurement contract for both IT systems will be finalized during 2012–2013. Installation of RAMIS and ITMIS will be completed during 2013–2014, with both IT systems expected to become operational during 2014–2015, which is expected to yield additional benefits in terms of the effective management of public resources. Most importantly, fiscal consolidation is likely to continue, given ongoing effort. The fiscal deficit increased in 2008 and 2009 as a result of the fiscal stimulus response to the global crisis, but prudent fiscal policy has been implemented following stabilization of the economy. Nevertheless, the overall fiscal deficit of 7% of GDP in 2011 remains above the 5% of GDP target that was to be achieved by end of 2006 as per the 2003 Fiscal Management Responsibility Act.

46. Sustainability is likely to benefit from the support of Sri Lanka's development partners in the areas of public sector management, economic growth, governance, social development, and capacity development, guided by the government's 10-Year Horizon Development Framework 2006–2016. Under the Standby Facility from 2009, the IMF seeks to strengthen the country's fiscal position while ensuring the availability of resources for post-conflict reconstruction and relief efforts, rebuilding of international reserves, strengthening of Sri Lanka's domestic financial system, and

[12] ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Loan and Technical Assistance Grant to the Democratic Socialist Republic of Sri Lanka for the Fiscal Management Efficiency Project.* Manila.

protection of the most vulnerable in the country from the burden of the needed economic adjustment. The World Bank focuses primarily on improving the capacity of central and local government agencies to deliver services, enhancing income and quality of life of poor households through community development and livelihood improvement, and promoting economic growth through capacity development and improved access to and use of public information.

47. Despite these achievements, weaknesses and institutional gaps remain. Well defined institutional structures and capacities for managing RAMIS and ITMIS are not present within either MOFP or IRD. Effective management of these two IT systems will be a key enabler of public financial management and tax administration under FMEP. A project management team, supported by ADB consultants, has been established to manage these projects, but responsibility for IT management and operations will need to be transferred to MOFP and IRD. MOFP is planning key capacity-building initiatives to address these gaps, and is creating permanent structures for IT operations management in MOFP and IRD. In addition, structural and capacity gaps also exist in audit and investigation departments at IRD, which need to be strengthened to improve IRD's ability to monitor and enforce tax compliance. The government has expressed a strong commitment to further reform these key revenue institutions; further assistance will be needed to enhance the capacity and systems of these revenue institutions to ensure sustainability.

### E. Impact

48. The potential impact of the program and projects was achieved, notwithstanding the minor reduction in scope. There have been substantial development impacts affecting tax and revenue administration, public expenditure management, fiscal discipline, fiscal transparency, and fiscal decentralization. The program supported an integrated information technology development plan leading to the introduction of RAMIS. As a first phase, MOFP implemented the modernization of IRD, and developed TIN enforcement, which will be further strengthened in line with a single taxpayer database using an updated and cleansed TIN.

49. The program contributed to improved sustainability of public investments, particularly in the less-developed regions of the country, through more effective public resource management, enhanced fiscal space for social and economic development resulting from improved tax administration and compliance (as a result of better revenue management), and a more efficient public financial management system (as a result of integrating treasury management and developing human resource capacity in relevant departments). These development impacts directly contributed to successful implementation of various programs, including the IMF Emergency Program.

## IV. OVERALL ASSESSMENT AND RECOMMENDATIONS

### A. Overall Assessment

50. The program is rated *successful*.[13] The program achieved its outcome and outputs, as a result of the relevant, effective, and efficient design. The program's sustainability is ensured as a result of the strengthening of institutions through restructuring, process reengineering, capacity building, and the government's demonstrated commitment to reforms. Additional assistance from ADB through the FMEP and from other development partners such as the IMF is expected to further enhance the program's sustainability.

[13] Overall assessment is in accordance with the definition and guidelines of ADB's Independent Evaluation Department: http://www.adb.org/Documents/Guidelines/Evaluation/PPER-PSO/default.asp

## B. Lessons

51. **A sequence to reforms.** A key consideration in sequencing is that legislative and regulatory reforms require changes in the capacity of institutions (policy and rules), organizations charged with implementation, and the competencies of responsible government officers to change their management practices. This cascade of legislation–institutions–organizations–people provides a strategic sequence for reforms. However, in practice this is not a linear sequence. Rather, people (officials and stakeholders) are involved from the outset of the reform process. As policy reforms are an iterative, negotiated process, attention needs to be given to developing and maintaining a broad consensus for reform, as this is one of the most difficult and important challenges in sustaining change management processes. It is important to note that developing and maintaining a broad consensus for reform was one of the hallmarks of the FMRP that ensured unwavering government commitment to the program's strong legislative and regulatory reform content.

52. **Capacity constraints and project complexity.** In addition to appropriate reform sequencing, ambitious and complex programs and projects are more likely to succeed if significant attention is given to building the capability and ownership of a broad range of stakeholders. As a sector development program, the FMRP successfully tackled a wide range of issues within a short time frame, while also contributing significantly to human development in several key implementation agencies. Advisory services to government under the project were also effective in keeping the program on track, especially in technical areas where previous experience was limited.

53. **Developing "soft" capacities.** Institutionalizing change management practices among those charged with implementing reforms—such as the efforts undertaken in the program to provide staff with technical skills to implement systems and procedures at MOFP and the key revenue departments—requires upgrading of technical and change management competency. It is necessary to enable government to sustain capacity development programs beyond the life of a program (for example, by providing training experts, particularly to develop soft capacities).

## C. Recommendations

### 1. Program Related

54. **Future monitoring.** The Sri Lanka Resident Mission should play a greater role in future monitoring of output indicators and progress in policy reforms for upcoming programs in the public finance sector. Coordination and collaboration between the resident mission and ADB Headquarters should be strengthened at every stage of upcoming programs (from formulation to implementation) to ensure effective monitoring in support of program outcome and outputs.

55. **Covenants.** The covenants were relevant and in line with the program requirements. The covenants in the loan and program agreements should therefore be maintained in their existing form.

56. **Further action or follow-up.** The winding-up period for the two project loans was extended in October 2012 so that the controllers can process the remaining requests for liquidation and cancellation of unused funds, and ensure the two project loans can be financially closed in 2012.

57. **Additional assistance.** Given the importance of placing public finance on a sustainable path and improving the effectiveness of public expenditures, ADB should continue its policy dialogue with the government in the sector. Following the government's request, the FMEP was approved in March 2010 and is expected to be completed by the end of October 2013. The FMEP aims to increase the resources available for social and economic development through improved tax administration and compliance, and an efficient public financial management system. The expected outputs include (i) more accountable revenue management, (ii) more efficient expenditure management, and (iii) more capable public resource managers. To support FMEP's project

management unit in reengineering business processes to align with the applications for RAMIS and ITMIS, TA was provided on a grant basis by the Japan Special Fund (footnote 12). To further build on the work of FMRP and FMEP, a second FMEP will be finalized in 2014, using project preparatory TA in 2013.

58. **Timing of the program performance evaluation report.** It is recommended that a program performance evaluation report be prepared in 2013, in accordance with the timeline associated with fulfilling all the performance indicators and targets in the program's framework.

### 2. General

59. Adequate consultation with stakeholders is crucial during program formulation to avoid an inappropriate diagnosis, which can result in weaknesses in the policy matrix. Extensive consultation during early the stages of program processing led to the effective diagnosis of issues, and a strong and relevant proposed policy matrix. Detailed consultation during implementation also ensured sustained government ownership of the reforms. Program implementation was effective notwithstanding the unsettled political environment that prevailed during a portion of the implementation period.

60. The institutional capacity of implementing agencies needs to be carefully assessed so that reform measures can be prioritized accordingly and realistic timelines can be set. The program's successful achievements resulted largely from adoption of a strategic sequence for reforms and the strong support provided through capacity enhancement of the implementing agencies. The sector development program modality in the FMRP proved to be effective in supporting implementation of challenging legislative and regulatory reforms, through building of IT and change management capacity in the implementing agencies.

## ACHIEVEMENT OF PERFORMANCE TARGETS AND/OR INDICATORS IN DESIGN AND MONITORING FRAMEWORK FOR THE FISCAL MANAGEMENT REFORM PROGRAM

| Design Summary | Performance Targets and/or Indicators | Achievements |
|---|---|---|
| **Impact** | | |
| Strengthened public finances. | Improved overall performance assessed according to actual trends achieved on revenue and expenditure sides under the Government's medium-term reform program compared to quantified and time-bound targets in the Medium-Term Fiscal Program (MTFP) | 1. **Achieved** |
| | Fiscal discipline to be assessed against compliance with transparency and reporting requirements under the Fiscal Management (Responsibility) Act | 2. **Achieved** |
| | Fiscal decentralization assessed in accordance with increased own provincial share of expenditure and revenues in total provincial budgets | 3. **Achieved** |
| | Key fiscal reforms are successfully identified, prioritized, sequenced, and built into agreed frameworks, policies, strategies, and time-bound action plans | 4. **Achieved** |
| **Outcome** | | |
| Necessary conditions for improved public finances in place and functioning as intended | Tax and nontax revenue yields meeting time-bound targets laid out in the MTFP | 1. **Achieved** |
| | Timeliness and effectiveness of budget preparation, execution, and monitoring based on medium-term budget framework. | 2. **Achieved** |
| | More effective tax administration to be assessed against time-bound targets in MTFP for overall and primary fiscal deficits | 3. **Achieved** |
| | Improved budget framework | 4. **Achieved** |
| | Enhanced public expenditure management control systems assessed in accordance with targets in MTFP including public debt outstanding and debt service cost | 5. **Achieved** |
| | Greater fiscal discipline to be assessed against time-bound targets in MTFP regular and timely publication of key fiscal indicators | 6. **Achieved** |
| | Strengthened fiscal decentralization to be assessed against targets for | 7. **Achieved** |

| Design Summary | Performance Targets and/or Indicators | Achievements |
|---|---|---|
| | provincial council (PC) share of general government expenditures and revenues | |
| **Outputs** | | |
| Creation of a modernized revenue administration | Approved cabinet policy paper on modernized revenue administration (November 2004) | 1. **<u>Achieved</u>** |
| | Ministry of Finance and Planning (MOFP) approves and implements a task list with clearly defined time-bound actions to support the creation of the Modernizing Revenue Administration (November 2004) | 2. **<u>Achieved</u>** |
| | Modernization Strategies for inland revenue, customs, and excise departments in place (November 2004) | 3. **<u>Achieved</u>** |
| Better tax collection/ compliance and strengthened systems | MOFP submits to Parliament amendments to Value-Added Tax (VAT) and Inland Revenue (IR) acts to introduce revenue enhancing measures (November 2004) | 1. **<u>Achieved</u>** |
| | Introduction of Economic Service Charge (November 2004) | 2. **<u>Achieved</u>** |
| | Tax code updated and simplified (June 2006) | 3. **<u>Achieved</u>** |
| A streamlined budget procedure | National Budget Department (NBD) introduces effective use of expenditure ceilings for budget preparation of line agencies (November 2004) | 1. **<u>Achieved</u>** |
| | NBD and National Planning Department (NPD) to establish budget and planning guidelines for the purpose of unifying medium-term capital and recurrent budgeting procedures (June 2006) | 2. **<u>Achieved</u>** |
| Management of off-budget and expenditure borrowings strengthened | Inventory of special funds finalized and disclosed (November 2004) | 1. **<u>Achieved</u>** |
| | Guidelines for classification of off-budget liabilities as actual or contingent for central Government (June 2006) | 2. **<u>Achieved</u>** |
| Improved budget estimates | Creation of fiscal policy committee (FPC) responsible for formulating fiscal policy framework, monitoring fiscal performance, and ensuring discipline in budget preparation and execution (November 2004) | 1. **<u>Achieved</u>** |
| | As part of budget preparation, MOFP's | 2. **<u>Achieved</u>** |

| Design Summary | Performance Targets and/or Indicators | Achievements |
|---|---|---|
| | National Budget Department, Fiscal Policy Department, Research Department, and RB to meet, discuss, and reach agreement on annual and medium-term revenue estimates by source and based on reporting of critical assumptions for revenue projections (June 2006) | |
| Fiscal decentralization process strengthened | Finance Commission (FC) Act to be submitted to Parliament | 1. **Not achieved** Establishment of a new Finance Commission Act was delayed. |
| | Government to establish (i) a high-level biannual meeting to discuss interprovincial and center-provincial issues and (ii) quarterly working group meetings to discuss PCs' implementation of resolutions of the high level meeting and on interprovincial and center-provincial issues (June 2006) | 2. **Achieved** |
| | FC to review intergovernment transfers criteria and report on the optimality of the current arrangement (December 2007) | 3. **Achieved** |

ADB = Asian Development Bank, BOI = Board of Investment, FC = Finance Commission, FMRP = Fiscal Management Reform Program, FPC = fiscal policy committee, HR = human resources, IR = Inland Revenue, IT = information technology, MIS = management information system, MOFP = Ministry of Finance and Planning, MTBF = medium-term budgeting framework, MTFP = medium-term fiscal program, NBD = National Budget Department, NPD = National Planning Department, PC = provincial council, PIU = project implementation unit, RAMIS = Revenue Administration Management Information System, RB = revenue board, TA = technical assistance, VAT = value-added tax.
Source: Asian Development Bank.

## TASK LIST FOR THE MODERNIZATION PROGRAM OF THE REVENUE ADMINISTRATION

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| **RB 1—Internal audit units to be created at HQ levels in all departments to report directly to the department heads** | | **01/06/05** | **Chief Advisor/Internal Audit Advisor** | **01/06/06** |
| 1 | Revise organizational structure to ensure unit reports directly to head | | | |
| 2 | Revise functional work of unit to ensure it exclusively deals with internal audit of systems and staff | | | |
| 3 | Develop operational procedures for the unit and position descriptions for staff | | | |
| 4 | Develop an annual work plan for the unit | | | |
| 5 | Train staff in internal audit techniques and staff irregularity investigation | | | |
| **RB 2—A code of ethics must be prepared, published and disseminated to all employees, tax practitioners and the public** | | **01/03/05** | **Chief Advisor/Internal Audit Advisor** | **30/06/05** |
| 1 | Draft a code of ethics | | | |
| 2 | Publish the code through posters and leaflets available at all revenue dept offices | | | |
| 3 | Each employee must be given a copy and must sign declaration of receipt thereof | | | |
| **RB 3—Design and deliver a program of education for employees on ethics and integrity** | | **01/07/05** | **Chief Advisor/Internal Audit Advisor** | **31/09/05** |
| 1 | Design short seminar for all employees | | | |
| 2 | Train managers in delivery of seminar | | | |
| 3 | Managers to deliver seminar to all employees | | | |
| **RB 4—Selected employees to make a declaration of assets and liabilities** | | **15/04/05** | **Chief Advisor/Internal Audit Advisor** | **15/04/05** |
| 1 | Design declaration of assets and liabilities | | | |
| 2 | Develop confidential secretariat to oversee and store declarations for commissioner secretaries and senior officers | | | |
| 3 | Develop procedures for all operational staff to submit “open” declaration | | | |
| 4 | IA staff to analyze declarations and make enquiries where necessary | | | |
| **RB 5, 7, 8, 9—Create a dedicated customer service department within each revenue department and a pilot joint ‘one-stop’ shop** | | **01/03/05** | **Chief Advisor/Internal Audit Advisor** | **01/03/06** |
| 1 | Revise operational structure to establish dedicated CSD | | | |
| 2 | Staff Department with appropriate personnel and develop position descriptions | | | |
| 3 | Develop policies and procedures for CSD | | | |
| 4 | Train personnel in customer service techniques | | | |
| 5 | Draft leaflets and brochures for public distribution | | | |
| 6 | Initiate a proactive taxpayer/trader education program | | | |
| 7 | Create a pilot one-stop shop in Colombo manned by staff from all departments | | | |
| 8 | Create dedicated CS desks in all departmental offices dealing with the public | | | |
| 9 | Create a call center to provide information and consultation to taxpayers | | | |
| **RB 6—Develop and publish a taxpayer charter and customs charter** | | **15/04/05** | **Chief Advisor/Internal Audit Advisor** | **15/07/05** |
| 1 | Draft taxpayer charter and customs charter | | | |
| 2 | Publish in media and through posters at all offices open to the public | | | |
| **RB 10—Establish consultative committees** | | **01/06/05** | **Chief Advisor/Internal Audit Advisor** | **01/12/05** |
| 1 | Establish high-level consultative committees for tax, customs and excise to include membership from accounting, legal and trade bodies as well as from all revenue departments. | | | |
| 2 | Feedback from committees to be passed to modernization teams | | | |
| **RB 11, 12—Centralize issue of rulings and ensure dissemination** | | **01/03/05** | **Chief Advisor/Internal Audit Advisor** | **31/07/05** |
| 1 | Create a unit responsible for the drafting and consolidation of all rulings | | | |
| 2 | Unit to publish and disseminate rulings to all operational staff and make such available publicly | | | |

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| **RB 13, 14, 15—Develop a streamlined appeals process across all revenue departments** | | **01/05/06** | **Chief Advisor/Internal Audit Advisor** | **01/11/06** |
| 1 | Establish an independent administrative panel to review appeals and make recommendations to the Ministry of Finance | | | |
| 2 | Develop procedures for a transparent and independent appeals process | | | |
| 3 | Draft clear and comprehensive guidelines to be disseminated to all staff and public | | | |
| **RB 16, 17—Establish a comprehensive and integrated management information system** | | **01/04/05** | **Chief Advisor/Internal Audit Advisor** | **31/09/07** |
| 1 | Interview functional heads and establish information requirements | | | |
| 2 | Review information inputs (declarations, etc.) and establish deficiencies | | | |
| 3 | Revise informational inputs to correct deficiencies | | | |
| 4 | Develop functional specifications for an automated MIS and supported by appropriate performance indicators | | | |
| **RB 18—Establish or a comprehensive human resource development program for inland revenue, customs, and excise departments** | | **01/04/05** | **Chief Advisor/Internal Audit Advisor** | **31/12/07** |
| 1 | Assess human resource needs based on (i) greater integration of revenue administration functions; (ii) the implications of workplace automation; and (iii) competency-based, skills-acquired staffing. | | | |
| 2 | Consolidate benefits and payment into basic wages in a transparent manner. | | | |
| 3 | Develop a HR development program to be approved by RB and MOFP with appropriated performance indicators. | | | |
| **RB 19—Develop strategic plans for all revenue departments** | | **01/04/05** | **Chief Advisor/Internal Audit Advisor** | **01/08/05** |
| 1 | Draft strategic plans for all functional units | | | |
| 2 | Draft strategic plan for each department | | | |
| 3 | Prepare institutional performance indicators for each functional unit/department. | | | |
| **RB 20—Establish a joint MOFP/revenue departments group to examine all proposed changes to the revenue legislation** | | **01/04/05** | **Chief Advisor/Internal Audit Advisor** | **01/08/05** |
| 1 | MOFP to establish a consultative group comprising representative from all revenue departments to ensure legislative changes are thoroughly considered for administrative input and are introduced on a timely basis | | | |
| **HR 15, 16, 17, 18—Establish a revenue administration training unit** | | **01/06/05** | **Chief Advisor/Training Advisor/Tax Proc./Customs/IT Advisors** | **30/06/06** |
| 1 | Establish core training team through competitive selection process | | | |
| 2 | Establish joint training facility in Colombo, to include IT laboratory | | | |
| 3 | Develop core training curriculum by priority | | | |
| 4 | Establish three regional training units | | | |
| 5 | Complete training needs assessment for all staff within the revenue departments | | | |
| 6 | Develop an interim training plan | | | |
| 7 | Complete train-the-trainer courses | | | |
| 8 | Develop an annual training plan for each department | | | |
| 9 | Training plan implemented | | | |
| **IRD1, CD10, IT9—Create a single taxpayer database operating on a unique and unified taxpayer identification number and used for all revenue activities** | | **01/04/05** | **Chief Advisor/Customs Advisor/IT Advisor** | **30/06/06** |
| 1 | Form a working group to improve the registration process in all departments, to identify the requirements for a separate trader database, and to develop an integrated master file of all revenue payers based on the TIN | | | |
| 2 | Cleanse the master file to update all records that are inactive and to ensure that the same individual or company is not registered twice | | | |

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| **Inland Revenue Modernization Program** | | | | |
| **IRD 2, 12—Develop simplified tax processes and procedures** | | **01/06/05** | **Chief Advisor/IT Advisor/Audit/Collection/Tax Admin-D.** | **31/05/06** |
| 1 | Create a Tax Procedures Simplification Unit | | | |
| 2 | Draft and agree to TOR, reporting requirements and deliverable schedule for the unit | | | |
| 3 | Fully document all current processes | | | |
| 4 | Develop new simplified processes making best use of automation | | | |
| **IRD 14—To identify and register taxpayers operating outside the tax net (non-filers)** | | **01/04/05** | **Chief Advisor/Tax Proc./Audit/Collection/Tax Admin-D.** | **30/03/06** |
| 1 | Create a RMU to draft procedures for non-filer program | | | |
| 2 | Draft and agree program including the setting of targets for district offices | | | |
| 3 | Review and agree to program and select pilot sites | | | |
| 4 | Implement program in pilot sites | | | |
| 5 | Review program and revise if necessary | | | |
| 6 | Rollout program for all district offices to implement | | | |
| **IRD 13—To identify and resolve taxpayer who fail to furnish tax returns (stop-filers)** | | **01/04/05** | **Chief Advisor/Tax Proc./Audit/Collection/Tax Admin-D.** | **31/03/06** |
| 1 | RMU to draft procedures for stop-filer program | | | |
| 2 | Draft and agree to program making full use of current automation | | | |
| 3 | Review and agree to program and select pilot sites | | | |
| 4 | Implement program in all offices with adequate automation | | | |
| 5 | Rollout program to all offices as automation improves | | | |
| **IRD 4, 5, 6, 7, 9, 10—Review the audit process and develop new streamlined and efficient procedures** | | **01/04/05** | **Chief Advisor/Audit/Tax Admin.-D./Bus. Proc.** | **31/03/07** |
| 1 | RMU to review and modernize the audit process within IRD | | | |
| 2 | Draft and agree to TOR, reporting requirements and deliverable schedule for the WG | | | |
| 3 | Draft report with recommendations on, as a minimum:<br>Audit selection methodology<br>Case selection, assignment and management<br>Coordinated audits | | | |
| 4 | Review/approve recommendations | | | |
| 5 | Draft new procedures to be included within a comprehensive audit manual | | | |
| 6 | Implement new procedures, including training | | | |
| **IRD 5, 6—Improve the efficiency and effectiveness of the LTU** | | **01/05/04** | **Chief Advisor/Audit/Tax Admin.-D./Bus. Proc.** | **31/12/06** |
| 1 | Audit of large taxpayers should be conducted in coordination with audit of company directors | | | |
| 2 | Audit of large taxpayers should be done using a team concept | | | |
| 3 | Provide training to auditors in the LTU for computer audit skills | | | |
| 4 | Draft procedures to streamline the data entry system in the LTU to provide for timely data input, which would permit effective monitoring of compliance | | | |
| 5 | Develop and implement an electronic tax filing and transaction database for comparative purposes<br>Regulate requirement for all taxpayers to report transaction values above a certain limit<br>Develop a database of transactions to be used for audit selection and comparative purposes, and ongoing review of transaction value<br>Extend the procedure to all large taxpayers outside the LTU | | | |

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| **Customs Modernization Program** | | | | |
| **CD 1, 2—Develop simplified customs processes and procedures** | | **01/09/04** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **30/09/06** |
| 1 | Create a CMU headed by a deputy director general that will review and recommend actions regarding tasks described below | | | |
| 2 | Draft and agree TOR, reporting requirements and deliverable schedule for the TF | | | |
| 3 | Fully document all current processes | | | |
| 4 | Develop and implement new simplified processes, making best use of automation | | | |
| **CD 3—Facilitate the payment of customs duties and fees at commercial banks** | | **01/09/04** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **01/02/06** |
| 1 | CMU to work in collaboration with departments, ICT agency, and commercial banks to establish a payment process for taxes and customs duties and electronic transfer of that information | | | |
| 2 | Draft and agree TOR, reporting requirements and deliverable schedule for the CMU | | | |
| 3 | Develop action plan | | | |
| 4 | Approve action plan | | | |
| 5 | Develop procedures and necessary automated support | | | |
| 6 | Institute new payments system | | | |
| **CD 4, 5, 6, 8—Introduce a full risk management system for cargo clearance including the introduction of a 'star' class facilitation program and other facilitation measures** | | **01/08/03** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **31/08/05** |
| 1 | CMU to take responsibilities for the following tasks. | | | |
| 2 | Draft and agree to TOR, reporting requirements and deliverable schedule for the CMU | | | |
| 3 | Evaluate current operational test of ASYCUDA selectivity module | | | |
| 4 | Develop selectivity structure using three channel system—red/yellow/green | | | |
| 5 | Approve the introduction of the new selectivity system as pilot | | | |
| 6 | Evaluate pilot and after any amendments approve rollout nationwide | | | |
| 7 | Develop "star" class facilitation program | | | |
| 8 | Select traders to participate in star class program | | | |
| 9 | Approve introduction of star class program | | | |
| 10 | Devise procedures and policies for random spot checks | | | |
| 11 | Approve procedures and policies for random spot checks | | | |
| 12 | Introduce random spot checks | | | |
| 13 | Devise procedures and policies for pre-import rulings | | | |
| 14 | Approve procedures and policies for pre-import rulings | | | |
| 15 | Introduce pre-import rulings | | | |
| **CD 7—Improve the customs valuation database** | | **30/09/04** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **30/06/06** |
| 1 | CMU to enhance valuation database | | | |
| 2 | Draft and agree to TOR, reporting requirements and deliverable schedule for the CMU | | | |
| 3 | Develop content and procedures for maintenance for valuation database including specifications for automation | | | |
| 4 | Approve development of valuation database | | | |
| 5 | Complete development work | | | |
| 6 | Rollout valuation database to all Customs posts | | | |
| **CD 11—Complete an equipment needs assessment** | | **01/05/05** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **01/03/06** |

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| 1 | Complete an equipment (non-IT) needs analysis for Customs with a draft report that includes:<br>Identified needs in excess of current inventory<br>Justification for equipment needs<br>Specifications for identified equipment needs<br>Estimated costs<br>Identification of any subsequent training needs | | | |
| 2 | Review and consider assessment and prepare budgetary projections accordingly | | | |
| **CD 12—Complete a review of examination and storage facilities and consider the introduction of DPs** | | **01/01/05** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **31/12/05** |
| 1 | CMU to review the examination and storage facilities currently in use | | | |
| 2 | Draft and agree TOR, reporting requirements and deliverable schedule for the CMU | | | |
| 3 | Draft report with recommendations to improve facilities and to include consideration on the use of DPs. The latter to include location, costs, and operational procedures for operation of decided feasible. | | | |
| 4 | Review/approve recommendations | | | |

**a. Excise Modernization Program**

| | | | | |
|---|---|---|---|---|
| **ED 1—Transfer the Excise Special Provisions Unit within Customs to the Excise Department** | | **01/03/05** | **Chief Advisor/Customs Advisor** | **01/10/07** |
| 1 | Create a EMU | | | |
| 2 | Draft and agree TOR, reporting requirements, and deliverable schedule for the EMU | | | |
| 3 | Draft report from WG with analysis and recommendations | | | |
| 4 | Evaluate/approve recommendations | | | |
| 5 | Fully integrate staff, resources, and work within the Excise Department | | | |
| **ED 3—Develop simplified excise processes and procedures** | | **01/03/05** | **Chief Advisor/Customs Advisor/Customs Advisor-D** | **30/09/07** |
| 1 | EMU to review and simplify excise tax procedures | | | |
| 2 | Draft and agree TOR, reporting requirements, and deliverable schedule for the EMU | | | |
| 3 | Fully document all current processes | | | |
| 4 | Develop new simplified processes making best use of automation | | | |
| 5 | Review and endorse new procedures as and when completed | | | |

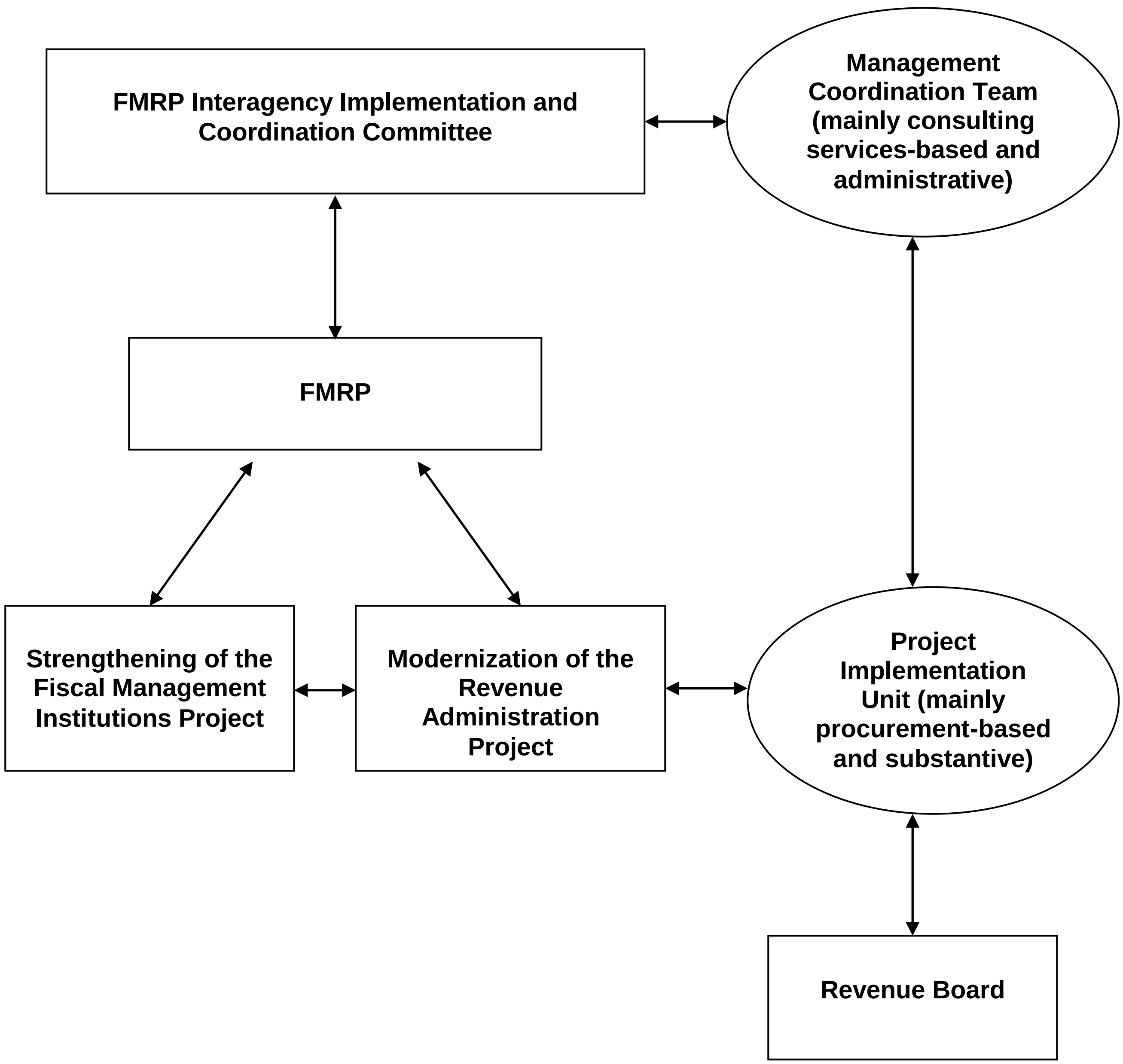
**b. Legislative Issues**

| | | | | |
|---|---|---|---|---|
| **Draft a new Administrative Code** | | **01/03/05** | **Tax Lawyer/Attorney-D/Chief Advisor/Tax Proc.** | **01/01/07** |
| 1 | Complete a comparative study of tax administration procedures in all the relevant statutes | | | |
| 2 | Draft a uniform Tax Administration Code | | | |
| 3 | Review and approve draft with Revenue Department. and other stakeholders | | | |
| 4 | Review/approve draft | | | |
| 5 | Submit draft to MOFP/Cabinet/Parliament | | | |
| 6 | Draft regulations and rules for implementation | | | |
| 7 | Review/adopt implementing procedures | | | |
| **CD 20—Review and revise current customs legislation** | | **01/06/05** | **Customs/Customs-D/Attorney-D/Chief Advisor** | **01/06/06** |
| 1 | CMU to oversee customs legislation | | | |
| 2 | Review and approve draft amendments | | | |
| 3 | Submit draft to MOFP/Cabinet/Parliament | | | |
| 4 | Draft regulations and rules for implementation | | | |
| 5 | Review/adopt implementing procedures | | | |
| **ED 7—Review and revise current excise legislation** | | **01/06/05** | **Attorney-D/Chief Advisor/Tax Proc.** | **01/06/06** |
| 1 | EMU to oversee the excise legislation | | | |

| Task Reference | Description of Task | Start Date | Resources | End Date |
|---|---|---|---|---|
| 2 | Review and approve draft amendments | | | |
| 3 | Submit draft to MOFP/Cabinet/Parliament | | | |
| 4 | Draft regulations and rules for implementation | | | |
| 5 | Review/adopt implementing procedures | | | |

ASYCUDA = automated system for customs data, CD = Customs Department, CMU = customs modernization unit, CS = customer service, CSD = customer service department, DP = dry ports, ED = Excise Department, EMU = Excise Modernization Department, HR = human resources, HQ = headquarters, IA = implementation agency, ICT = information and communication technology, IRD = Inland Revenue Department, IT = information technology, LTU = large taxpayer unit, MIS = management information system, MOFP = Ministry of Finance and Finance, RB = Revenue Board, RMU = Revenue Mobilization Unit, TIN = tax identification number, TOR = terms of reference, WG = working group.
Source: Asian Development Bank.

**ORGANIZATION CHART OF THE FISCAL MANAGEMENT REFORM PROGRAM IMPLEMENTATION AND COORDINATION ARRANGEMENTS**




FMRP = Fiscal Management Reform Program

## STATUS OF COMPLIANCE WITH LOAN COVENANTS

| Covenant | Reference in Loan Agreement | Status of Compliance |
|---|---|---|
| 1. MOFP will set up an FMRP interagency implementation and coordination committee to meet every quarter to coordinate and ensure the effective implementation of the reforms under the Program. | Section 4.01 for Loan 2131; Section 4.01(b) for Loan 2132 | **Complied with.** The PSC has been set up, and the members are meeting frequently to coordinate the effective implementation of the program and project reforms. The program manager and her team are functioning as the secretariat for the PSC in close consultations with other departments and agencies. |
| 2. (a) The Borrower shall (i) maintain, or cause to be maintained, separate accounts for the Project; (ii) have such accounts and related financial statements audited annually, in accordance with auditing standards consistently applied, by independent auditors whose qualifications, experience and terms of reference are acceptable to ADB; (iii) furnish to ADB, as soon as available but in any event not later than six (6) months after the end of each related fiscal year, certified copied of such audited accounts and financial statements and report of the auditors relating thereto (including the auditors' opinion on the use of the Loan proceeds and compliance with the covenants of the Loan Agreement as well as on the use of the procedures for imprest account/statement of expenditures), all in the English language; and (iv) furnish to ADB such other information concerning such accounts and financial statements and the audit thereof as ADB shall from time to time reasonably request.<br><br>(b) The Borrower shall enable ADB, upon ADB's request, to discuss the Borrower's financial statements for the Project and its financial affairs related to the Project from time to time with the Borrower's auditors, and shall authorize and require any representative of such auditors to participate in any such discussions requested by ADB, provided that any such discussion shall be conducted only in the presence of an authorized officer of the Borrower unless the Borrower shall otherwise agree. | Section 4.02 for Loan 2131; Section 4.05 for Loan 2132 | **Complied with.** Audited documents were prepared for FY2003, FY2004, FY2005, FY2006, FY2007, FY2008, FY2009, and FY 2010. |
| 3. The Borrower enables ADB's representatives to inspect the Project, the goods financed out of the proceeds of the Loan, and any relevant records and documents. | Section 4.04 for Loan 2131; Section 4.06 for Loan 2132 | **Not requested.** |
| 4. The Borrower shall furnish, cause to be furnished, to | Section 4.03 for | **Complied with.** |

| Covenant | Reference in Loan Agreement | Status of Compliance |
|---|---|---|
| ADB quarterly reports on the carrying out of the Project and on the operation and management of the Project facilities. | Loan 2131 | |
| 5. The Borrower shall cause competent and qualified consultants, acceptable to ADB, to be employed to an extent and upon terms and conditions satisfactory to the Borrower and ADB. | Section 4.03 (a) and (b) for Loan 2132 | **Complied with.** |
| 6. The Borrower shall cause the Project to be carried out in accordance with plans, design standards, specifications, work schedules and construction methods acceptable to ADB. The Borrower shall furnish, or cause to be furnished, to ADB, promptly after their preparation, such plans, design standards, specifications, and work schedules, and any material modifications subsequently made therein, in such detail as ADB shall reasonably request. | Section 4.03 (a) and (b) for Loan 2132 | **Complied with.** |
| 7. The Borrower shall cause the Project to be carried out with due diligence and efficiency and in conformity with sound administrative, financial engineering, environmental, information technology and financial management practices. | Section 4.01(a) for Loan 2130 and Loan 2132 | **Complied with.** |
| 8. The Borrower shall make available, promptly as needed, the funds, facilities, services and other resources with are required, in addition to the proceeds of the Loan, for the carrying out of the Program. | Section 4.04 for Loan 2130 | **Complied with.** |
| 9. The Borrower shall make available, promptly as needed, the funds, facilities, services and other resources with are required, in addition to the proceeds of the Loan, for the carrying out of the Project and the operation and maintenance of the Project facilities. | Section 4.02 for Loan 2132 | **Complied with.** |
| 10. The Borrower shall ensure that the Project facilities are operated, maintained and repaired in accordance with sound administrative, financial, engineering, environmental, information technology and maintenance and operational practices. | Section 4.07 for Loan 2132 | **Complied with.** |
| 11. The Borrower shall ensure that the activities of its departments and agencies with respect to the carrying out of the Program are conducted and coordinated in accordance with sound administrative policies and procedures. | Schedule 4.03 for Loan 2130 | **Complied with.** |

| Covenant | Reference in Loan Agreement | Status of Compliance |
|---|---|---|
| 12. The Borrower shall furnish, or cause to be furnished, to ADB all such reports and information as ADB shall reasonably request concerning: (i) the Counterpart Funds and the use thereof; and (ii) the implementation of the Program, including the accomplishment of the targets and carrying out of the actions set out in the Policy Letter. | Schedule 4.05 for Loan 2130 | **Complied with.** |
| 13. The Government shall effectively adhere to a fiscal consolidation adjustment path in accordance with its medium-term fiscal program and its fiscal consolidation strategy. | Schedule 5 for Loan 2130 | **Complied with.** The government established the fiscal committee, which is operating to ensure coordination of activities in preparation of the budget. The main assumptions for revenue estimation were published as part of the 2006 budget, as well as the fiscal responsibility requirements under the section, and technical details of the budget estimates for 2005 and 2006. The fiscal consolidation adjustment has been pursued in line with the medium-term fiscal program and its fiscal consolidation strategy. |
| 14. The MOFP will produce semiannual comprehensive statements of the general Government's financial position in the budget, showing all financial assets and liabilities, including commitments, guarantees, and contingent liabilities by 15 March and 15 September of each year. | Schedule 5 for Loan 2130 | **Substantially complied with.** The government has published a consolidated statement of financial performance for the year ending 31 December 2005, which includes the outstanding amount of (i) funded debts or loans, and (ii) any sinking funds. Moreover, the statement describes assets and liabilities directly related to receipts and payments as of the end of the 2005. The consolidated statement will be prepared on a continual |

| Covenant | Reference in Loan Agreement | Status of Compliance |
|---|---|---|
| | | basis. |
| 15. The Government will stop tax exemptions under BOI schemes to be transferred to IRD. | Schedule 5 for Loan 2130 | **Complied with.** The government has amended the consolidated IRA. The IRA amendment refers to any concession of tax exemptions, and is consistent with the tax code under the IRA. Moreover, a new regulation has been prepared under the BOI scheme to contain possible discretionary approvals, and it will be published soon. |
| 16. The Government will stop providing tax amnesties. | Schedule 5 for Loan 2130 | **Complied with.** The government has provided no new tax amnesties during program implementation. |

ADB = Asian Development Bank, BOI = Board of Investment, EA = executing agency, FMRP = Fiscal Management Reform Program, FY = fiscal year, IRA = Inland Revenue Act, Internal Revenue, IRD = Internal Revenue Department, MOFP = Ministry of Finance and Planning, PSC = program steering committee.
Source: Asian Development Bank.