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KYRGYZ REPUBLIC

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Quarterly Report



ECONOMIC REFORMS TO ENHANCE COMPETITIVENESS

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Significant issues affecting implementation:

- Political events of April 7-8, 2010, which resulted in the country's leadership change and overall instability, had impact on the EREC Project activities. The working group established for validating property data for KPTS delayed implementation of its activities. Also, EREC had to postpone the planned survey to measure taxpayer awareness. But the most significant harm to the project accomplishments and to the State Tax Service (STS) overall was the total destruction of the largest Rayon Tax Office, caused by fire and looting. Although these political events had a negative impact on the EREC Project activities in the Tax Administration area, the new State Tax Service Chairman is very supportive of the project initiatives and there is a good progress being made in their development.
- EREC Project received letters from the Project counterparts (STS, Ministry of Finance and National Bank of the Kyrgyz Republic), requesting technical and in-kind assistance. The requested assistance is outside of the Project current scope, and the letters were forwarded to USAID/Kyrgyzstan and USAID/CAR for their further consideration.

Significant meetings with counterparts & donors:

- Mr. Temir Sariyev, Acting Minister of Finance, Deputy Chairman of Interim Government
- Ms. Cholpon Saparbaeva, Head of Financial Reporting and Internal Audit Methodology Department, Ministry of Finance
- Ms. Dinara Shaidieva, State Secretary of the Ministry of Finance
- Mr. Adylbek Kasymaliev, Acting Chairman of the State Tax Service
- Mr. Matyev N., State Secretary of the STS
- Mr. Mambetkazyev N., Head of Registration Unit of the STS
- Mr. Mambetkadyrov N., Head of Appeal Unit of the STS
- Ms. Karimova B., Head of Local Taxes Department/STS
- Ms. Sharshkeeva R., Head of the Taxpayer Service Department of the STS
- Ms. Tumenbayeva E., Head of STS Training Unit
- Mr. Turdubayev S., Head of IT Department of STS
- Ms. Davletova J., IT Consultant at GosRegister
- Mr. Abylgaziev N., IT Consultant at GosRegister
- Mr. Emirov K., IT Consultant at GosRegister
- Mr. Junusov B., Head of the Property Registration Department of the GosRegister
- Ms. Makarenko L., Tax Law University Professor of KRSU
- Mr. Paul Goldberg, ADB Tax Modernization Project
- Mr. Kubanychbek Kulmatov, Acting Chairman of State Customs Committee
- Mr. Bekbolot Aliev, Head of the Revenue Department of the Ministry of Finance
- Mr. Azamat Tumenbaev, Advisor to the Minister of Economic Regulation
- Mr. Sultankulov R., Deputy Head of Audit Department of the STS
- Ms. Nursulu Ahmetova, Director of USAID Business Environment Improvement Project (BEI)
- Mr. Omuraliev, Director of the Training Center of the Ministry of Finance
- Mr. Adylbek Kasymaliev, Acting Chairman of the State Tax Service (STS)

- Ms. Aidaralieva R., Head of the Taxpayer Service of STS
- Mr. Mamanov N., Head of the Local Taxes and Methodology Unit of STS
- Mr. Kabirov T., Leading IT Specialist, National Bank of the KR
- Mr. Mambetakunov A., Head of the IT Department, National Bank
- Mr. Listvin O., Head of the Software Unit, National Bank
- Mr. Lewis Baurer, Team Leader of ADB Tax Modernization Project

A. Public Accounting & Audit

1. Highlights & accomplished tasks/activities against the work plan

- Ms. Shaidieva, State Secretary of the Ministry of Finance overseeing public sector accounting reform, noted ongoing technical assistance provided by USAID, in particular the recent development of an updated action plan on transition to IPSAS, work on the accounting regulation and staff training.
- EREC Project local consultants presented the final draft of the Accounting regulation to Ms. Cholpon Saparbaeva, Head of Financial Reporting and Internal Audit Methodology Department of the Ministry of Finance. The 268-page Accounting Regulation incorporates comments and suggestions proposed by the Department staff members.
- EREC Project presented to the Accounts Chamber the draft introductory section for the financial audit manual. The Accounts Chamber specialists provided their initial comments on it. EREC Project will meet with the Accounts Chamber and Ministry of Finance officials to discuss these comments and suggestions.
- EREC Project continued the second level (taxes and law) certified accounting practitioner course (CAP) for four staff members of the Financial Reporting and Internal Audit Methodology Department of the Ministry of Finance.
- Per the Ministry of Finance request, EREC Project provided a letter supporting the Kyrgyz Government's decision to implement International Public Sector Accounting Standards (IPSAS) using the cash-based accounting.

2. Future activities & events

- EREC Project will incorporate comments and suggestions to the introductory section of the financial audit manual provided by the Accounts Chamber and the Ministry of Finance.

B. Revenue Analysis

1. Highlights & accomplished tasks/activities against the work plan

- EREC Project prepared the report "Current Issues in Revenue Policy" 2009 Collections Performance and Analysis and submitted it to the Minister of Finance, Deputy Minister of Finance and Head of the MOF Revenue Department. A very illuminating factor in the report is that since the introduction of the new tax code on January 1, 2009 the consumption tax burden on the poorest sector of society increased by 19.2% while the wealthiest experienced a reduction of 14.9%. The report was also sent for wider

distribution to the Director of the USAID Business Environment Improvement Project and the Deputy Chairman of the Investment Council.

- EREC Project provided written recommendations to bring tax policy under the Ministry of Finance, to abolish the sales tax, increase the VAT rate to 16% and strengthen the operational independence of the State Tax Service by creating a criminal tax investigation function within the STS. EREC also recommended making the heads of Tax and Customs Services accountable to the Minister of Finance. Per the Minister of Finance request EREC Project wrote a letter to the Chairwoman of the Interim Government with the recommendations to bring the tax and customs policy under the MoF and abolish the sales tax.
- Per the Ministry of Finance request, EREC Project had a meeting with the Acting Minister of Finance to discuss areas of technical assistance to the Ministry in view of recent political events in Kyrgyzstan. The letter from the Acting Minister of Finance, requesting material and technical assistance, was forwarded to the USAID/Kyrgyzstan and USAID/CAR.
- EREC Project prepared recommendations to the Acting Minister of Finance in regard to the following:
 - draft Structure of the Government and, particularly, the MOF structure and the boundaries with the Minister of Economy,
 - tax and budget provisions of the Constitution.The recommendations on tax and budget provisions were also forwarded to the Constitutional Council.
- EREC Project met with the USAID Business Environment Improvement Project (BEI) to discuss the status of EREC recommendations on tax policy and revenues. Following the meeting EREC presented outline recommendations for the Interim Government on effective methods of calculating excise on tobacco and drinks, and on benefits of adopting a single tax number for customs and tax purposes. This would facilitate improved tax controls and the automated checking of VAT refunds.
- EREC Project participated in the Donor Economic Assessment Mission and took part in several meetings, including meetings with the Minister of Finance, Acting Chairman of the State Tax Service, Acting Chairman of the State Customs Committee, Head of the Revenue Department of the Ministry of Finance and Advisor to the Minister of Economic Regulation. The main goal of the meetings was to identify topical issues arising from the April 2010 events and establishment of the Interim Government. The Mission findings and recommendations will be presented at the conference on July 8, 2010.
- EREC Project collected data on the actual and forecasted revenue for 2010.
- EREC Project reviewed the proposed amendments to the Tax Code from legal perspective and provided recommendations to the STS, the MERT and the MOF.
- EREC Project Lawyer had a meeting with the Finance Minister to discuss tax policy issues and nationalization of the MOF's resort Dostuk. Based on the meeting results, EREC Project Lawyer prepared letters to the General Prosecutor's Office and the Property Ministry regarding the resort nationalization.

2. Future activities & events

- EREC Project will continue working on the Local Revenue Forecasting Methodology.

C. Tax Administration

1. Highlights & accomplished tasks/activities against the work plan

- Per the State Tax Service (STS) request, EREC Project met with the State Tax Service Acting Chairman Adylbek Kasymaliev to discuss the current situation within the STS and damage to the Pervomayskiy Tax Office. Mr. Kasymaliev expressed his intention to submit a request to USAID/Kyrgyzstan for funding restoration of the tax office and providing additional technical assistance to continue reforms that were commenced by USAID EREC Project. Follow up letters were forwarded to the USAID/Kyrgyzstan and to the USAID/CAR.
- EREC Project commenced working in the Methodology Commission under the Ministry of Economic Regulation for improvement of the Tax Code and Social Security Legislation. The Commission held 18 meetings to reconcile the amendments proposed to the Tax Code and address them to the Coordination Committee of the Interim Government.
- EREC Project made an analysis of the Customs Union (Russia, Kazakhstan, Belarus) impact on the Kyrgyzstan tax system.
- EREC Project started working on procedures for automated transmission of tax payment data from the Clearing Center of the National Bank to the State Tax Service. EREC made a review of applicable national legislation and held meetings on the subject with the IT staff of the National Bank of Kyrgyzstan.
- EREC Project made a presentation of the Work Measurement System (WMS) to the STS Chairman. The STS specialists reviewed the system and made certain proposals for modifying it. EREC and STS agreed to test the system in audit departments of the pilot tax offices. EREC Project commenced installing the Work Measurement System (WMS) in the pilot audit units. Public Outreach Specialist and IT team visited the Audit Department to see the facilities, install the WMS system and check connectivity of the Audit Department with the STS server. It was discovered that the Audit Department had only one computer for use by 22 auditors. Since this will prevent online submission of timesheets and audit results, it was agreed that the auditors would fill in their timesheets manually and submit them to an operator who would be entering the data.
- EREC Project participated in the meeting organized by the Acting Director of the National Agency for Local Government (NAMSU) to discuss the strategy and vision for local governments' development in view of the new Constitution adoption. The NAMSU Acting Director requested EREC Project to provide recommendations on funding mechanisms for local governments based on the best international practices. It was agreed that EREC Would provide recommendations in writing by the end of July.
- EREC Project met with the ADB Tax Modernization Project Team Leader to discuss the tax modernization program and in particular support for the Pervomaiski Tax Office which was completely destroyed.
- EREC Project completed the first part of analysis of Kyrgyz tobacco excise taxation and developed recommendations on its simplification.
- EREC Project developed the draft simplified corporate income tax computation accounting for small and medium enterprises.
- EREC Project received from the STS Audit Department the list of auditors working at the pilot audit departments for testing the Work Measurement System (WMS) developed by EREC. All users were entered into the WMS database, WMS installation disk was prepared and WMS database was deployed. Additionally, the IT Team modified the application in

accordance with the STS recommendations. The WMS guidance was revised according to the comments received from the STS.

- EREC Project continued administration and maintenance of the STS corporate network system. Continued providing assistance to the STS in relation to security and backup procedures.

2. Future activities & events

- EREC Project will continue administration and maintenance of the STS corporate network system. Will continue providing assistance to the STS in security and backup procedures
- EREC Project will continue working on developing the automated accounting system for collecting tax payment details coming from the National Bank Clearing Center.
- EREC Project will continue deploying the WMS application in the pilot tax offices. The WMS database will be deployed on the server and the users will be trained on the WMS operation.
- EREC Project will continue working in the Methodology Commission and the Working Group for making amendments and additions to the Tax Code and Social Security Legislation.
- EREC Project will draft the law proposing simplification of excise taxation of tobacco products.

D. KPTS development

1. Highlights & accomplished tasks/activities against the work plan

- EREC Project developed technical requirements for the centralized web-based Kyrgyz Property Tax System (KPTS). The data analysis was made and the core classes for KPTS development were modeled. EREC studied the issues of integration with external automated systems based on Java Business Integration and the Enterprise Service Bus (ESB) implementing products. Prepared the server for developing the source code with the repository support. Installed Debian, subversion, redmine, LDAP and their integration. EREC installed a web-server to support KPTS and necessary application server. Transferred the 'redmine' project management system data and the source code management system data.
- EREC Project developed business processes for tax deferrals and tax payments in installments, property tax sanctions, fines and penalties. Prepared the plan for initial population of data in KPTS, carrying out the function of filtration, verification and property classification by the property types. Designed references for (a) functional classification and (b) construction materials of property objects. Also, EREC Project obtained from the National Statistics Committee the Classifier of administrative and territorial units of the Kyrgyz republic. Based on this information, EREC made an analysis of the settlements and modified the settlements coding in the KPTS, in order to apply a simplified reference number.
- EREC Project continued analyzing and describing the KPTS object model.
- EREC Project organized a workshop on double entry accounting procedures for project analysts and programmers developing the Kyrgyz Property Tax System (KPTS). These

specialists are now aware of requirements for structuring the accounting module but yet they will need accounting experts to prepare the detailed technical requirement for the accounting module. Also, EREC had a meeting with the MOF Training Center Director to assess existing training programs on international accounting standards and, in particular, double entry bookkeeping.

- EREC Project, jointly with the MOF and STS experts, continued working on the KPTS reports. Also, EREC continued working with the STS officials on ensuring that the taxpayer notification forms, developed by the Project, will meet all requirements.
- EREC Project made preparations for the software development, which includes setting up the ant, jboss and jboss-seam programs and creating the system. The system was placed under the Subversion system management, which would allow the entire IT team to take part in further system development.
- EREC Project implemented the KPTS authentication mechanism, providing a subsystem for operation by users and defining user roles. The interface templates were transferred from the KPTS demo version and an administrative and territorial units' reference was implemented. The reference shall be used for determining the property object location. It covers oblast, rayon, and settlement.
- EREC Project configured the data received from the National Statistics Committee and imported it to the KPTS.
- EREC Project prepared a brief review of the GosRegister's database structure covering the mechanism of a new property entry to the database, the order of the code assignment, the Uniform Property Number card and entry of the technical parameters from Technical Passport to the database. In order to enhance the joint activities with the GosRegister, a series of meetings were held with the GosRegister's IT specialists. Based on the meetings results, a list of critical issues was prepared. It includes the issues related to the GosRegister database and the current Regulation on interaction between the STS and the GosRegister. The list was sent to the GosRegister.
- EREC Project prepared recommendations on developing the software application which would provide transfer of KITIS data to the KPTS. The GosRegister retains more substantial data on residential property while the STS maintains updated data on commercial property. Also, EREC had a meeting with the STS IT Department Head to discuss the KPTS and KITIS related issues and electronic filing. It was agreed to arrange a joint meeting with the STS and IFC experts.
- EREC Project made a review of the legal framework for allowances and preferences; studied the laws and regulations on the mapping, rules and principles for the property objects numeration. EREC also developed the universal property tax estimation forms for the objects of the first, second and third groups to reduce the quantity of the forms to be entered into and generated by KPTS. The forms will also be used in cases when a taxpayer disagrees with the tax accrued and for receiving information about an account or account elimination. The forms were submitted to the KPTS working group for reconciliation.
- EREC Project prepared the draft list of accounts and operations for the KPTS.
- EREC Project installed Java packages (Jboss server, Seam framework, Eclipse Galileo IDE, NetBeans, etc.) for developing Java WEB application. Continued analyzing and describing the KPTS object model.
- EREC Project started developing the concept for the process of collecting information on tax payment details directly from the Clearing Center of the National Bank.

- EREC Project prepared recommendations for improving the car taxation system in Kyrgyz Republic. The memo with recommendations was sent to Director of USAID Business Environment Improvement Project (BEI) for inclusion into combined USAID tax policy recommendations to the Interim Government.
- EREC Project commenced delivery of database and communications servers for development of the Kyrgyz Property Tax System (KPTS). The equipment will enable quality programming and collecting extensive volumes of property data for the system. EREC developed the appeal reports for inclusion into KPTS. Delivered and installed database and communications servers for the KPTS development. They were installed in a secure room of the State Tax Service. The programming is currently being performed using the new server.
- EREC Project, jointly with local consultants, continued development of the accounting module. The list of possible transactions and accounting entries related to the property tax accounting were discussed with the STS tax officials from the property tax unit and revenue department. It is expected that the local consultants will provide the draft accounting procedure for review and comments at the beginning of July.
- EREC Project continued working on KPTS reports with the MOF and STS experts.
- EREC Project held a meeting with the Central Treasury officers in order to obtain details of revenue account numbers of local self-governments to enable automatic revenue crediting to Treasury Accounts. The principle, which is currently being applied to KPTS, will be extended to all taxes. This new process can potentially save at least 200 job positions within the STS.
- EREC Project developed the mechanism of 'rule based' business logic and researched the ways of implementing the principles of double entry.
- EREC Project assisted in preparation of accounting procedures by independent consultants. EREC drafted a Chart of Accounts, listed KPTS operations and collated examples of double entry records based on the property 'object'.
- EREC Project developed new information sheets for collecting information, as the existing STS forms focus on taxpayers and not on the property. EREC developed the table that contains the codes for inhabited areas along with budget classification codes for Bishkek and Alamedin region. The names of inhabited areas and the National Statistics Committee codes were verified against the names and codes used by the Gosregister. The missing inhabited areas were clarified by local self-governments.
- EREC Project started designing items for the administration user's mode (KPTS references); continued analyzing and describing the object model of the KPTS; continued learning Seam WEB Development; continued drawing up charts of accounts and operations for an individual taxpayer account.

2. Future activities & events

- EREC Project will develop business processes and operations flowchart for tax preferences in KPTS. Make analysis of the current code system used by GosRegister and National Statistics Committee for the settlements.
- EREC Project will continue providing ad hoc advice to IT department of the STS on enhancement of the corporate network. Continue assisting in the administration of the STS corporate network.

- EREC Project will continue providing assistance on KITIS related issues at the request of STS.
- EREC Project will prepare a detailed technical requirement for the accounting module in the KPTS, which will cover: billing, interests' calculation, penalties application, payments processing, individual taxpayer accounts, transfers between accounts and control accounts functioning.
- EREC Project will design the property account number (PAN) structure and rules for PAN assigning, which include update of characteristics, elimination or suspension of an account.
- EREC Project will meet with the Acting Chairman of the National Bank of Kyrgyz Republic (NBKR) to review the issue of receiving property tax payment information electronically from the Clearing System and directly feeding it into the KPTS.
- EREC Project, jointly with local consultants, will finalize the accounting procedure for the KPTS.
- EREC Project will finalize the chart of accounts and operations of a personal tax account.
- EREC Project will design KPTS tables and screens and will continue developing the application. Also, EREC will continue analyzing and describing the KPTS object model.
- EREC Project will continue designing items of administration user's mode (KPTS references).
- EREC Project will start designing accounting subsystem of KPTS.
- EREC Project will develop the double entry based accounting module for KPTS.

E. Public Education & Outreach

1. Highlights & accomplished tasks/activities against the work plan

- EREC Project had a meeting with the newly appointed Acting Chairman of the STS to discuss the current and future public outreach activities. The Acting Chairman was briefed about the Work Measurement System developed by EREC; it was agreed that the WMS presentation to the Chairman would be held in early May.
- EREC Project had a meeting with the ADB Tax Administration Reform and Modernization Project to make a presentation of the Work Measurement System. ADB ICT Specialist was supportive of the WMS system stressing its benefits for the STS leadership in terms of resource management and planning.
- EREC Project supported organization of the 2nd university conference related to the Tax Code application in Kyrgyz Republic. The conference was held at the Kyrgyz-Russian Slavic University and was attended by the students and professors from the Kyrgyzstani universities, representatives of the State Tax Service, Ministry of Finance and international organizations. At the conference the University Representative thanked USAID for the assistance provided to the students and professors, particularly, with publication of the journal and one-year subscription to Toktom legal database. The students who produced the best research on the subject were awarded with diplomas from the USAID EREC Project and the State Tax Service. As a follow-up to the conference, EREC Project published a collection of research papers of KRSU University students and professors on tax policy and tax administration issues. The

research papers cover all main taxes effective in Kyrgyzstan, examine their application and burden on taxpayers and offer suggestions on improving the tax code. EREC issued a press release on research papers publication.

- EREC Project made an assessment of media and communications outreach at the Ministry of Finance. The meetings were held with the MOF Press Secretary and the IT Department Head. The assessment indicated that the MOF does not use its media resources to the full extent. The website provides little information on the state budget. At the weekly MOF meeting EREC Project, on the base of the assessment results, highlighted the necessity of improving the MOF media outreach. Particular attention was paid to the need of furnishing the MOF website with comprehensive updated budget information. The MOF State Secretary instructed the Department Heads to review relevant sections of the website and regularly update the budget information.
- EREC Project extended for one year the KRS University Finance and Credit Chair subscription to the 'Toktom' electronic legislation database. The database ensures access to the national and CIS laws for students of Economics Faculty and their professors.
- EREC Project revitalized the Joint Council initiative with the new STS Chairman, who supported its creation. The STS Chairman appointed the Council Secretary, who, jointly with EREC, commenced preparations for the meeting. The letters were sent to all Council members soliciting their proposals and topics for the first meeting. The STS received positive feedback from the Council members, who in their responses raised the most pressing issues that taxpayers face today. EREC Project and the STS developed an annual meeting plan, based on the proposals received. Also, the STS received telephone calls from the businesses willing to become members of the Joint Council and acknowledging the need for such a forum, where the taxpayers' problems could be addressed. All received proposals were forwarded to the STS Chairman, who will determine the date for the first meeting and approve the agenda.
- EREC Project made a recommendation to the new STS Chairman to continue issuance of tax brochures and leaflets. The proposed list of brochures for publication through the end of the year was discussed and supported by the Chairman. Three leaflets were drafted: on calculation of excise tax, on use of the excise stamp and on tax sanctions. Currently EREC Project is working on the leaflets design.

2. Future activities & events

- Due to the April political disturbances in Kyrgyz Republic it was decided to postpone the nationwide poll to measure the increase of public tax awareness.
- EREC Project will assist the STS in making preparations and conducting the first meeting of the STS Joint Council.
- EREC Project will continue writing and issuing tax leaflets and brochures.
- EREC Project will work with the Ministry of Finance on redesign of the MOF website.
- EREC Project will train users on WMS operation and monitor application of the Work Measurement System in pilot tax offices.