

ASIAN DEVELOPMENT BANK

TAR:KAZ 36403-02

TECHNICAL ASSISTANCE
(Cofinanced by the Governance Cooperation Fund)

TO THE
REPUBLIC OF KAZAKHSTAN
FOR
SUPPORTING LOCAL GOVERNMENT REFORMS

October 2003

CURRENCY EQUIVALENTS

(as of 2 September 2003)

Currency Unit	–	tenge (T)
T1.00	=	\$0.007
\$1.00	=	T147.69

ABBREVIATIONS

ADB	–	Asian Development Bank
EU-TACIS	–	European Union Technical Assistance for Commonwealth of Independent States
MEBP	–	Ministry of Economy and Budget Planning
TA	–	technical assistance
USAID	–	United States Agency for International Development

NOTE

In this report, "\$" refers to US dollars.

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I. INTRODUCTION

1. During the 2002 Country Programming Mission of the Asian Development Bank (ADB), the Government of Kazakhstan requested technical assistance (TA) for local government reform. Subsequent programming missions and missions related to the Governance Assessment¹ undertaken by ADB in cooperation with the Government, confirmed that reforms in this area are urgently needed. The TA was included in the 2002 Country Strategy and Program Update for Kazakhstan. It was also agreed that the TA would proceed in two phases.

2. The TA represents phase I of ADB assistance, and aims to develop a medium-term strategy for local government reforms by resolving basic issues in structuring administrative and financial relations between the central and local governments. Phase II will provide TA for implementing the recommendations arising from phase I. A Fact-Finding Mission fielded by ADB during 25 June-10 July 2003 reached an understanding with the Government on the objectives, scope, and implementation arrangements for phase I.² The TA framework is in Appendix 1.

II. ISSUES

3. Kazakhstan has three levels of local government. The oblast-level governments represent the 14 regions, and the cities of Astana and Almaty, whose status is similar to that of the regions. The raion-level governments represent the 195 smaller regions and cities, and the rural-level governments represent the 2,283 rural districts. The distribution of functions and authorities between these levels is at the discretion of the oblast government, and is often centralized at the oblast level.

4. The Law on Local Governance (No.148-II, January 2001) provides the legal basis for the oblast governments. Each oblast government has an executive body called the *akimat*, which is headed by the *akim*. According to the law, akims are representatives of the President and the Government (Constitution Article No. 87) and are appointed by the President. Each oblast also has an elected council, called the *maslikhat*. The oblast akims appoint the raion akims, and the raion akims in turn appoint the village akims. Civil servants working at the local level report both to central authorities and the local akimat under what is commonly referred to as the “dual subordination” system.

5. Oblast governments are generally responsible for building, operating, and maintaining typical municipal services, such as transport infrastructure, water and electricity, and law enforcement. They also administer health care, education, and poverty reduction programs. However, there is no explicit delineation of functions between the Republican and local governments. This results in overlapping of some functions performed by the local offices of the central government agencies, and those performed by local government bodies dealing with the delivery of similar services. In addition to wasting resources, the overlap and duplication of functions often create uncertainty regarding accountability.

6. Financial relations between central and local governments have been formalized to some degree over the past few years through the adoption of the Law on Budget System, the Law on Local Governance, and the Law on State and State-Guaranteed Borrowing and Debt.

¹ ADB. 2001. *Technical Assistance to Kazakhstan for Governance Study and Capacity Building for Administrative Reform*. Manila.

² The TA first appeared in *ADB Business Opportunities* in March 2003.

However, a stable and effective framework is still evolving. The local budget is prepared by the akim and the relevant members of the akimat. The budget is subject to the Budget System Law, and once approved, is consolidated into the national budget. While the initial revenue forecasts are prepared at the oblast level, they are often reviewed/amended by central authorities. When revisions are significant, local akimats have difficulties meeting their expenditure assignments.

7. Differences in resource endowment and development level result in an uneven distribution of revenue sources among the regions. For example, in 2002 the ratio of per capita revenue of the richest and the poorest oblast was 11.5. An effective mechanism for revenue equalization is therefore necessary to ensure equal access to public services for the population. However, the existing mechanism for intergovernmental fiscal transfers is not fully effective. As a result, per capita expenditures on social services such as health and education between regions show significant imbalances.

8. In acknowledging these concerns, the Government has made local government reforms one of its top priorities. The draft Law on Local Self-Government recently submitted to Parliament envisages local governments as separate legal entities. The Government has established the State Commission for Delineation of Authorities Between Levels of Government and Improvement of Intergovernment Fiscal Relations (State Commission), headed by the Prime Minister and managed by a working group of representatives from key ministries. The State Commission has prepared the Concept for Delineation of Authorities Between Levels of Government and Improvement of Intergovernment Fiscal Relations (Concept). Highlighting weaknesses in the current allocation of responsibilities among various levels of government and the methodologies for intergovernmental fiscal transfers, the Concept stipulates that each level of government be assigned clearly defined functions, and supported by adequate financial resources. The Concept has been approved by the President and adopted by the Government through Resolution No. 147, February 2003. While the development of the Concept provides a good starting point, the Government is keenly aware that the reform process will be long and complex, and that a well-developed strategy for implementing the reforms is needed. The TA will assist the Government by developing frameworks for functional and financial relations between various levels of government, and outlining a detailed strategy for sequencing and phasing necessary reforms.

9. ADB has undertaken a comprehensive Governance Assessment of Kazakhstan in close cooperation with the Government (footnote 1). The assessment emphasizes the urgency of local government reform and accordingly proposes ADB assistance during the reform process.

10. ADB has coordinated closely with Kazakhstan's other development partners. In the past the United Nations Development Program has been involved in developing the Civil Service Law and in conducting functional reviews of specific line ministries. The projects of the European Union Technical Assistance for Commonwealth of Independent States (EU-TACIS) are focused on civil service training, including an ongoing large-scale project aimed at training trainers in all oblasts. Under its Fiscal Reform Project, the United States Agency for International Development (USAID) has provided considerable support for implementing program budgeting, developing an improved budget code, and improving budget administration. USAID is also providing technical assistance for enhancing the transparency of intergovernmental fiscal transfers by developing models for estimating the revenue-generating capacity and the expenditure needs of each oblast. Given the relevance of this work, ADB will continue to coordinate closely with USAID during TA implementation. However, ADB's efforts will focus more broadly on intergovernmental functional and financial relations as they relate to

decentralization, and on developing a strategy for implementing necessary reforms over the medium term.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

11. The TA will assist the Government in developing a medium-term strategy for local government reforms by resolving basic issues in structuring central-local government relations. The outputs will be (i) a functional framework for improving the division of responsibilities between various levels of government; (ii) a financial framework for improving local governments' capacity to effectively undertake their expenditure responsibilities; and (iii) a medium-term strategy for implementing local government reforms.

B. Methodology and Key Activities

12. The TA will undertake the following:

1. Develop a Functional Framework

13. This activity will entail

- (i) conducting a functional analysis of public service delivery in selected oblasts, and identifying remaining inefficiencies and constraints;
- (ii) reviewing the division of responsibilities among various levels of government in light of the Concept developed by the Government;
- (iii) making recommendations, identifying specific conditions and criteria for the optimal delegation of responsibilities among various levels of government; and
- (iv) making recommendations for managing the traditional system of "dual subordination" of civil servants, and for improving accountability at each level of government.

2. Develop a Financial Framework

14. This activity will entail

- (i) reviewing expenditure and revenue arrangements in selected oblasts;
- (ii) outlining current procedures for revenue-sharing among oblasts, vertical and horizontal fiscal transfers between governments, intergovernmental loans, and market borrowing by local governments;
- (iii) reviewing the potential for improving local-level tax administration, and expanding the revenue base to reduce local governments' dependence on fiscal transfers; and

- (iv) making specific proposals for allocating revenue sources in line with expenditure assignments at each level of government.

3. Develop a Medium-Term Strategy for Implementing Local Government Reforms

15. This activity will entail

- (i) outlining alternative transition paths for decentralization and local government reforms, using (1) and (2) and incorporating relevant international experience;
- (ii) elaborating the legal and institutional changes involved in each transition path;
- (iii) detailing sequencing and phasing of reforms under each transition path; and
- (iv) conducting a workshop with participation from central and local governments and other local representatives, to discuss the transition strategy and medium-term action.

C. Cost and Financing

16. The total cost of the TA is estimated to be \$358,000 equivalent comprising \$210,000 in foreign exchange, and \$148,000 equivalent in local currency costs. The Government has requested ADB to finance \$250,000 equivalent, covering the entire foreign exchange cost of \$210,000 and \$40,000 equivalent of the local currency costs. The TA will be financed on a grant basis from the Governance Cooperation Fund³ (\$100,000) and ADB's TA funding program (\$150,000). The Government will finance the remaining \$108,000 equivalent. Detailed cost estimates are in Appendix 2.

D. Implementation Arrangements

17. The Ministry of Economy and Budget Planning (MEBP) will be the Executing Agency, and will provide necessary logistical support, workshop facilities, and counterpart staff. The TA will be implemented over a period of 8 months, beginning November 2003. The TA will require 6.5 person-months of services of an international consultant and 10 person-months of domestic consultants. The international consultant will be an expert on decentralization, with substantial experience in transitional economies. The three domestic consultants will be a local government organization expert, a fiscal reform expert, and a legal/regulatory reform expert. The consultants will be selected and engaged by ADB individually, and in accordance with its *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB for selecting and engaging domestic consultants. The consultant team will be responsible for procuring goods and services, which are required for the TA. Procurement will be in accordance with ADB's *Guidelines for Procurement*. The terms of reference for consultants are in Appendix 3.

18. The international consultant will be responsible for coordinating the inputs of the consultants. An inception report will be presented within 3 weeks of the start of services. The team will also prepare a midterm report on TA progress. The consultants will present a draft

³ The Governance Cooperation Fund is an umbrella fund with contributions from the Canadian and Norwegian governments, and is administered by ADB.

final report on all aspects of the TA 2 weeks before the end of the TA. The draft will be finalized upon receipt of comments from the Government and ADB.

IV. THE PRESIDENT'S DECISION

19. The President, acting under the authority delegated by the Board, has approved (i) ADB administering a portion of technical assistance not exceeding the equivalent of \$100,000 to be financed on a grant basis by the Governance Cooperation Fund, and (ii) ADB providing the balance not exceeding the equivalent of \$150,000 on a grant basis, to the Government of Kazakhstan for Supporting Local Government Reforms, and hereby reports this action to the Board.

TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Goal Efficient and equitable public service delivery</p>	<p>Different levels of government have clearly defined responsibilities.</p> <p>Local governments have adequate financial resources to fulfill their expenditure assignments.</p> <p>Accountability of local governments is improved.</p>	<p>Country reports</p> <p>Consultations with Government and other aid agencies</p>	<p>Macroeconomic and political stability</p> <p>Sustained political will and commitment to reforms</p>
<p>Purpose Develop a medium-term strategy for local government reforms by resolving basic issues in intergovernmental functional and financial relations</p>	<p>By July 2004: Framework for optimal division of labor between various levels of government has been identified.</p> <p>Financial framework for enabling local governments to fulfill their expenditure responsibilities has been developed.</p> <p>Alternative transition paths for local reforms are outlined.</p> <p>Government adopts strategy for implementing necessary reforms.</p>	<p>TA report</p> <p>TA review mission</p>	<p>Political will to undertake necessary reforms</p> <p>Limited institutional changes and staff turnover in relevant governments</p>
<p>Outputs Functional framework for optimal division of responsibilities between various levels of government</p>	<p>Detailed review of public service delivery at selected oblasts</p> <p>Conditions and criteria for optimal delegation</p>	<p>TA report</p> <p>TA review mission</p>	<p>Necessary information and cooperation provided by the Executing Agency and relevant local authorities</p>

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
<p>Financial framework for allocating revenue sources in line with expenditure assignments</p> <p>Medium-term strategy for implementing local government reforms</p>	<p>of responsibilities</p> <p>Specific recommendation for improving accountability at each level of government</p> <p>Review of expenditure and revenue arrangements at selected oblasts</p> <p>Assessment of potential for improving tax administration and expanding revenue base at local levels</p> <p>Specific proposals for allocating revenue sources in line with expenditure assignments at local levels</p> <p>Alternative transition paths with necessary institutional and legal reforms outlined</p> <p>Sequencing and phasing of necessary reforms clarified</p> <p>Workshop held to agree on and adopt reform strategy</p>		<p>Necessary information and cooperation provided by the Executing Agency and relevant local authorities</p> <p>Willingness of authorities to consider recommendations of the TA</p>
<p>Inputs</p> <p>Consultants</p>	<p>\$162,000 for 6.5 person-months of international consultant, and \$17,000 for 10 person-months of domestic consultants</p>		

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
Computer and facsimile machine	\$10,000		
Workshop	\$40,000		
Counterpart staff	\$47,000		
Government funding	\$108,000		
ADB	\$250,000 GCF: \$100,000 TASF: \$150,000		
Total	\$358,000		

COST ESTIMATES AND FINANCING PLAN
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration and Per Diem			
(i) International Consultant	162	0	162
(ii) Domestic Consultants	0	17	17
b. International and Local Travel	14	3	17
2. Office Space ^b	0	10	10
3. Equipment ^c	10	0	10
4. Translation and Miscellaneous Costs	4	5	9
5. Contingencies	20	5	25
Subtotal (A)	210	40	250
B. Government Financing			
1. Logistical Support	0	21	21
2. Counterpart Staff Remuneration	0	47	47
3. Workshop	0	40	40
Subtotal (B)	0	108	108
Total	210	148	358

^a Financed by the Governance Cooperation Fund (\$100,000) and ADB's TA funding program (\$150,000).

^b Due to space constraints, the Government has requested ADB to provide office accommodation.

^c Includes computer and facsimile machine. Equipment will be procured in accordance with *ADB's Guidelines for Procurement* through direct purchase procedure with quotations from at least three suppliers.

Source: Asian Development Bank estimates.

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

A. International Expert on Decentralization (6.5 person-months)

1. The consultant will be a decentralization expert, with extensive advisory experience in administrative and fiscal reforms in transitional economies. A working knowledge of Russian will be highly desirable. The consultant will serve as a team leader and coordinate the overall activities of the technical assistance (TA), working closely with counterpart staff from the Government and other consultants. The consultant will also coordinate closely with other aid agencies with related activities in Kazakhstan.

2. The terms of reference for the international consultant will include, but will not be limited to, the following:

- (i) Outline criteria and conditions for the optimal delegation of authority and responsibilities at each level of government, and the degree of consolidation and decentralization needed. Specify how this framework will improve public service delivery at the local level.
- (ii) Make recommendations for reforming the “dual subordination” system and reporting requirements for civil servants, and for transition arrangements for accountability at local levels.
- (iii) Clarify revenue and expenditure arrangements at local levels, including intergovernmental fiscal transfers and loans, and market borrowing by local governments.
- (iv) Review the scope for improving tax administration, and for expanding nontax revenue sources at the local level to reduce reliance on financial transfers.
- (v) Incorporating equity and efficiency considerations, recommend specific measures to allocate revenue sources in line with the expenditure responsibilities of local governments.
- (vi) Incorporating relevant international experience, outline alternative transition paths, elaborating in each case the design, implementation, and sequencing and phasing of necessary reforms.
- (vii) Organize workshop with the participation of central and local governments to agree on and adopt a medium-term strategy for decentralization and local reforms.

B. Domestic Local Government Organization Expert (4 person-months)

3. The consultant will have a strong background in local government administration and institutional reform. In conducting the functional review, the consultant will work closely with selected local-level governments. The terms of reference for the consultant will include, but not be limited to, the following:

- (i) Familiarize himself/herself with the main issues highlighted in the Concept for Delineation of Authorities Between Levels of Government and Improvement of Intergovernmental Fiscal prepared by the Government.
- (ii) Conduct detailed analysis of the operating environment for local governments. Aim, in particular, to identify specific problems related to the lack of clear delineation of functions and inadequate revenue sources.
- (iii) Clarify the implications of the traditional system of “dual subordination” of local civil servants, and suggest alternative arrangements for improving accountability and incentives of local-level governments.
- (iv) Assist the international consultant in organizing workshops and preparing TA reports.

C. Domestic Fiscal Reform Expert (4 person-months)

4. The consultant will be an expert on fiscal reforms, with strong knowledge of the budget system, intergovernmental fiscal issues, and local finances. In conducting the financial review, the consultant will work closely with selected local governments. The terms of reference for the consultant will include, but will not be limited to, the following:

- (i) Familiarize himself/herself with the main issues highlighted in the Concept for Delineation of Authorities Between Levels of Government and Improvement of Intergovernmental Fiscal prepared by the Government.
- (ii) Review expenditure and revenue arrangements at the local level.
- (iii) Outline current procedures for intergovernmental loans and fiscal transfers, and for market borrowing by local governments.
- (iv) Address the fiscal implications of the “dual subordination” of local tax collectors, and highlight other inefficiencies in local tax administration.
- (v) Assist the international consultant in organizing and conducting workshop and preparing reports.

D. Domestic Legal/Regulatory Expert (2 person-months)

5. The consultant will have a strong background in legal and regulatory reform. The consultant’s responsibilities will include, but will not be limited to, the following:

- (i) Review and provide advice on a relevant legal framework, including the Law on Local Governance, Law on Local Self-Governance, Law on the Budget System, and Law on State and State Guaranteed Borrowing and Debt.
- (i) Advise on the main legal issues pertaining to local reforms and decentralization, and identify specific legal reforms involved in the transition strategies recommended by the TA.