PROGRAMMATIC APPROACH CONCEPT PAPER

1. The programmatic approach of the Improving Domestic Resource Mobilization Program comprises three subprograms to be implemented during January 2014–December 2016. Subprogram 1 was implemented during January–September 2014, subprogram 2 is being implemented from October 2014–September 2015, and subprogram 3 is expected to be implemented during October 2015–December 2016.

2. The overall program is expected to deliver four outputs: (i) improved management of debt, cash and fiscal risk, (ii) strengthened revenue and public expenditure management, (iii) enhanced generation of domestic savings, and (iv) increased mobilization of private resources for investment.

3. The four outputs will be delivered through a set of policy actions chronologically sequenced over subprograms 1, 2 and 3, with each subprogram advancing the progress made in the preceding subprogram(s). The policy actions are presented in the policy matrix (Appendix 4 of the report and recommendation of the President). Subprogram 1 has been completed and approved by the ADB Board of Directors on 27 November 2014. The policy actions for subprogram 2 will be fulfilled before Board consideration, scheduled for 22 September 2015. The policy actions for subprograms 3 are indicative and may be revised to ensure consistency. Subprograms 2 and 3 will be submitted for Asian Development Bank (ADB) Board consideration upon completion of their respective policy actions.

4. The targets and indicators for each output and the overall impact will be tracked through the program design and monitoring framework (Appendix 1 of the report and recommendation of the President of each subprogram).

5. Subprogram 3 under each output will advance the progress made under the respective subprograms 1 and 2 as follows:

6. **Output 1: Improved management of debt, cash, and fiscal risk**. The objective of this output is to strengthen debt, cash, and fiscal risk management. Debt management is being strengthened by improving relevant government processes, increasing transparency, preparing and implementing strategies, amending legislation and developing analytical and forecasting capabilities. Fiscal risk management is being strengthened by drafting a strategy for dealing with the different types of fiscal risks and conducting risk assessments for these risks, including those associated with loan guarantees and other contingent liabilities. The requisite in-house capacity will be developed to assess and monitor such risks on an ongoing basis.

7. Subprogram 1 (i) established an internal procedures manual for external borrowing for investment financing and budget support; (ii) developed procedures manuals for public debt service processing, debt data recording, and validation for an efficient debt management and monitoring process; (iii) put into place a system of regular website posting of information on projects and programs financed by external sources covering total loan amounts and disbursed amounts reflected in the state budget, as well as a statistical bulletin on public debt presenting overall performance, treasury securities issuance, and transactions on primary markets; (iv) carried out an inventory indicating the fiscal position of large SOEs and their audited financial situation; and (v) developed a strategic template for monitoring and dealing with all types of fiscal risk confronting the country.

8. Subprogram 2 (i) prepared a Debt Strategy for medium term debt management covering loan portfolio, goals and principles for incurring new debt, and managing issues of debt sustainability; (ii) prepared an action plan to strengthen the Middle Office (analytical) function of the PDEFD for advising on terms of funding for government projects and evaluating public debt portfolio; (iii) developed a systematic process for debt and loan guarantees recordkeeping, reporting and validation; (iv) set up a dedicated analytical function for cash flow forecasting with adequate budget and personnel; (v) established a dedicated staffed and budgeted function to manage fiscal risks including contingent liabilities of SOEs and PPP projects; (vi) established procedures, assigned institutional responsibilities, and set aside adequate human and financial resources to monitor and advise on the management of the different types of fiscal risk confronting the government; and (vii) carried out a first complete assessment of a) macro risk, b) external debt sustainability, and c) reviewed risk associated with loan guarantees and other similar contingent liabilities.

9. Subprogram 3, building on the accomplishments of subprograms 1 and 2, will continue to improve the management of debt, cash and fiscal risk over the medium term. On the basis of the newly prepared debt strategy, the required legislative amendments will be submitted to the Parliament. The debt management and risk analysis systems will be upgraded, and a systematic process developed for tracking debt and loan guarantees and reporting on these areas in a timely manner in the government's financial statements. Information on contingent liabilities related to SOEs and public–private partnership projects will be provided.

10. **Output 2: Strengthened revenue and public expenditure management**. The objective of this output is to increase the effectiveness and efficiency of revenue collection, improve public expenditure management, and strengthen local government budget transfers. Because of a lack of internal capacity, the government in the past relied on external tax auditors under the umbrella of the Alternative Audit Program. Through increased recruitment and training efforts, these external auditors are being replaced by in-house tax auditors. Increased efforts have been made to collect tax dues and arrears, and write off certain categories of old tax liabilities deemed uncollectable Budgeting and budget execution functions of government entities are being increasingly integrated into the public financial management system and the treasury single account.

11. Subprogram 1 (i) implemented strengthened tax collection procedures by establishing a new administrative department; (ii) approved a strategy to reduce the statutory time limit of tax notices and taxpayer notices incrementally from 6 years to 3 years to shorten the tax liability imposition period and provide relief to taxpayers; (iii) approved an action plan to phase out the Alternative Audit Program and to increase in-house audit capacity in specialized sectors; (iv) prepared amendments to the budget code to allow the finances of local self-governments and legal entities of public law (LEPLs)[1] to be managed through the public financial management system, with payments and receipts through the treasury single account; (v) provided detailed supplementary information on types and funding of capital projects in the state budget documents; and (vi) paved the way for approval of the Local Self Governance Code by Parliament, resulting in reforms in intergovernmental finances including transfers.

12. Subprogram 2 (i) recovered arrears from active tax payers amounting to at least GEL80 million; (ii) reduced the statutory time limitation of tax notices and taxpayer notices from 6 to 5

[1] A number of general government functions are carried out by LEPLs. They collect and are allowed to retain income from services they provide. LEPL finances historically have been managed outside the treasury system. Payments by and to them flow through individual accounts held in commercial banks.

years, shortening the tax liability imposition period and providing relief to taxpayers; (iii) increased the number of in-house tax auditors to 286 (out of which 147 are women), correspondingly decreasing the number of alternative auditors; (iv) enabled cash operations of LSGs and LEPLs (except schools and kindergartens)[2] channeled through the TSA and the budgeting, budget execution and accounting processes through the PFMS; (v) MOESD identified gaps in the legal and regulatory framework for preparation, appraisal and implementation of public private partnership projects; and (vi) Government submitted to Parliament proposals for amendments to the Budgetary Code, defining the separation of revenues among the budgets of state, autonomous regions and municipalities.

13. Subprograms 3 will build on the accomplishments under subprogram 1 and 2. Reduction in time limitation of tax notices, writing off tax arrears of defunct businesses on the basis of legally approved categories, and increasing the number of in-house tax auditors to the full requirement will streamline tax collection efforts. Drafting of regulations for the preparation, appraisal, and implementation of public–private partnership projects will facilitate participation of the private sector in capital projects.

14. **Output 3: Enhanced generation of domestic savings**. The objective of this output is to reform the existing pension system to one that is adequate to prevent old-age poverty, affordable for both individuals and society, and sustainable over the foreseeable future. The aim is to streamline the government-funded universal pension (pillar zero)[3], and to establish an additional contributory pension savings scheme (containing elements of pillars 2 and 3).[4] The key areas of the pension structure are being designed defining issues such as membership contributions, investment of benefits, tax considerations, beneficiary arrangements, and relationship with the existing system.

15. Subprogram 1 (i) established a pension reform unit with adequate budget and staff and an interagency working group to devise a time-bound action plan to develop the new pension plan, and (ii) issued a public notification on the broad concept and direction of pension reforms, both mandatory and voluntary systems.[5]

16. Subprogram 2 (i) completed actuarial valuation of present and future cost of universal pensions under various scenarios; (ii) submitted to government the pension system revisions that would ensure continuity of equitable treatment for men and women; (iii) completed analysis of the key areas of pension system design and structure, incorporating mandatory and voluntary dimensions; (iv) issued consensual paper on the nature of hybrid pillars including issues such as membership, contributions, tax considerations, benefits, gender, and relationships with the zero pillar; (v) submitted to Cabinet for approval a strategy and time-bound action plan for pension reforms, including legal and regulatory gaps, data privacy and tax legislation; (vi) developed the approach for public awareness programs for zero and hybrid/joint pillars, outlining specific measures for continuity of equitable treatment of men and women; and

[2] There are more than 2,000 schools and kindergartens, many of them in remote and rural areas which do not strictly come under the purview of LEPLs.
[3] Pillar zero is the existing state run universal pension plan of the government, which offers basic coverage and is primarily focused on reducing poverty.
[4] Pillar II is a funded system that recipients and employers pay into, this includes pension funds and defined contribution savings plans. Pillar III is voluntary private funded accounts, including individual savings plans, insurance etc.
[5] The interagency council for pension reform has representation from the Ministry of Economy and Sustainable Development (MOESD), Ministry of Finance (MOF), the Ministry of Labor, Healthcare and Social Affairs (MOLHSA), the Office of the State Minister for Diaspora Issues, the National Bank of Georgia (NBG), the Budget and Finance Committee of the Parliament, and the National Statistics Office of Georgia.

(vii) completed the review of existing structure of private pensions to incorporate any required changes in the related legislation.

17. Under subprogram 3, the preparatory steps for implementation will take place, including the development of an individual account system, drafting of the legislation for the private pension savings scheme, and the launching of a nation-wide communications campaign.

18. **Output 4: Increased mobilization of private resources for investment**. The objective of this output is to develop capital markets to mobilize long-term finance, and to enhance access to finance through small-business financing, development, and gender targeting. Capital market reforms will include bond market development, legal and regulatory reforms, and money market instruments so they can contribute to pension reforms under output 3.

19. Subprogram 1 (i) built on the policies laid down under Georgia 2020 for the development of financial intermediation and mobilization of private investments; (ii) established an interagency committee and working group to devise a time-bound action plan on capital market reform and development;[6] (iii) established the Entrepreneurship Development Agency with staffing and allocated budget of GEL110 million for 2014–2018; (iv) established the Georgia Innovation and Technology Agency with staffing and allocated budget of GEL20 million for 2014–2016; (v) earmarked GEL3 million from its budget for a matching grant facility for micro, small, and medium-sized businesses with 20% reserved for businesses owned by women; (vi) earmarked GEL2 million from its budget for mini grants and innovation vouchers for private sector innovation and technology development with 20% reserved for businesses owned by women; and (vii) adopted a gender action plan to ensure equal participation of men and women in economic and business activities.

20. Subprogram 2 (i) issued a public notification on the concept and direction of capital market reforms, including corporate securities, expanding bond market and money market instruments for secured interbank trading; (ii) submitted to the Economic Council for approval, as a precursor to Cabinet, a strategy and time-bound action plan for capital market reforms, including addressing legal and regulatory gaps and improving the structure and efficiency of the market infrastructure; (iii) allocated a budget of GEL21 million to the Entrepreneurship Development Agency; (iv) allocated a budget of GEL6 million to the Georgia Innovation and Technology Agency; (v) EDA (within its budget) expanded matching grant facility for micro, small and medium-sized enterprises by GEL4 million, with 30% earmarked for women businesses; (vi) GITA (within its budget) expanded financial instruments to support private sector innovation and technology development with GEL3 million, with 30% earmarked for women businesses; and (vii) implemented the gender action plan and publicly reports on results included in the program policy areas such as small business training and financing. Additionally, EDA launched a new program “Produce in Georgia” with a component on micro and small enterprise development in rural areas, with a budget of GEL20 million (for 2015-2017). GITA created Geolab—a mobile training and knowledge-exchange platform and fablab—facility for research and development with a budget of GEL1.1 million. In addition 3 Innovation Labs (Ilabs) were created by GITA’s support, and construction of the first Techno Park in Georgia is ongoing.

21. Under subprogram 3, the preparatory steps for implementation of capital market reforms will take place, including review of laws, bylaws, and regulations on investment, governance,

[6] The interagency committee and working group for capital market reform has representatives from the Ministry of Economy and Sustainable Development, the Ministry of Finance and the National Bank of Georgia.

risk management, and fund managers, approval of account and prudential regulations for repos and securities lending, and expansion of the matching grant facility for micro, small, and medium-sized enterprises with specific gender targets.