

ARTF IP Program Adjustments 2016

The second technical review March 2016 and subsequent IP technical discussions agreed on the need to adjust the IP 2016 and 2017. Benchmark adjustments are part of the regular IP process and are an important element to ensuring the incentive compatibility of the program

This note summarizes the agreements reached with Government on the changes in the ARTF IP benchmarks following the 2nd technical review meeting. Annex I compare the changes to the original program. Annex II includes the refreshed ARTF IP matrix.

- **Electronic Payments System:** The Government's financial inclusion reform has taken an unanticipated leap towards strengthening mobile payment systems. In order to support the development of mobile payment services, the Government decided to diversify the civil service payment system to mobile operators. In the future, as the reform process moves forward, civil servants will have the choice between either receiving salary pay through the banks or through mobile operators. The Central Bank has now moved to regulate payment system operators to assure the financial soundness of the process. The new reform direction has implications for the policy framework and internal systems of the DAB, including the Automated Transfer System (ATS). We therefore adjusted the timeline of the reform process to allow Government more time to make the necessary and important changes. Moreover, high-level political constraints to progress on the issuance of biometric ID's rendered the second of the benchmarks (issuance of biometric ID's to smallholders) unviable. Since the IP is not expected to have any traction in the biometric ID reform discussion (and was not designed as such), we agreed to remove the sub-trigger from the IP. However, in order to balance ambition, we agreed to enhance results by accelerating the transition process from manual to e-payments for civil servants (from 60% to 80% coverage of the total wage bill of central Ministries)
- **Modernization and Re-organization of the Afghan Revenue Department (ARD):** ARD entered into the negotiations of the IP benchmark with great ambition and a robust reform plan. However, during the course of implementation, a number of core system vulnerabilities within ARD required urgent attention in order to ensure that tax collection proceeds without interruption in 2016. ARD subsequently adjusted the reform implementation plan to reflect these realities and manage available capacity. One part of the reform plan – the institutional restructuring of ARD's reflected in the second part of the IP trigger – had to be delayed to focus capacity building on core business processes and systems (now supported by the ARTF PFMR II project). As an alternative measure, ARD agreed to reorient the IP triggers towards streamlining tax payment and tax filing procedures which currently impose an unnecessary high burden on tax payers.
- **Baseline formula for O&M Spending:** The 2nd technical review indicated that the O&M facility may have not reflected the right level of ambition. In order to increase the level of ambition, Government agreed to raise the floor for minimum O&M spending. This will effectively increase the Government's

contributions to O&M spending. This change is now reflected in the O&M baseline formula which will move the O&M baseline proportionally to revenue growth.¹ This change will apply to the 2016 and 2017 program.

¹ Previously the baseline moved under-proportionally to revenue growth.

Annex I: Comparison of New versus Original Benchmarks

Benchmark #3: Tax Administration – Re-organization and Modernization	
Original	New
2016	
<ul style="list-style-type: none"> i. ARD fully roll-outs SIGTAS and risk-based compliance audits, to at least five additional (key) provinces; ii. The Civil Service commission approves the new Tashkeel for ARD. 	<ul style="list-style-type: none"> i. No change. ii. ARD streamlines tax payment and reporting procedures to remove obstacles to taxpayer compliance. This includes the issuance of tax clearance certificates irrespective of planned or active audits and reducing the number of administrative steps to pay taxes by cash and by wire transfer.
2017	
<ul style="list-style-type: none"> i. ARD roll-outs SIGTAS and risk-based compliance audit to the <u>remaining</u> provinces in the country; ii. ARD establishes fully functioning tax payer’s service centers according to the new organization structure and Tashkeel in five key provinces, including Kabul. 	<ul style="list-style-type: none"> i. ARD roll-outs SIGTAS and risk-based compliance audit to at <u>least five additional</u> (key) provinces ii. ARD reduces the administrative burden for tax payers through removing rigid restrictions and introduces more flexibility for tax filing.

Benchmark #8: Electronic Payment System	
Original	New
2016	
<ul style="list-style-type: none"> i. DAB rolls-out the Automated Transfer System (ATS) and begins with migration of public sector salary payments through the ATS. ii. DAB approves framework for new biometric Identity card to serve as optional registration requirement for small value accounts 	<ul style="list-style-type: none"> i. DAB finalizes the functional specifications of ATS and policy framework for operation of ATS. ii. DAB and MoF transfer 20% of central ministries public salary by existing electronic means.
2017	
<ul style="list-style-type: none"> i. DAB and MoF migrate 60% of all government salary payments by value through the ATS system 	<ul style="list-style-type: none"> i. Develop a comprehensive process and roadmap for complete migration of public sector salary payments to the new e-payment systems. ii. DAB and MoF process public sector salary payments for 80% of central ministries through ATS.

O&M Baseline Formula

Original

$$B_{t0} = B_{t-1} + \left(\frac{R_{t-1} - R_{t-2}}{2R_{t-2}} \cdot B_{t-1} \right)$$

New

$$B_{t0} = B_{t-1} + \left(\frac{R_{t-1} - R_{t-2}}{R_{t-2}} \cdot B_{t-1} \right)$$

The baseline for O&M moves **underproportionally to revenue growth** e i.e. if revenue grows by 20%, the Government's minimum contribution to O&M spending grows by 10% before the IP triggers disbursement.

The change will bring in proportionality e.g. if revenue grows by 20%, the Government's minimum contribution to O&M spending grows by 20% before the IP triggers disbursement.

ANNEX 2: ARTF INCENTIVE PROGRAM – STRUCTURAL REFORM SCHEME (refreshed May 2016)

	Area	2015		2016		2017	
		IP Trigger	Verification	IP Trigger	Verification	IP Trigger	Verification
Goal 1: increasing fiscal revenue by enhancing tax potential, improving compliance and reducing leakages							
1	Customs: HR Reforms	The Cabinet approves a comprehensive a HR reform policy for ACD. The policy will allow ACD to develop a roadmap for the establishment of a new HR platform and will provide authority to ACD to conduct an HR review, take HR actions on existing customs staff, introduce a transparent and competitive recruitment process, determine hiring and commissioning requirements as well as to deploy performance management and related remuneration packages.	Copy of cabinet approved HR policy, copy of minutes reflecting the relevant cabinet decision, and copy of the HR reform plan.	ACD begins implementing the HR reforms in line with the approved HR policy including changes to recruitment, promotion, mobility, remuneration and provisions on restrictions and exemptions to lateral entry. ACD ensures that 25% of existing grade 2,3 and 4 customs officers will have passed the Customs Academy and qualify to remain in ACD, that all new recruitments will be subjected to competitive process and that any lateral entries follow the procedures laid down in the new HR Policy.	World Bank review of ACD HR actions. Copy of approved Tashkeel, and records from HR and Academy.	(i.) ACD completes 3 rounds of customs exams for 5 and 6 customs officers and ensures that all custom officers have attended Customs Academy and cleared appropriate exams to qualify to remain in ACD. (ii.) ACD introduces a performance management system and conducts a review of HR reforms.	World Bank review of ACD HR actions, copy of records from HR and Academy and copy of performance management reports.

2	Customs: Enforcement	The Cabinet approves the establishment of a Preventive and Enforcement wing within ACD with powers of search, investigation and arrest throughout Customs territory.	Copy of minutes reflecting the relevant cabinet decision.	<p>(i.) The Cabinet approves amendments to the Customs law. The amendments will include provisions that regularize ACD's new enforcement wing, in particular regarding the power for Customs to exercise their powers on the Afghan customs territory.</p> <p>(ii.) The Civil Service Commission approves the new Tashkeel for the ACD Preventive and Enforcement Wing.</p> <p>(iii.) ACD prepares and begins implementing the Preventive and Enforcement Plan which will cover provisions on organizational structure, training and deployment of staff.</p>	Copy of cabinet approved customs law, copy of minutes reflecting the relevant cabinet decision, copy of approved Tashkeel and copy of the organizational and operational plan.	ACD ensures that the new prevention and enforcement wing is operational with appropriately competent staff recruited or transferred from other duties and deployed.	World Bank review and copy of activity report of the Preventive and Enforcement Wing
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3	Tax Administration: Re-Organization and Modernization	<p>(i.) ARD fully rolls-out SIGTAS to the five most populated province, and introduces risk-based compliance audits in all tax payer's offices in Kabul.</p> <p>(ii.) The Cabinet approves a plan for the re-organization and re-structuring of ARD, including the proposal, policy procedures and a new organization structure. The re-organization aims at providing the ARD with more autonomy in decision making, reducing the fragmentation of ARD functions across ARD HQ and provincial tax offices, and at strengthening relevant reporting lines.</p>	<p>(i.) Copies of provincial SIGTAS reports; reports of the audit committee indicating details on the selection and results of the audits.</p> <p>(ii.) Copy of the cabinet-approved restructuring plan and copy of relevant minutes recording the decision.</p>	<p>(i.) ARD fully roll-outs SIGTA and risk-based compliance audits, to at least five additional (key) provinces;</p> <p>(ii.) ARD streamlines tax payment and reporting procedures to remove obstacles to taxpayer compliance. This includes the issuance of tax clearance certificates irrespective of planned or active audits and a reduction in the number of administrative steps to pay taxes by cash and by wire transfer.</p>	<p>(i.) Copies of provincial SIGTAS reports; reports of the audit committee indicating details on the selection and results of the audits.</p> <p>(ii.) Copy of the administrative order introducing the new procedure</p>	<p>(i.) ARD roll-outs SIGTAS and risk-based compliance audit to the remaining provinces in the country;</p> <p>(ii.) ARD reduces the administrative burden for tax payers through removing rigid restrictions and introduces more flexibility for tax filing.</p>	<p>(i.) Copies of provincial SIGTAS reports; reports of the audit committee indicating details on the selection and results of the audits.</p> <p>(ii.) Administrative orders that regulate key functions and responsibilities, job descriptions, tashkeel and allocation of resources (staff and funding).</p>
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4	Tax Policy	<p>(i.) As part of the revenue measures agreed with the IMF under the SMP, MoF decrees the introduction of a mobile telecommunication top-up fee, an increase in the Business Receipt Tax and an increase in the fuel and toll fees.</p> <p>(ii.) MoF establishes and the cabinet authorizes an inter-Ministerial and inter-departmental committee for tax policy. The main function of the committee, which may have a flexible structure, should review, discuss and advise on all major tax policy proposals in a time-bound manner prior to approval by cabinet and ensure that all relevant stakeholders are consulted.</p>	<p>(i.) Copies of the gazetted decrees and satisfactory review by IMF staff,</p> <p>(ii.) copy of cabinet approved procedure and committee's ToR and minutes of cabinet decision</p>	<p>The Cabinet approves amendments to the Corporate and Personal Income Law. The amendments, based on recommendations from a detailed review, will address current weaknesses with respect to tax efficiency, equity, and incentives for compliance.</p>	<p>Copy of cabinet approved Corporate and Personal Income law and copy of minutes reflecting the relevant cabinet decision.</p>	<p>The cabinet approves all necessary legislation for an improved property taxation regime (including on rentals, sales, and property ownership). A technical and legislative review, including a tax incidence analysis, will be conducted in 2015/16 and provide recommendations to improve the regime for property taxation in Afghanistan.</p>	<p>Copy of cabinet approved Property Taxation laws and copy of minutes reflecting the relevant cabinet decision.</p>
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Goal 2: Mobilizing revenue by improving conditions for private-sector led-growth							
5	Land Administration and Management	The Cabinet approves the new land management law. The new law will include provisions that moves land titling from a court-based to an administrative system, improves security of tenure for various land users (incl. communities, women and private investors), as well as strengthens rights and mechanisms for the restitution of public and private land.	Copy of cabinet approved Land Management Law and copy of minutes reflecting the relevant cabinet decision.	(i.) The cabinet approves the new land acquisition law. The new law will include a resettlement and compensation framework in accordance with international good practice. (ii.) ARAZI establishes a fully operational complaints and grievance redress unit, including an anti-corruption and complaint hotline.	(i.) Copy of cabinet approved Land Acquisition Law and copy of minutes reflecting the relevant cabinet decision. (ii.) WB field visit report	(i.) The cabinet approves a new national land and resettlement/land allocation policy, which will reflects the governance values and principles for land management and administration; (ii.) The cabinet approves new regulations on community-based and participatory land dispute resolution.	(i.) Copy of cabinet approved national land resettlement and allocation policy and copy of minutes reflecting the relevant cabinet decision. (ii.) Copy of cabinet approved regulations
6	Doing Business reforms	The Cabinet approves a road map which includes a description of all required institutional and regulatory changes for the establishment of a unified business registration system which provides the right to invest, trade and conduct usual business activities to the license holders as well delineates the roles, ownership and management responsibilities of MOCI and AISA in relation to business	Copy of the roadmap and Minutes of the Cabinet meeting / Presidential decree for establishment of the unified business registration system.	The Government unifies and implements the business and investment licensing and registration systems under the Afghanistan Central Business Registry (ACBR) across the country	WB field visit report and registry report showing issuance of at least 250 business licenses renewed within 25 days from submission of complete applications per quarter.	MoCI/AISA, MoF/ARD, Mol and Passport Office create an electronic interface for unified business services (registration, licensing, tax clearance and business visa application) for Kabul and in at least 3 regional business hubs, in order to reducing process steps, time and costs to customers, while increasing the availability of accurate and consistent business data for government.	Registry report showing issuance of at least 300 business licenses renewed within 10 days from submission of complete applications per quarter.

		registration and licensing.					
Goal 3: Improving the efficiency, accountability and transparency of public spending							
7	Sustainability of Pension and Social Benefits	<p>i) MoF and MoLSAMD conduct a review of the pension and social benefits system which lays out the fiscal implications of the current pension schemes (Civil Servants, Security, Martyrs & Disabled) with recommendations on how to ensure that pensions and social transfers remain fiscally sustainable in the future. The findings of the review will be presented to the President, the Council of Ministers as well as the Cabinet.</p> <p>ii) MoLSAMD has introduced biometric verification / proof of life for the public pension beneficiaries registered in the PMIS.</p>	<p>(i) Minutes of meeting of the Cabinet, Council of Ministers and President.</p> <p>(ii) WB field visit report certifying the integration of the biometric verification module with the Pension MIS and banks verification systems.</p>	<p>(i) The Cabinet approves amendments to the pension related laws in line with recommendations from the pension review</p> <p>(ii) MoLSAMD has introduced biometric verification / proof of life for the M&D beneficiaries registered in the MDMIS</p>	<p>(i) Copies of the amendments and Minutes of the Cabinet meeting.</p> <p>(ii) M&D MIS reports, and Independent Audit of the M&D MIS and the bio-metric verification Module</p>	<p>(i) The Cabinet approves amendments to the pension related regulations to implement the new pension scheme.</p> <p>(ii) MoLSAMD has completed the transition from paper based to technology based administration of the Public Pension Scheme (Civil Servants and Security). All Public Pension (Civil service and security sector) beneficiaries are registered in the Pensions MIS and are paid through Bank accounts.</p> <p>(iii) MoLSAMD has completed the transition from paper based to technology based administration of the Martyrs and Disabled Benefit scheme. All Martyrs and Disabled Benefit scheme beneficiaries are registered in the M&D MIS and are paid through Bank accounts.</p>	<p>(i) Minutes of the Cabinet meeting approving amendments to relevant regulations.</p> <p>(ii & iii) Pension MIS and M&D reports, and bank payment reports</p>

8	Electronic Payment Systems	DAB issues a clear and transparent regulatory framework for payment system providers and payment system operators and issues an appropriate license to the Afghanistan Payments System (APS)	(i) Copy of the regulation issued by DAB for payment system providers and payment system operators; (ii) Copy of the license issued to Afghanistan Payments System (APS).	(i.) DAB finalizes the functional specifications of ATS and policy framework for operation of ATS. (ii.) DAB and MoF transfer 20% of central ministries public salary by existing electronic means	Copy of official communication by DAB announcing finalization of ATS functional specifications and internal policy framework. ii. Report from Treasury and DAB on details of salary payments processed through current electronic means. The evidence should show that salaries are credited to the salary disbursement account of each organization and then as per the authorization of MoF and detailed list of distribution the beneficiary bank credits the employee's individual account.	i. Develop a comprehensive process and roadmap for complete migration of public sector salary payments to the new e-payment systems. ii. DAB and MoF process public sector salary payments for 80% of central ministries through ATS.	Copy of official communication by DAB on completion of ATS implementation and field visit checks by the World Bank team. Report from MoF and DAB on details of salary payments processed through electronic means. The evidence should demonstrate that the ATS was used and that the salary was directly credited to the employees' bank account
9	Fiscal Deconcentration and Provincial Budgeting	(i.) The Cabinet approves the Provincial Budgeting Policy, allowing budget allocation of discretionary resources to provinces, based on clearly defined norms (developed by central line ministries) and in consideration of the capacity of the	(i) Minutes of the Cabinet meeting that approves the Provincial Budgeting Policy; (ii) Letter issued by MoF establishing the Fiscal Deconcentration Working Group.	MoF shifts the delegation of budget authority from central Ministries to provincial directorates for four ministries, in line with the budget policy and financial regulations.	Copy of budget circular that includes guidelines on delegation of budget authority to provincial directorates.	(i) MoF shifts the delegation of budget authority from central Ministries to provincial directorates for additional 6 Ministries, in line with the budget policy and financial regulations (ii.) Cabinet approves amendments to all relevant laws	(i) Copy of budget circular that includes guidelines on delegation of budget authority to provincial directorates; (ii) Minutes of cabinet meetings reflecting relevant decisions and

		<p>receiving Ministries as well as overall fiscal space.</p> <p>(ii.) MoF establishes a Fiscal Deconcentration Working Group that oversees the implementation of the provincial budgeting policy.</p>				governing PFM and subnational bodies to ensure that the policy can be implemented	copies of approved laws
10	External Audit	<p>(i) The Supreme Audit Office (SAO) develops and agrees on a framework and methodology for Performance Audits in line with INTOSAI Auditing Standards.</p> <p>(ii.) SAO prepares and presents a report to Parliament and President on the status of outstanding audit observations and compliance with the audit recommendations of the least three years by each line ministry and government department. With assistance of the Ministry of Finance, SAO notifies an audit follow-up mechanism requiring the line ministries to implement the agreed</p>	<p>(i.) Copy of the framework/guidelines issued for Performance Audits.</p> <p>(ii.) Copies of audit report and notification letter from SAO to Line Ministries.</p>	<p>(i.) The Supreme Audit Office (SAO) carries out Performance audits of core functions of two ministries in line with INTOSAI standards. As part of the audit process, SAO develops mechanism for citizen participation in audits and issues a policy governing citizen participation in public oversight of public funds.</p> <p>(ii.) In line with the notification letter, four key Government ministries implement at least 40% of the agreed audit recommendations in FY15 Audit reports.</p>	<p>(i) Copies of Audit reports and copy of policy for citizen participation in public oversight.</p> <p>(ii.) Copies of updated audit and/or M&E Reports on the status of outstanding audit observations and compliance with the audit recommendations.</p>	<p>(i.) The Supreme Audit Office (SAO) carries out Performance audits of core functions of five ministries in line with INTOSAI standards, including pilots instruments for citizen participation.</p> <p>(ii.) In line with the notification letter, four additional key Government ministries implement at least 60% of the agreed audit recommendations in FY16 Audit reports.</p>	<p>(i) Copies of Audit reports and progress report on integration of citizen participation criteria in audits.</p> <p>(ii.) Copies of updated audit and/or M&E Reports on the status of outstanding audit observations and compliance with the audit recommendations</p>

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