

Project No: LE-99.03.01

1. **Title: Strengthening of the tax and customs administration: Institution building/human resource development and installation of a tax audit management system (State Revenue Service Modernisation)**

2. **Location**

Ministry of Finance, Smilšu street 1, Riga LV-1919, Latvia
Mrs. Valentina Andrejeva, State Secretary

3. **Objectives**

The overall objective of the Project is to develop, support and strengthen the change process initiated in the State Revenue Service, by making a major contribution to increasing the efficiency and effectiveness in the use of human resources

Specific objectives:

1. to ensure that the tasks carried out in the State Revenue Service are in line with clearly defined strategic and operational objectives;
2. to ensure that the information is provided to managers at all levels which enable them to monitor operational performance at regional, national, and individual levels;
3. to have information available to managers to facilitate the direction of human resources to areas of highest priority;
4. to provide facilities to ensure efficient, effective and timely training in appropriate revenue collection skills.

The programs would intensify the process of integration of Latvia into the internal market. The program objectives cover the priority actions of Latvia defined both in the III National Program for Adoption of Acquis and Accession Partnership:

NPAA:

Priority theme 5.3, Sub-priority 2, Measure 2.4 – Improvement of customs performance, preparation of customs system to be integrated in the EU system.

Priority theme 5.4, Sub-priority 2, Measure 2.1 – Strengthening of Tax Administration.

Accession Partnership:

Short-term/Medium-term, Reinforcement of institutional and administrative capacity: structural reform of customs and tax administrations to ensure readiness to apply the acquis.

4. **Description**

Purpose of the Project

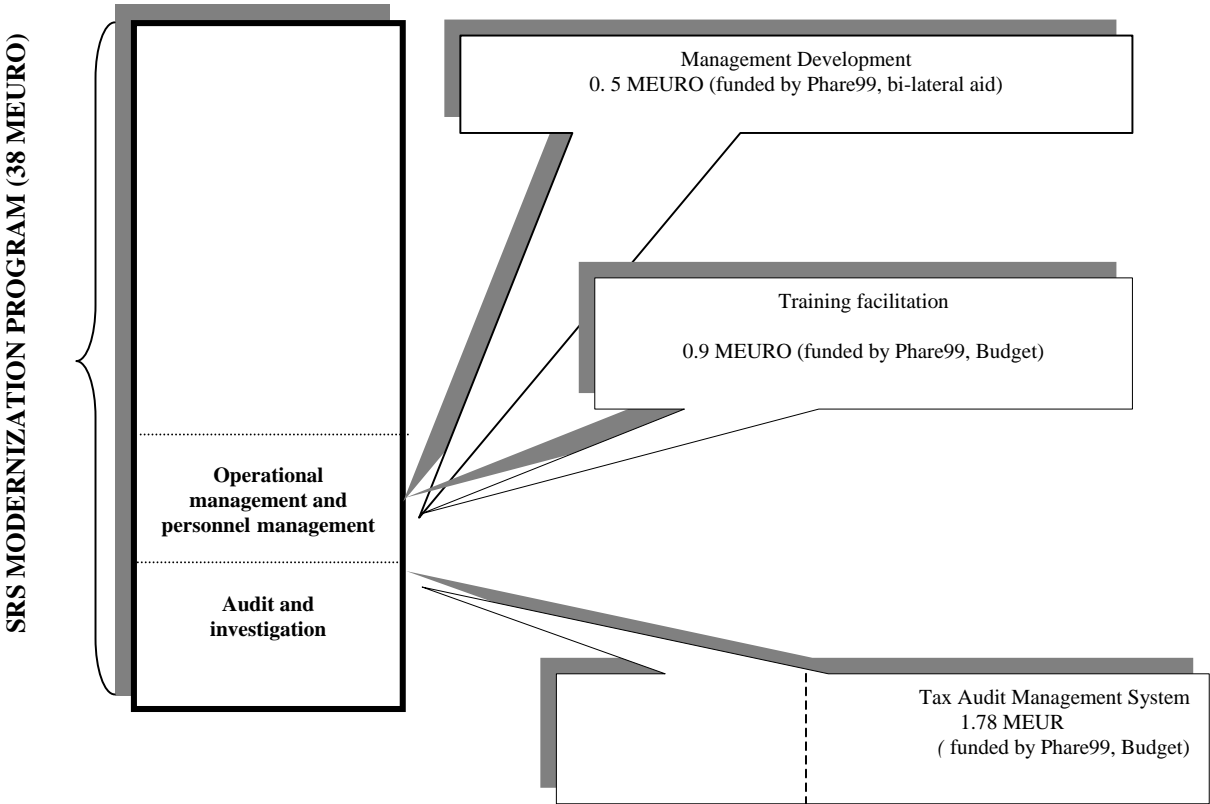
Revenue administration in Latvia needs further organisational and administrative arrangements that match Latvia's success in its transition to a market economy. The Government has taken significant initiatives to increase effectiveness of the revenue administration. To improve its systems SRS has embarked on a broad-based modernisation program known as a Four-year State Revenue Service Modernisation Project. This program entails an integrated set of investments to strengthen SRS organisational, management and operational capabilities. The program is financed by the state budget, bilateral donors and Phare. To support the investment costs associated with the project, the Government has allocated an amount of Ls 7.8 million (11.8 MEUR) in the 1999 Public Investment Program for SRS (6.8 MEUR allocated to SRS in 1998). The government has strong commitment to allocate the funds required to complete the program (total cost of the program is estimated to be approx. MEUR 38).

The high cost of financing the modernisation programme by the Latvian Government is backed by a loan from the World Bank (a total of MEUR 4.5 to be disbursed in 1998-2002). To set out the terms of the loan an assessment of priorities was carried out with recommendations as to how the money should be allocated. This is in the form of an agreed schedule of priorities.

The present Phare 99 project is a continuation of all the previously mentioned efforts. It will assist in deepening some of the recent reforms, while addressing other critical areas at SRS where institutional capacity

needs to be strengthened. The overall objective of the project is to make a major contribution to increasing the efficiency and effectiveness in the use of human resources in the State Revenue Service. The assistance will be carried out also with twinning arrangements.

It has to be stressed that this proposal does not overlap areas covered by other Phare or bi-lateral aid programmes either in progress or planned. (see Annex 5 for details).



Project component 1 – Improvement of the State Revenue Service

Sub-Component 1.1 - Implementation of systems for Strategic and Operational Planning; and performance monitoring (management development).

The objective is to implement systems, which will fulfil project objectives 1 and 2, and will contribute to the fulfilment of objective 3.

The State Revenue Service modernisation programme, in its intention to reduce the number of regions from 28 to 7, provides the opportunity to improve the strategic and management planning systems. The assessment of priorities identified this as a key area for improvement, and the need to implement a system common to all areas of the State Revenue Service. This includes changes in the management planning and information systems at central and regional level in order to create management systems able to cope with the revised structure.

Considerable training and re-training is required to implement these techniques and technical assistance for their implementation is necessary. The Customs department has benefited from Phare and bi-lateral assistance already given in these areas but the rest of the State Revenue Service has not been provided with such assistance. Therefore it is necessary to continue the development of these techniques in the customs area and extend the development to the rest of the State Revenue Service. It is now necessary to extend performance assessment to individual levels, and introduce staff reporting and recruiting systems.

INPUTS

The realisation of project covers financing for the following inputs:

Institutional building

♦ Training Assistance

12 training courses will be held in Latvia, in the following subjects: use of resources, performance monitoring, delegation of powers and project planning. Each training course will require 2 man weeks of EU expertise. These will concentrate on training Latvian trainers. 3 study visits, for 8 participants each will cover the same areas.

OUTPUTS

Expected outputs of implementation of the Project's sub-component 1.1 are:

- Operational SRS strategic and management planning system
- Reduced administrative costs
- Improved internal and external communication
- Established system for delegation and monitoring of budgets
- Introduced systems for assessing staffing requirements
- Introduced systems for staff recruiting and reporting
- Established Career management system

Sub-Component 1.2 - Training facilitation

The objective of this activity is to fulfil project objective 4.

The modernisation programme of the State Revenue Service will require extensive training and re-training of personnel. The training facilities in the SRS are limited to one well-equipped classroom in Riga. The anticipated training programme will involve very high expenses on transportation, accommodation and in the inefficient use of working time. The demand for services of the existing training centre is already at a premium and the facility is not capable of meeting the requirements of the next few years.

Many technical subjects require many hours of formal classroom training the effectiveness of which is questionable. Computer based training consists self teaching packages on CD-ROM which allow students to work in their own time and at times convenient to the work place. Such programmes are interactive in that they

allow the student to be allocated training tasks by the computer programme followed by assessment of performance. Although these programmes can be used at the office, the concentration needed requires the student to be provided with an uninterrupted environment away from their work desk. By their nature computer-based training programmes are highly complicated and sophisticated and production of them requires high degree of accuracy in the technical subject input and specialist programming skills.

INPUTS:

The realisation of project sub-component 1.2 will require Phare financing for the following inputs:

◆ Investment

Equipping of one computer training classroom in Riga. Provision and installation of 12 computers and connection to the SRS networks.

Preparation of 7 regional computer-based training rooms. Each of the 7 regional offices should have one computer-based training room, each equipped with 5 or 6 computers.

Equipping all new classrooms with general training equipment [overhead projectors, video equipment, etc].

Equipping of the training manager's office in Daugavpils with copying and fax facilities.

◆ Institutional building

1) The production of the computer-based training programmes.

The programmes can be either produced as originals, or translated from existing programmes in other countries. The former involves great deal of work in producing the technical specifications and writing the educational programmes. It is estimated that it will be necessary to produce two original programmes.

2) Translation of the material for computer-based training.

It is estimated that it would be possible to find ten foreign programmes capable of translation into Latvian. Latvia shall contribute an additional 25,000 to the costs of translations.

3) Training required to implement the computer-based training systems.

Some training will be required to ensure the effective organisation and planning of the computer based training. It is considered that this can best be met by a study visit to a country using such systems extensively. It is estimated that one study visit should be carried out for 14 participants.

➔ Twinning

Placement of a Pre-Accession Adviser in the State Revenue Service shall contribute towards the successful implementation of Component 1.

The Pre-Accession Adviser shall provide advice and assistance to the Latvian State Revenue Service on both management development within the SRS and on training management for the Daugavpils training centre.

OUTPUTS

- ◆ Two training classrooms in Riga.
- ◆ Two training classrooms and a training manager's office in Daugavpils.
- ◆ One computer training classroom in Riga.
- ◆ 7 regional computer-based training rooms.
- ◆ 12 computer-based training programmes.
- ◆ Well established computer-based training system.

Project component 2 – Tax Audit Management System

The objective of this component is to provide the systems fulfil project objective 3 and make a major contribution to the fulfilment of objective 2.

Strategic and operational planning must be supported by systems, which will provide information to facilitate the allocation of resources to the areas of highest priority. The State Revenue Service Strategic Plan and the Customs Business Strategy state the intention to use risk assessment techniques to direct resources to the areas of highest risk. The Customs service is in the process of installing systems to facilitate the selection of customs declarations based on risk information, but no such facility exists for tax audits.

Risk assessment depends on the ability to access historic trader information; to update that information from audit results; and create a trader risk profile. The system proposed in this component will perform all these functions and may be linked to other databases at a later stage to enhance the risk information. In addition it will provide accounting and standard audit calculation facilities to assist the auditor during the audit itself. In the update facility it can be linked to the accounting systems to provide automatic debt notifications.

The existing tax accounting system does not provide sufficient support for SRS auditors and managers at all levels. Among the crucial drawbacks of the system at hand are:

- ineffective manual selection of audits;
- inadequate alleviation of the mechanical side of work;
- poor early stage taxpayer-problem allocation mechanism, which later causes further complications.

A sophisticated solution like that defined in *Annex 8* would have enormous potential for improving the compliance process. However supply of such a solution is a complex process requiring a combination of the appropriate technical skills, compliance expertise and the ability to conduct large development projects with active input from the user organisation itself. The lack of any of these elements can seriously limit the chances of a successful project. Pre-requisites of this system will be:

- preparation of a user requirement, to be provided from Phare 98 National funding.
- early education of audit staff in the culture of risk assessment, in order to prepare the ground so that the audit management system can be used to its full potential and not just as a mechanical process. Managers will also require training in how to use the system for management control purposes.

INPUTS

Technical assistance will be required at the early stages of the system's development. Phare financing (1,02 MEUR) accompanied by the budget funds (760.000EUR as envisaged in the 1999 Public Investment Program) would be directed towards four initial stages involving the following inputs:

- ◆ **Training of personnel:**
 - preparation of training manuals (responsibility of software supplier);
 - training of “trainers” (18 man/weeks of studies in the member states for local personnel organised by software supplier).
- ◆ **Procurement of audit system software** (see *Annex 8* for details).

OUTPUTS

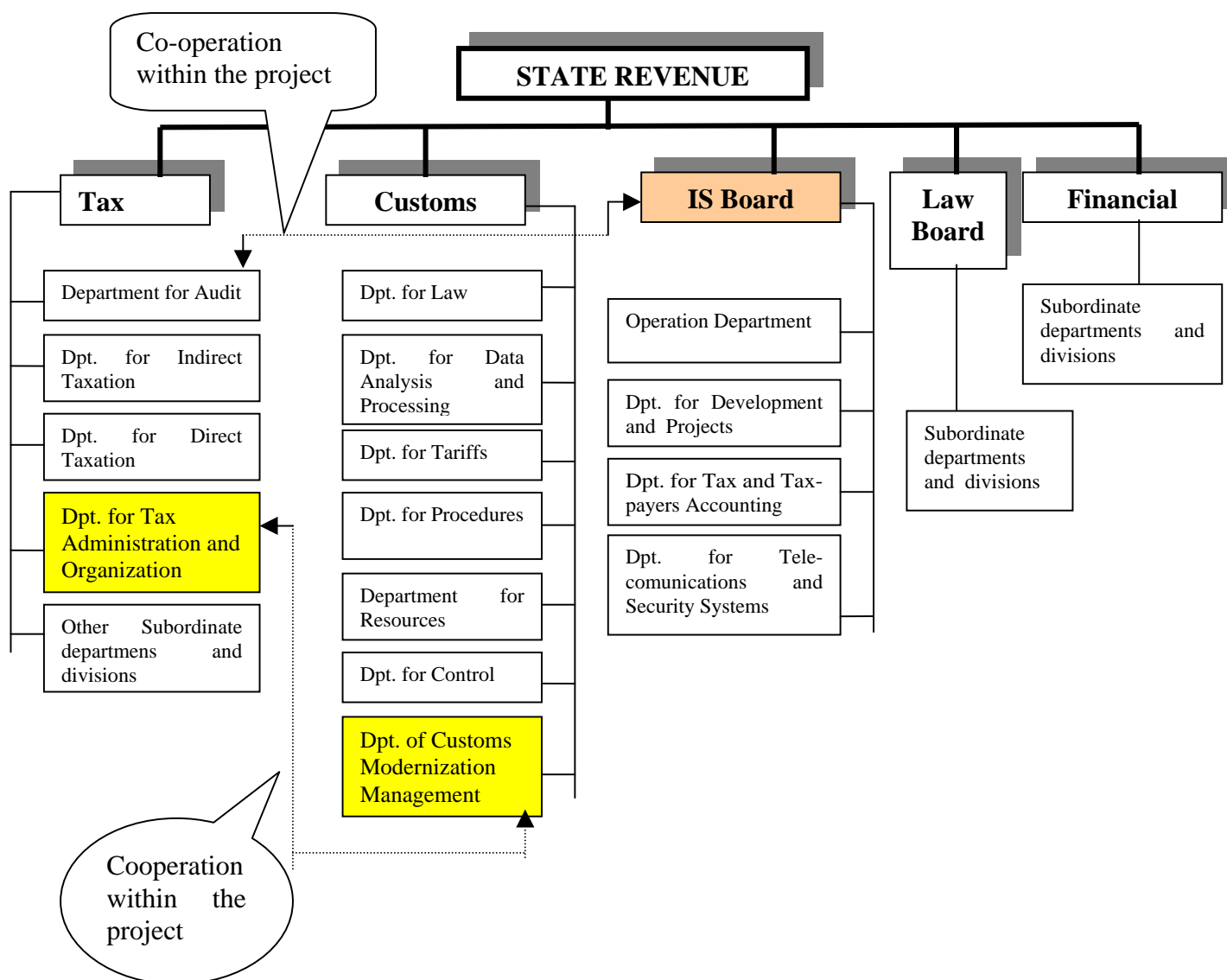
Project immediate outputs would be:

- The initial stage of introduction of new audit system completed
- Improved audit strategy
- Foundation for further upgrade and development of SRS audit system laid down
- More effective use of audit resources
- Audit IS consolidated with Tax IS and Customs IS.

5. Institutional framework

As a separate entity under the direct supervision of the Ministry of Finance (the overall framework can be found in Annex 6), the State Revenue Service is the key institution responsible for registration of taxpayers, collection of all state taxes, fees and specific obligatory duties in Latvia. The SRS plays crucial role in efficient execution of budget. Its structure is shown in the figure below: Customs and taxation services are integrated within the State Revenue Service, sharing common services, and information where appropriate. Although the majority of Customs work involves processing declarations and carrying out border control, the move over the next few years is towards post importation audit. New computer systems to develop by the Information Divisions will include the facility for exchange of information to benefit both customs and tax audit.

The State Revenue Service currently comprises Headquarters Divisions and 28 Regional offices. The SRS Modernisation Project will reduce these regions to about 7 in number, with consequential changes in the regional office and headquarters structures.



6. Budget (EUR)
1999+2000

	Investment		Institution building		Total Phare (=I+IB)	Recipient (state budget)	IFI *	TOTAL
Improvement of the SRS	200.000		530.000		730.000	145.000	275.000	1.150.000
Twinning			250.000		250.000			250.000
Audit Management System	1.020.000				1.020.000	760.000		1.780.000
TOTAL	1.220.000		780.000		2.000.000	905.000	275.000	3.180.000

* Swedish bilateral assistance

7. Implementation arrangements

Twinning

The EU Member State administrations seconding the PAAs and short-term experts will continue to pay the salaries of these civil servants. This will be arranged in a Framework Agreement between the European Commission and the Member State.

Contractual and Financial Implementation:

Central Financial and Contracting Unit, PAO Valentina Andrejeva, State Secretary of the Ministry of Finance

Technical Implementation:

This will be a full responsibility of the State Revenue Service. In order to achieve maximum effect, implementation of each part of the project will involve the structures of SRS most closely engaged in the respective field.

8. Implementation Schedule

Start of tendering: May 1999

Start of project activity: September/October 1999

Completion: February/March 2001

9. Equal opportunity

Recruiting employees the SRS takes into account the professional qualification, level of competence and correspondence to the Law on State Civil Service of the candidates not their sex, age or nationality. There will be equal opportunity for both men and women.

10. Environment

Not applicable.

11. Conditionality and Sequencing

The following activities should be completed before the project should begin:

- Adequate staffing in the recipient institutions has to be put in place for implementation and monitoring of the project components.
- The project components must be closely coordinated with other programmes and projects funded by budget, or bilateral sources.
- Project steering committee is established

The following sequence is proposed for each of sub-components of the Project component 1:

Sub-component 1.1:

- ◆ Project planning
- ◆ Alignment of management plans and operational plans
- ◆ Training in management and operational planning
- ◆ Design and implementation of performance monitoring system
- ◆ Design of staff reporting system
- ◆ Training in staff reporting procedures and implementation

Sub-component 1.2:

- Provision of equipment (computers etc)
- Provision and installation of the training equipment
- Support in introduction of computer-based training
- Technical assistance to training experts
- Technical assistance to the SRS restructuring

For Project component 2:

- Preparation of personnel
- Procurement of Audit System software
- Pilot site initiation and preparation

Annex 1				Date of drafting: <i>January 1999</i>
LOGFRAME PLANNING MATRIX FOR STATE REVENUE SERVICE MODERNISATION			Contracting period expires: 31 July 2001	Disbursement period expires: 31 July 2002
<i>Project Number LE9903.01</i>			<i>Total Budget: 3,180,000</i>	<i>Phare contribution: 2,000,000</i>
Wider Objective	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks	
<ul style="list-style-type: none"> Improvement of efficient and effective use of resources in the SRS 	<ul style="list-style-type: none"> Increase in state revenues Reduction of overall costs 	<ul style="list-style-type: none"> By use of quarterly statistics SRS Planning Unit 	<ul style="list-style-type: none"> Commitment of the government to its policy stays in place Adequate financing 	
Immediate Objectives	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks	
<ul style="list-style-type: none"> Clearly defined strategic and operational objectives Monitoring of performance Human resources directed to highest priorities Effective and timely training 	<ul style="list-style-type: none"> Production of strategic and management plans Introduction of quarterly monitoring system Increase in revenues Effective audit management system at SRS 	<ul style="list-style-type: none"> As above Monthly project reports to the Customs Modernization Division and SRS Project Implementation Unit 	<ul style="list-style-type: none"> Adequate financing Project activities are carried out according to the timetable 	
Outputs	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks	
<ul style="list-style-type: none"> Strategic and management planning system in place Increased revenue Reduced staff and administrative costs New SRS structure able to perform long term planning, effective use of resources, management of change and effective training of SRS personnel Audit management system capable of being upgraded and developed 	<ul style="list-style-type: none"> Production of SRS management and operational plans Movement in revenue receipts Noticeable reduction of costs at SRS SRS training centers ready to operate Reorganized SRS systems in place Number of non-reliable tax payers detected 	<ul style="list-style-type: none"> As above 	<ul style="list-style-type: none"> Adequate financing Project activities are carried out according to the timetable 	

Inputs	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks
<ul style="list-style-type: none"> • TA • Investments 	<ul style="list-style-type: none"> • SRS training facilities are operational • SRS staff is trained • Audit management system software is procured 	<ul style="list-style-type: none"> • As above 	<ul style="list-style-type: none"> • Project activities begin/end on time

Annex 2
Detailed Cost Breakdown (in MEUR)
State Revenue Service Modernisation – LE 9903.01

	Investment		Institution building		Total Phare (=I+IB)	Recipient (state budget)	IFI *	TOTAL
	DIS		DIS					
1.Improvement of the SRS								
Training assistance (inc. computer based training)			530 000		530 000	45 000	275 000	850 000
Twinning			250.000		250.000			250.000
Equipping of the training centres	200.000				200.000	100.000		300.000
Total	200.000		780.000		980.000	145.000	275.000	1.400.000
2.Audit Management System								
Software procurement	1.020.000				1.020.000			1.020.000
Pilot sites initiation and Implementation of IS						760.000		760.000
Total	1.020.000				1.020.000	760.000		1.780.000
TOTAL	1.220.000		780.000		2.000.000	905.000	275.000	3.180.000

Annex 3

IMPLEMENTATION SCHEDULE									Date of drafting	
									January 1999	
Title	STATE REVENUE SERVICE MODERNISATION LE 99.03.01									
	Implementation Schedule (Quarters)									Cost Estimate In MEUR
	PLANNED									
	1999				2000				2001	
	I	II	III	IV	I	II	III	IV	I	
Improvement of the SRS		D	C+I	I	I	I	I	I		730,000 EUR
Audit Management System for SRS		D	D+C	I	I	I	I			1,020,000 EUR
Twinning			D	C	I	I	I	I	I	250,000 EUR

Annex 4a

COMMITMENT (CONTRACT) SCHEDULE									Date of drafting	
									January 1999	
Title	STATE REVENUE SERVICE MODERNISATION LE 9903.01									
	Commitment Schedule (Quarters)									Cost Estimate In MEUR
	PLANNED									
	1999				2000				2001	
	I	II	III	IV	I	II	III	IV	I	
Component 1			730'000							730'000
Component 2			1'020'000							1'020'000
Twinning					250'000					250'000

Annex 4b

DISBURSEMENT (PAYMENT) SCHEDULE									Date of drafting	
									January 1999	
Title	STATE REVENUE SERVICE MODERNISATION LE 99.03.01									
	Disbursement Schedule (Quarters)									Cost Estimate In MEUR
	PLANNED									
	1999				2000				2001	
	I	II	III	IV	I	II	III	IV	I	
Component 1 (Management development and training facilitation)			95,000	210,000	380,000	505,000	670,000	730,000		730,000
Component 2 (Audit Management System for SRS)				200,000	400,000	670,000	1,020,000			1,020,000
Twinning					40,000	80,000	140,000	220,000	250,000	250,000

Annex 5.

Relation of project with Previous Phare activities and with ongoing projects financed from other sources (national, bilateral or multilateral funding).

State Revenue Service Modernisation – LE 99.03.01

Budget line	Title of project	Description	Implementation Status
EU Phare			
LE-9405	Technical Assistance to the Latvian Customs Administration	Assistance in construction of the customs Program Management Unit (PMU). Implementation of strategic and management planning systems in the customs service. Implementation of performance monitoring system in the customs service.	PMU created and working. Strategic and management planning system implemented and being further developed. Monitoring systems currently being implemented.
LE-9806.01	SRS IT Project	The project will finance preparation of specification for new audit system in SRS.	Not started yet
LE-9605.02.01	"Assistance to the Tax sector in Latvia"	The project covers projects on basic issues of legislation, administration and training in direct and indirect taxes. [No assistance has been granted in the areas of management planning and performance monitoring, computer-based training, introduction of automated audit system].	Ongoing

National (state budget, local funds etc., including loans)			
	The State Revenue Service Modernization Program.	The State Revenue Service has requested assistance from the World Bank in the form of a loan to finance the modernization program. The bulk of the loan relates to assistance with computerization, but assistance in other areas is also needed.	Contract and loan are being negotiated.
	Operational expenses for Program Management Unit for LE-9405	Provision of staff employed by the PMU from January 1997. Creation of Customs Resources Unit to maintain management planning systems and monitor performance.	Modernization division (including PMU) created in January 1997. Resources Unit created in January 1998.
Bilateral			
	Swedish bilateral contract on co-operation with the Latvian customs.	Customs senior management training which included seminars on management planning, resources planning and performance monitoring. These latter items were done in co-operation with PHARE project 96-1497.00. The Swedish aid also included study visits and seminars in Sweden for senior managers and establishment of Riga training center. The Swedish project took place over a 3 year period which ended in June 1998.	Contract finished June 1998.

