Title
Strengthening Institutional and Regulatory Capacity in the Public Finance Sector

Sub-Programme
Strengthening the Institutional and Administrative Capacity to Manage the Acquis

Geographical Location
Ministry of Finance

Objectives
The immediate objectives are:

- to implement essential legislative and administrative reforms to ensure Czech Republic compliance with EC principles and legal and reporting requirements in the area of internal financial control;
- to ensure the appropriate management of the flow of financial funds in compliance with the EU requirements, including issues of inter-relations between the State and EU budgets;
- systematically to strengthen the legal, institutional and administrative capacity of the tax administration system to implement the acquis, in particular, but not exclusively, focused on VAT and excise duties.

Institutional Framework
The Ministry of Finance, as the main body of the state administration responsible for public finance, is responsible for the revenue budget side including taxes and for the financial control of public funds. These two areas are subject of the assistance to be rendered via the respective sub-projects.

Currently, there is no fully unified Internal financial control system in the state administration. The line ministries have different organisational structure (units, departments etc.) and responsibilities for the internal control. The present system is being developed in compliance with the EU requirements and national needs. Following the practice and experience of the EU member states new approach has been adopted with respect to methodology and management from single focal national point.

The programming and use of funds falls within the responsibility of beneficiary ministries, while the financial and budgetary aspects is the responsibility of the Ministry of Finance. The financial flow of funds is managed by several Departments in charge of the income and expenditure of the State Budget and other Departments related to public finance.

With regard to future linkage to the Structural Funds the Ministry of Finance is responsible for the management of flow of financial funds, while the Ministry of Regional Development is responsible for co-ordinating regional development activities. For this purpose the Working Group for Economic and Social Cohesion, chaired by MRD, is composed of 12 Ministries involved, including MoF, with the aim to prepare the Czech Republic for using EU resources.

In compliance with the present legislation the tax administration falls within the competence of the Ministry of Finance and the statutory Deputy Minister is responsible for the overall area of tax legislation and tax administration.
In the institutional provision of the tax and custom administration performance the Czech Republic is close to the standard conditions of the performance of administration of taxes in the EU member states. Relatively large net of the territorial financial authorities (about 223 tax administrations) has been constitute under the comprehensive management of 8 regional Financial Directorates.

As of 1 January 1996, basic institutional conditions for managing tax administrations have been created from the level of the Ministry of Finance by establishing the Central Directorate for Financing and Taxation. Apart from these positive results problems persist in the tax administration, regarding the stabilisation and the professional level of officials and the performances at particular stages of the taxation procedure and the international co-operation.

Description

This **2.0 MEUR** Project consists of **2 Sub-Projects**: (1) Internal Financial Control and Management of Community Assistance (2) Tax Administration.

1. Internal Financial Control and Management of the Community Finance:

This **1.0 MEUR** sub-project will have two components, managed together as one project.

The first component will support the strengthening of the institutional and administrative capacity for implementation of the *acquis* in the area of public finance, establishing a coherent and comprehensive modernisation of the internal financial control system within the state administration system (including ex-ante, on-going and ex-post control, at different levels of state administration).

Previous Phare support in the area of public finance was provided (under the 1993 and there are running projects under 1995 and 1997 Programmes), in close co-operation with SIGMA and the EC. Support under the 1997 Programme in the area of financial control will result in preliminary findings in the course of 1999, which, combined with previous activities, will lay the basis for this Sub-Project, via its:

- assessment of the current state of the internal financial control system within the Czech state administration system,
- comparative review of the Czech system against EC requirements and against the internal financial control systems in the EU Member States,
- detailed recommendations (strategic plan) regarding the necessary legal and institutional reforms, plus human resource developments to be introduced in the area of internal financial control in order to ensure a fully comprehensive system in conformity with the EU/EC can be put in place over the medium-term.

By the end of the project financed from Phare 1997, the Ministry of Finance will have the necessary information to decide on the outline of the financial control system to be put in place.

This current Sub-Project under Phare 1999 will provide for expertise to assist the Ministry of Finance with the introduction of the necessary institutional and administrative mechanisms to ensure compliance with EU requirements.

The second component will provide for expertise to assist the Ministry of Finance with the introduction of the necessary administrative structure and mechanism to ensure the appropriate management of the flow of financial funds related to the interface between the state budget of the Czech Republic and the EU budget in compliance with EU requirements.

The project will require the inputs of one long-term twinner to be complemented by a series of short-term specialists, plus an extensive staff training programme, possibly including stages in the EU Member States.
The expert team will be responsible for:

- assisting the Ministry of Finance to implement the outcomes of the 1997 Programme regarding the necessary legal, institutional, administrative and personnel measures and their timing, to ensure implementation of the recommendations, related to the setting up of the internal financial control system,
- assisting the Ministry of Finance with the preparation and implementation of legal measures, the establishment of institutional structures, the development of administrative mechanisms and carrying out a comprehensive staff training programme required for the proper functioning of the internal financial control system.
- analysing the current legislation and practice concerning the budget inter-relations; and to suggest the concept and respective legal and institutional measures between the State Budget and the EU budget, including management of the financial flow as required;
- assisting the Ministry of Finance in the preparation of appropriate management of the financial flow of Community funds, taking into account in particular the results of the Phare project „Task Force for MRD and Working Group 10“ (CZ 9705-01-01-03) and projects under Programme 1998: Multi-Beneficiary Special Preparatory Programme for Structural Funds - Economic and Social Cohesion (CZ 9805-01);
- assisting the Ministry of Finance with the preparation of appropriate management of the own resources by the Czech Republic to EU budget;
- helping with the development of legal and institutional structure and administrative mechanism, and to carry out a comprehensive staff training programme related to the management of Community finance.

By the end of the project, the Czech Republic should have established a fully-functional system of internal financial control which meets EU requirements and an appropriate system for management of flow of financial funds, including Community assistance and own resources to EU budget, compliant with EU requirements in this area.

Given the significance for the preparation of Structural Funds, the project team will report to Working Group 10 or its successor responsible in the Czech government for Structural Funds.

2. Tax Administration

This 1.0 MEUR Sub-Project (2) will support the systematic strengthening and transformation of the legal, institutional and administrative capacity of the tax administration system (primarily, but not exclusively, VAT and excise duties and other areas of indirect taxation) to implement the acquis effectively, within the context of a single market without barriers, at the point of EU accession.

Previous Phare support in the area of tax administration was provided since the beginning of Phare programme, in close co-operation with the EC and EU Member States. Preparatory work for the sub-project to be financed from the Programme 1999 will be done during the implementation of COP 97 project. This will lay the basis for this Sub-Project, via its:

- assessment of the current state of tax legislation and administration within the Czech Republic (indirect taxation and broader issues of administration relating to direct taxation), with a comparative assessment of the level of compliance with EC requirements and broader EU Member States’ standards and practices,
- detailed recommendations regarding the necessary legal and institutional reforms, plus human resource developments to be introduced in the area of tax administration, in order to ensure that the transformation to a fully comprehensive system, in conformity with participation in the single market without barriers, can be put in place over the medium-term.
This Sub-Project, to be achieved via close co-operation with the EU Member States and the EC, will provide for expertise to assist the Ministry of Finance with the introduction of the necessary institutional and administrative mechanisms to ensure compliance with EU/EC requirements.

This will require the inputs of one long-term twinner, to be complemented by a series of short-term specialists, an extensive staff training programme, including stages to the EU Member States and the EC, plus public awareness measures and up-grade of the tax information system and services such as translation and interpreting.

The twinning experts will be responsible for:

- assisting the Ministry of Finance, based on the outcomes of the 1997 Programme, to prepare a suitable detailed strategic plan regarding the necessary legal, institutional, administrative and HRD and their timing, to ensure implementation of the recommendations,
- such assistance should reflect a comparative and analytical review of EU Member States’ practices, plus include advice to the Ministry of Finance on the issue of harmonisation of tax rates (particularly VAT and excise duties), plus on issues relating to the legislative and operational situation in such areas as: tax and fees administration, property and municipal taxes, new laws on income taxes, inheritance taxes, gift taxes, real estate transfer taxes, legislation on legal enforcement, law on territorial financial authorities, tax advisory issues, etc
- support the Ministry of Finance with the preparation and implementation of legal measures, the transformation of institutional structures and the development of administrative mechanisms,
- support the Ministry of Finance with the implementation of a comprehensive staff training programme (stages to the EU Member States’ tax authorities and the EC, plus seminars/workshops in the Czech Republic, management and language training),
- support the Ministry of Finance with the development and implementation of public awareness measures,

If recommended by the advisers, this Sub-Project may also support the up-grade of the tax information system. At present all 231 local tax offices are connected, via a data communication network, to the information system. It is planned that other state administration and self-administration bodies be gradually connected (under strict confidentiality controls). This up-grade of the information system and improved accessibility, will facilitate efforts to combat tax avoidance and tax evasion.

The first phase of the up-grade involves connecting the state administration district offices to the information system. The estimated total cost for hardware and software development is 160 MCZK (c. 4.6 MEUR). Under this Sub-Project, Phare support could provide the testing of inter-connection and SW development in 3 districts. Following the results from this testing, the decision will be on further enlargement of the information system.

If agreed, Phare support for this component will be given following open tender in accordance with Phare regulations.

**Budget**

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<th>Sub-Project</th>
<th>Inst. Build. (IB)</th>
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*IB = Institution Building, I = Investment, IFI = International Financial Institution*
Implementation Arrangements

Responsibility for the administration related to the procedural aspects of procurement, contracting and accountancy will rest upon the CFCU. Responsibility for the administration related to the preparation, technical control and implementation will rest with the PIU MoF responsible for the projects of the Ministry of Finance and the financial non-banking sector.

Implementation Schedule

Start of tendering: 3Q/99  
Start of project activity: 4Q/99  
Completion: 2Q/01

Equal Opportunity

Equal opportunity principles and practices in ensuring equitable gender participation in the Project will be guaranteed.

Conditionality and Sequencing

Annexes to Project Fiche

1. Logframe Matrix
2. Detailed Cost Breakdown for Sub-Projects
3. Detailed Implementation Chart
4. Contracting and Disbursement Schedule for the Project
5. Relation of Project with Previous Phare Activities and On-Going Projects Financed from Other Sources
### Strengthening Institutional and Regulatory Capacity to Manage the Aquis

**Programme name and number:**

**Date of drafting:** 02/1999

**Cont. exp. date:** 31/12/2000

**Disb. exp. date:** 31/12/2001

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<td>Strengthening Institutional and Regulatory Capacity in the Financial Sector</td>
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### Immediate Objectives

A set of proposals and recommendations concerning the legal, institutional and administrative framework for:

- setting up the Internal Financial Control system within state administration, compliant with EU requirements;
- introduction of an appropriate system for management of flow of financial funds between CR a EU within state administration, compliant with EU requirements;
- further harmonisation of legislation and administrative practice with the EU in area of taxation.

**Indicators of Achievement**

- Acceptance of the proposals and recommendations; analytical and comparative studies; trained personnel.

**Sources of Information**

- Internal MoF sources (decisions).
- State Gazette, Government and / or Ministry of Finance regulations and announcements.
- Independent sources (studies of the relevant non-profit organisations, institutes, press).

**Assumptions and Risks**

Implementation of recommendations will depend on political decisions within the Government and in some cases will be subject to the approval by the Parliament.

### Results of Projects

- **Sub-Project 1**: concrete proposals / amendments under component 1a/ (internal financial control system) and component 1b/ (management of flow of EU-related financial funds) regarding the structure, possible legislative amendments and methodology; monitoring, supervisory and regulatory functions of state administration bodies or appropriate institutions entrusted with these tasks.

- **Sub-Project 2**: concrete proposals / amendments regarding the concepts, legislative and other aspects of the tax administration.

- Possible recommendations for other actions within the state administration outside the Ministry of Finance or in other parts of public sector and / or in private sector.

**Indicators of Achievement**

- Ibid.

**Sources of Information**

- PIU, CFA and EC / DEC files.

**Assumptions and Risks**

It is assumed that the appropriate (EU) consultants and local staff will be involved in the project implementation and that sufficient provision will be made for services, such as translation and interpreting. No major risk is foreseen.
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### Cumulative Quarterly Disbursement Schedule (MEUR)

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Relation of Project with previous Phare activities and on-going projects

Sub-Project 1

Activity 1a) Internal Financial Control
This activity is closely related to the on-going project on Financial Control under COP 1997 (code no. CZ 9703-01-02-05-03). In a broader context the activity is linked to projects dealing with the public finance issues (under programmes 1993 and 1995). The results of COP 97 project can be conceived in general as the input to sub-project 1.

Activity 1b) Management of the Flow of Financial Funds
This activity will be dealt from its very initial stage to assist the Ministry of Finance in the preparation of appropriate management of the flow of financial funds from both the EU and own resources. In view of the preparation for the management of Structural Funds, it will be related particularly to the results of the Phare project „Task Force for MRD and Working Group 10“ (CZ 9705-01-01-03) and projects under Programme 1998: Multi-Beneficiary Special Preparatory Programme for Structural Funds - Economic and Social Cohesion (CZ 9805-01).

Sub-Project 2

Tax Administration
This sub-project is in a broader sense related to all previous Phare assistance throughout year from the initial stage of Phare programme, in particular sectoral Programme 1993 especially designed for the Ministry of Finance in area of taxation, accountancy and audit (CZ 9302-06). The assistance is being complemented by a number of horizontal projects at the national level, such as legal advise for harmonisation of legislation, seminars and study tours, and by the multi-country facilities such as TAIEX.