EFFECTIVENESS AND CHALLENGES OF FISCAL DECENTRALIZATION IN KYRGYZSTAN FOR THE EFFICIENT ECONOMIC GROWTH

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Executive Summary

This research examined how transition to decentralization in Kyrgyzstan fosters economic growth. The study was set out to answer the following research questions:

(1) *Determine what is the most efficient incentive mechanism that could be applied for sound system of relations between central and local government in Kyrgyzstan?*,
(2) *Identify areas of fiscal decentralization principles that hinder efficient service delivery and economic performance within the country.*

The dimensions being reviewed in this paper were tax assignation to various level of government, sources of revenue, mainly local tax and non-tax revenues, transfers and grants and their relationship to decentralization degree.

This paper focused mainly on two assumption that (1) *Broadening the scope of local tax and increasing the degree of self-finance, with reduction of transfers and grants could lead to sound system of relations between central and local government in Kyrgyzstan, providing incentive mechanism to reach maximal level of the efficiency, (2) For a small developing country like Kyrgyzstan, with less diversified economy, centralized form of governance is more desirable.*

The study used qualitative analysis based on secondary data, mainly from ADB, World Bank, and National Portal on Open Budget, and re-confirmed for Kyrgyzstan that current system of governance remains centralized due to lack of authority delegated to local government and inability to sustain economic growth without significant amount of transfers. The research findings from the current study supported the two assumptions.

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Throughout two years I was blessed to attend the seminar class with outstanding people, who not only showed their willingness to explain main theories discussed in the class and share their experiences, but also were a great example to me.

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List of Abbreviations

ADB: Asian Development Bank

EBRD: European Bank for Reconstruction and Development

GDP: Gross Domestic Product

IMF: International Monetary Fund

SME: Small and Medium Enterprises

UNDP: United National Development Program

VAT: Value Added Tax

WTO: World Trade Organization

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Chapter One

Introduction

1.1 Background

Based on the experience of the developed countries, transition to decentralized form of governance for the developing countries can be seen as right instrument to overcome daily problems of the regions, since decentralized state is more aware of local needs, economic activities of its citizens on local levels as well as it gives good incentives for rent-seeking . Coase Theorem supports the idea of decentralization to foster economic efficiency stating that delegation of services to the lower levels of government will lead to more efficient resource allocation, reduce transaction costs while disseminating information and enabling market players to negotiate their way to the efficiency.

There is no clear set of rules for perfectly-defined degree of decentralization level countries in transition period like Kyrgyzstan should use to be successful. Based on available literature and case studies we can conclude that each country should select its own the most optimal degree of decentralization based on country's population, historical background, political issues, geographical location, economic development, etc. Based on understanding country's specific characteristics the most appropriate degree of decentralization should be introduced to enhance economic efficiency, introduce and maintain incentives for governing, transparency. It took some

countries like China almost a century to decentralize, other countries, like Central Asian

Countries, reformed their system of governance within extremely short period of time, thus

keeping a lot of features of a previous regime in a new, so-called "decentralized" government.

1.2 History of Decentralization in Kyrgyzstan

Kyrgyzstan, a landlocked mountainous country with limited natural resources, frequent natural

disasters, was one of the poorest states in Soviet Union. For Kyrgyz Republic, after

dissemination of the Soviet Union, the decentralization was one of the key elements in transition

to democracy, since it is according to democratic principles to transfer the authority for decision-

making to local levels. Relatively rapid transition to decentralization was also caused by the

weakness of newly formed central government.

Country's GDP growth from 1990 to 2009 shows the weakness and lack of sustainability of

Kyrgyz economy at given period of time.

Sudden and severe drop of country's GDP in early 1990's is the result of Soviet Union collapse,

and as a result crisis in all industries. In conditions of "shock therapy" (fast liberalization,

abandon of central planning principles, no control on pricing issues and competition as the main

market tool) hundreds of factories and plants stopped their operations and the process of

deindustrialization took place. People learned to rely on themselves, and many males of

productive age left the country to work in Russia and Kazakhstan in order to send remittance to their families.

Kyrgyz GDP growth rate (from 1990 to 2009)
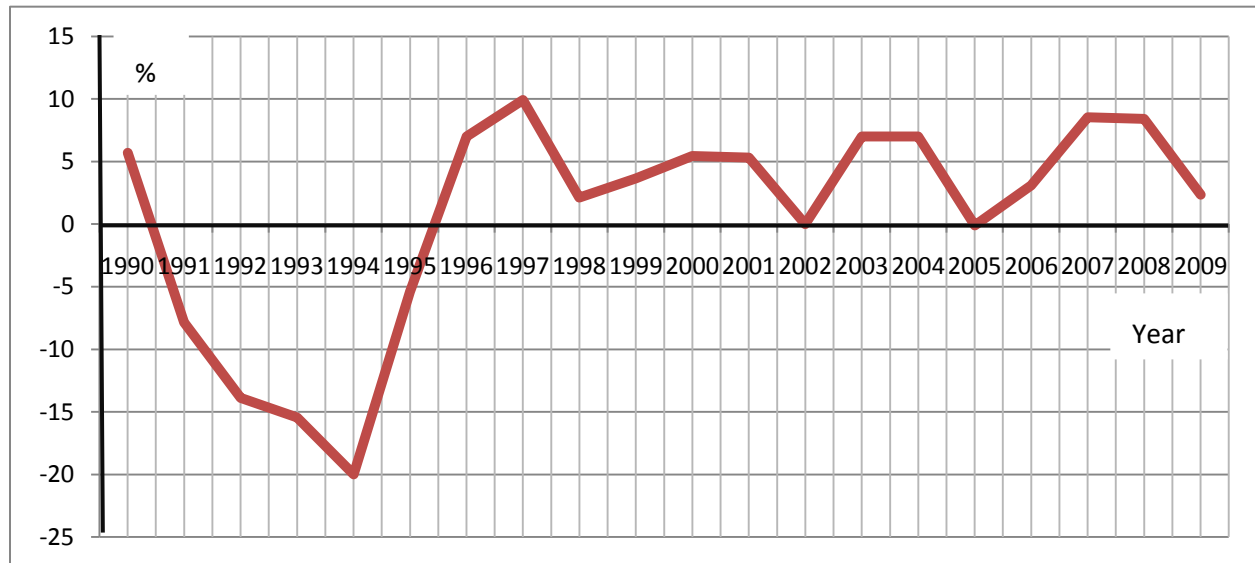
Source: World Bank countries GDP database

In 1994 GDP reached its critical point (-20%) due to currency crisis when new currency (som) had been introduced in 1993. All personal savings were devaluated due to inflation. There was no production as well as no profit from trade (due to closed external boarders).

This year is also remarkable for established relations with western countries, who through their organizations (IMF, UNDP) provided assistance and technical support to reform legislation, governance, etc. Given assistance did not lead to sudden increase of GDP growth in 1995 due to beginning of privatization, when a number of people were involved in speculation activities: buying out low-priced state's assets and reselling them overpriced. Shadow economy was widely

spread, thus data on GDP growth in 1995 might be slightly different from actual growth rate.

In 1996 people became involved in trade not only with Russia, but also with China, India.

Sudden increase of country's GDP in 1996-1997 was influenced with introduction of following industries: gold mining, revival of cement production plant, production of tobacco alcohol beverages. Nevertheless, electricity, machinery, textiles, sugar and meat industries are in critical condition of recession.

In 1998 Kyrgyzstan became a member of WTO, commerce and service sectors are developing. Products made in Kyrgyzstan are not competitive in international market, thus buying products from China, Turkey "*chelnochestvo*" and selling in Kyrgyzstan became the main source of income for many people.

In 2003-2004 world economy had been relatively stable, purchasing power of neighboring countries increased, Kyrgyz GDP increased because of trade and gold mining industry. Period of 2003-2004 was an era of increase of total foreign trade turnover, Kyrgyz economy, like economy of developing countries economy has gradually improved, since the country was actively engaged in re-exports.

In 2004, the law on Cooperatives had been introduced to develop agriculture sector, unite farmers and assign role to local government to provide incentives for local growth, but it did not influence GDP growth significantly. The reason might be hidden in tax distribution between

local and central levels. VIT, income tax and custom duties are the main sources of country's

income. Their collection is centralized and local government remains dependent on central

budget.

Political instability in the country resulted decline of GDP in 2005, 2008 and following years.

From 2000-2003 a number of laws on decentralization has been adopted covering the issues of

self-governance and local state administration, property rights, finance. National strategy

"Decentralization of public administration and local government development in Kyrgyz

Republic before 2010" has been approved by Presidential Decree. However, the actual attempt to

reform local governance showed the formality of given legislation, as the structure of governance

and the balance of power remained unchanged (Asanakunov, 2003)

1.3 State Administration in Kyrgyzstan

Kyrgyzstan practices multilevel system of governance: central (national), regional, rayon,

municipal (ayil okmotu, village self-governing units). In 2007 two-tier fiscal structure between

central government and village self-governing units had been established by the government,

formally involving regional government into budgetary matters. One year later, in 2008, the

three-tier system had been introduced, where importance of the local government was

maintained. Division into too many tiers of government can cause the problem of coordination of

service provision in all levels, as well as it can bring additional cost for taxpayers.

Local government taxes are regulated by the tax code, which, according to Taranchieva (2007),

undergone through "forty two amendments" and yet keeps a lot of controversial arguments.

There is no coherent connection between tax code and accepted laws on tax policy. Tax code

assigns tax inspectors from central government to collect local taxes, while the law on "Financial

and Economic Basics" delegates the authority to collect local tax and non-tax payments to

subnational tax officers (Taranchieva, 2007).

Fiscal structure of Governance in Kyrgyzstan (2007)

Levels of government	Number of jurisdictions
Central (National) government	
Regional Level (7 Oblasts, Bishkek and Osh cities)	9
Raion Level (raion in Oblasts)	40
Municipal Level	
• Ayil okmotu	494
• Villages	1,847
Total	2,390

Source: Taranchieva (2007)

There is a big inconsistency in *Budget* principles, when in theory the entire system is built based

on principles of cooperation between local and central government, presenting one shared budget

system with condition of availability of own sources of income at all levels of government.

Authority for decision making is important. When it comes to practice, subnational governments

are highly dependent on central government and, according to Taranchieva (2007), fiscal system of Kyrgyzstan is "built on the principle of centralism".

The weakness of given system and difference between tax code and laws raise the issue of Moral Hazard among some local authorities, who "overstep legal limits in budget design and approval, while others do not even submit their budgets to central bodies"(Taranchieva, 2007) due to not clearly defined responsibilities and authority on various levels of budgetary system.

Bertelsmann Stiftung (2010) questions the effectiveness of administrative offices, especially in regional levels due to lack of funds, hidden channels of state's influence, incompetence of local managers (so-called local authorities) and high level of corruption.

1.4 Hindering Factors

The main argument in favor of fiscal decentralization talks about efficient resource allocation and increased local influence. Several factors hinder given positive outcomes of fiscal decentralization in Kyrgyzstan: unclear budgetary policy and income distribution, hidden channels of state influence and increased probability of corruption.

Due to unclear budgetary support of the local government by the central government, central government has a privilege to transfer "unfunded" spending mandates from central to local budgets without increasing revenue responsibilities, thus increasing local budget's deficit. Moreover, central government still continues to manage local government through their local

offices. According to Taranchieva (2007), significant numbers of central state administrators work in field, regulating and monitoring local government activities. Administrators adjust central and local budgets relationships as well.

Tanzi (2000) finds <u>subnational government less transparent</u> who, comparing with central government, in most cases doesn't publish annual reports open for public use, and there is almost no fiscal data available on the lower levels. In addition, local mass media is highly dependent on subnational government.

For the recent years debates and arguments were taking place on the issue of nominating local authorities (regional chiefs). According to previous constitution (prior to 2010) regional chiefs are appointed by regional deputies, new constitution keeps it unclear whether they will be nominated by direct voting or nominated by regional deputies. Constitution states that "regional chiefs of executing bodies are nominated in accordance with Kyrgyz Republic legislation", bringing confusion and further debates on the selection process.

Given conditions make local authorities highly influenced by central government, who, in their turn, act as central government agents, rather than representing interests and needs of the local communities. Hidden channels of state influence are more likely to take place, when nominated by regional deputies local authorities promote states interests. Junosov (2011), claims that there might be a case when people with no prior experience in government service and with little

knowledge of self-governance can be elected due to corruption and support of the clans.

Moreover, there is a higher probability that local elites are better at "taking over the power" on

local level (Tanzi, 2000).

Ideal relationship between central and local governments and their role distribution can be seen

in developed economies with successful decentralization model like Central and Eastern Europe,

when there is a clear separation of powers and increasing decentralizing expenditures.

Budget constrains allocated for decentralization processes are causing the problems of incentives.

According to Libman (2008), decentralization in existing institutional environment is unable to

generate good incentives for proper governance due to deficit of resources. Asanakunov (2003)

states that the delegation of power to the local level was not supported with financial resources,

or the delegation of power was a formal procedure, keeping previous local authorities on the

local level.

1.5 Research Objectives

Thus, taking into consideration the factors hindering decentralization in Kyrgyzstan like inability

of the current system to generate good incentives for proper governance, deficit of resources,

unclear budgetary support for local government, and hidden channels of state influence this

research aims to:

1. Analyze process of fiscal decentralization in Kyrgyz Republic, look at budget allocation policies, taxation and transfers schemes to mark the most problematic areas, which do not represent decentralization principles or being misused by certain officials, thus hindering efficient service delivery and overall economic performance;

2. Evaluate efficiency of income distribution between central and regional/local government, level of regional financial independence and compare economic growth between regions and cities (who share budget with central government) to estimate country's sustainable development

1.6 Research Questions

Throughout the research two main questions will be addressed:

1. What is the most efficient incentive mechanism that could be applied for sound system of relations between central and local government in Kyrgyzstan?

2. Which areas of fiscal decentralization principles hinder efficient service delivery and economic performance within the country?

1.7 Structure of the Report

The paper is divided into two main parts. The first section contains theoretical framework describing key decentralization theories on intergovernmental relations, the relationship between

decentralization and economic performance, lack of efficiency as a result of inappropriate

transition to decentralization as well as it provides brief outline of decentralization processes in

Russia, Kazakhstan in comparison with Kyrgyzstan and successful case studies on transition in

Poland (Chapter Two and part of Chapter Three).

The second part of the research (from Chapter Three to Chapter Four) focuses on Kyrgyzstan.

Based on statistical sources of data and country reports, Chapter Three and Chapter Four analyze

macro-economic efficiency of fiscal decentralization, budget allocation among oblasts and city

of Bishkek and Osh, estimate capability of subnational government to rely on own sources of

finance (mainly from local tax gathering), look at factors which do not represent decentralization

principles or being misused, thus hindering efficient service delivery and overall economic

performance. Research findings will be further discussed and analyzed in Chapter Four. Chapter

Five is the final chapter of the report and presents conclusions and recommendations.

Chapter Two

Conceptual Framework

2.1 Introduction

Section begins with providing definition and main features of decentralization and followed by focus on fiscal decentralization in comparison with centralization. Theories on intergovernmental relations, incentive mechanisms are discussed, giving special attention to reasons causing these processes and to risks as well as benefits, associated with the process of decentralization. To understand the process of decentralization, factors that influence implementation of efficient decentralization are considered with provision of examples when transition to decentralization was successful in Poland and less successful in Russia and Kazakhstan. An attempt is made to examine the relationship between decentralization and sustainable growth of the country. The main question is whether or not decentralization had a positive impact on economic growth in selected countries with particular reference to Kyrgyzstan and to what level the country should decentralized.

2.2 Key Concepts of Decentralization

World Bank (2000) defines decentralization as "the transfer of political, administrative and fiscal responsibilities to locally elected bodies in urban and rural areas, and the empowerment of communities to exert control over these bodies".

Fiscal decentralization is defined as "decentralization of governance, expenditure delivery and revenue mobilization" (Bahl: Linn, 1994). It is important to keep in mind that fiscal autonomy is an important element of decentralization to improve both central and local governments.

Centralized form of governance can be more efficient for the developing countries. Bahl: Linn (1994) state that countries with less diversified economy are more vulnerable to international change of commodity prices, financial crisis, natural disasters, wars. Therefore the role of the central government to control main tax and borrowing is necessary.

Central government plays important role in intergovernmental income distribution that leads to economic development through subsidies and adjusted tax policies. As the last argument supporting centralization, Bahl: Linn (1994) conclude that national government has more competences and expertise in taxation and public service delivery, while local government has "very weak administrative practices" in almost every country.

Nevertheless, majority of developing countries with transition economies see fiscal decentralization as the main element for economic development.

2.2.1 Arguments supporting Decentralization

"The existence and pervasiveness of externalities would –in the presence of unlimited ability of a centralized authority to gather, process, and disseminate information-provide a strong argument

for centralization. But the ability to gather, process, and disseminate information is limited.

These limitations form the basis of the argument for decentralization" Stiglitz (1994)

Thus, among a number of arguments supporting decentralization, main statement deals with

efficient allocation of resources.

2.2.2 Efficient allocation of the resources

According to ADB (2000), strong local self-government is more efficient, compared to central

government, in the management or implementation of small to medium projects due to closer

supervision and greater accountability of local officials to local communities.

The economic efficiency increases by moving government closer to people, since local

government is more aware of people's needs and in ideal situation delivers special services for

different regions based on religion, ethnical background and other individual features of

population (Oates, 1972). Thus, taxpayers get incentives to contribute to regional development

and get necessary services provided by the government.

Main question here is how motivated are taxpayers to receive improved level of services by

paying higher rate of tax? Maybe in case of developed countries local population has higher

incomes to be willing to pay more tax for good service delivery, but in developing countries, like

Kyrgyzstan, when 65% of population lives in rural areas, with 35% out of 65 % living below

poverty line (portal of rural poverty), people prefer to cut down expenditures to cover local

budget deficit. High level of corruption among governmental authorities (both on central and

local levels) can be seen as another obstacle to earn trust of local tax payers.

2.2.3 Increased accountability

Bahl (2008) sees increased accountability of local governance in decentralized form of

governance because local officials become directly responsible for provision of good-quality

services delivered to local community who elected them. In case of centralized system, there is a

greater chance for local government to escape from taking responsibility, thus they have less

incentives to provide good level of services.

Nevertheless, if we look at Kyrgyzstan, as previously discussed in Chapter One, regional leaders

are nominated by regional government and not through the direct voting. Therefore, they would

rather act as central government agents rather than meeting local needs.

Unclear delegation of power and fiscal authority from central to local levels makes it difficult to

achieve transparency of current system. Absence of transparent formula to estimate the amount

of upcoming equalization grants and transfers for each region is known as another hindering

factor.

2.2.4 Local revenue increase

One more point in favor of decentralization is also described by Bahl (2008) stating that fiscal decentralization has potential to increase local revenue by broadening overall tax base: "Small firms, most individuals and owners of immovable property are "under-represented" in the tax base. Local government can broaden the overall tax base with a variety of tax instruments and administrative measures. These instruments include payroll taxes, levies on sales of assets of rims, licenses to operate, betterment charges and various forms of property taxation"

Tax base in Kyrgyzstan

Currently, state budget of Kyrgyzstan includes republican, oblast, Bishkek, rayon and ayil okmotu budgets. There are three types of taxes specially assigned to each level of government: local taxes (consisting of 18 types), shared taxes and regulated taxes. Local government keeps revenues generated through local taxes collection. "The two most important local taxes are land tax in all oblasts other than Bishkek, and the tax on retain sales, in Bishkek" (ADB, 2000). With present tax base revenue share for local government is lower compared with expenditure share, therefore subnational budget highly relies on intergovernmental transfers and equalization grants.

2.3 Conditions for efficient transition to decentralized form of governance

Decentralization has positive impact on overall macroeconomic stability only in condition that both central and local governments are committed to fiscal discipline in revenues and expenditure management.

Accountability of local government depends on its elections and transparency of information to enable voters to evaluate expenditures decisions of local government. In many developing countries, one or more of these conditions are not met (Bahl, 2008).

Institutions are the main stakeholders of decentralization, as they are defined as "the rules of the game". They are resistant to change even when reforms has long-term perspectives (EBRD, 2009). Unwillingness to lose privileged positions makes current institutions impose short-term costs to hinder efficient implementation.

Institutional structure can change over time when the opponents, supporting reforms get stronger and increase in size to promote their interests. Institutions can change due to a large shock, like collapse of the Soviet Union, economic crisis, national emergency when the process of change gets accelerated.

Large shock makes previous policy failures visible, encourage learning from experience and show the need to introduce changes in regulatory framework or institutional structure (EBRD, 2009).

Kyrgyzstan went on transition from previously strongly centralized form of governance to decentralized form due to weakness of central government after the collapse of the Soviet Union. Nevertheless, central government wanted to maintain its power on local level. According to ADB country evaluation report (2000), actual form of governance in Kyrgyzstan remained strongly centralized.

Among risk factors emerging as a result of transition to decentralization several factors are described in this paper.

2.4 Probability of corruption level increase

As previously discussed, decentralization leads to the efficient resource allocation thus promoting efficiency and sustainability in the economy with the hypothesis that local influence over public sector is increased. According to Bardhan and Mookherjee (2000), with transition to fiscal decentralization there is further risk that power will simply shift from central to subnational authorities, giving greater chance for increased level of corruption.

Era Dabla-Norris (2006) emphasizes the importance of institutional framework and the degree of accountability to minimize the impact of financial decentralization on corruption.

2.5 Measuring Decentralization

All developing countries with decentralized form of governance used to be centralized in the past,
with similar political structures, when local authorities were acting more as central government
agents, with limited fiscal responsibility. Based on different approaches towards decentralization,
some of the countries became more decentralized.

It is important to notice, that it is very difficult to measure the level of decentralization, since
they are several factors contributing to it. Decentralization involves not only the expenditure
assignment and revenue responsibilities, but also the extent of subnational policymaking
autonomy (Era Dabla-Norris, 2006). Thus, regular approach to measurement of decentralization,
when the share of subnational spending is viewed against total governmental spending in some
cases can give wrong results, as increased subnational spending does not reflect decision-making
authority on the local level.

Table 1 indicates expenditure assignment for each level of government in Kyrgyzstan,
Kazakhstan, Russia and successfully decentralized Poland.

Kyrgyzstan, compared to Russia and Kazakhstan, excluding Poland, has the highest subnational
spending on social insurance and health services and the highest subnational spending on
education (45% in comparison with 27.5% in Poland). Nevertheless, that factor does not
influence emergence of high decentralization degree in the country, as, according to ADB

country evaluation report (2000), conclusion has been made that Kyrgyzstan had centralized system of governance estimating the same year the statistics on subnational expenditure is presented. Instead, given conditions of high expenditure assignment delegated to subnational government and deficit in local budget result in reduced quality of services delivered or limited number of services delivered as local budget needs to cut down their expenses to meet budget constraints. Moreover, to secure funds for high share of spending covered by subnational government, transfers and grants are the main source of finance. In many developing countries, including Kyrgyzstan, the annual flow of grants and transfers from central to local budgets is not fixed or clearly defined by transparent formula, causing the weakness of, in given example, education and health sectors in conditions of under financing.

2.6 Sources of Finance for Subnational Governments

From the supply side, several sources of finance for subnational governments are considered: own revenues (obtained mainly from local taxes gathering), intergovernmental transfers (or equalization grants), tax sharing, subnational borrowing, etc.

Table 1 Expenditure structure for each level of government (% of total)

Country	Level	General public services	Defense and public order	Social insurance and health services	Education	Culture and recreation	Other	Total
Kazakhstan (2000)	Central	6.6	14.2	42.6	3.6	1.2	31.7	100
	Regional & Local	3.5	5.1	22.2	23.6	4.3	41.3	100
Kyrgyz Republic (2000)	Central	14.9	16	20.5	19.5	2.9	26.2	100
	Regional & Local	9.4	1.5	28.40	45	3.4	12.3	100
Russia (2000)	Central	7.6	17.8	32.5	2.3	0.7	39.1	100
	Regional & Local	25.6	2.8	19.20	17.8	3.5	31.1	100
Poland (2000)	Central	4	7.5	51.9	4.7	0.5	31.2	100
	Regional & Local	7.2	4.1	32	27.5	3.7	25.5	100

Source: Era Dabla-Norris, 2006

Sub-national borrowing might be quite influential for country's macroeconomic conditions.

Excessive borrowing might be dangerous for country's economy: sub-national deficits can lead

to bailout by national government. On the other hand, subnational governments should have

certain degree of access to borrowing to cover short-term fiscal deficit. World Bank talks about

number of approaches in allowing sub-national borrowing:

Reliance on market discipline (open capital markets, adequate information, responsiveness of

borrowers to market signals, and no-bail out policy of central government) is used by federal

countries like the United States.

Majority of developing countries directly control subnational borrowing by setting limits,

individual approval of loans and borrowing through Central Bank. Subnational governments

have certain ways to broaden the limits for borrowing, therefore both sides should have

incentives to properly manage and control subnational borrowing.

Own revenues include local taxes available for economic development of subnational

government. In Kyrgyzstan, for instance, two main sources of local tax include property tax and

land tax. In order to broaden local tax base, Bahl (2008) suggests to introduce "variety of tax

instruments and administrative measures. These instruments include payroll taxes, levies on sales

of assets of rims, licenses to operate, betterment charges and various forms of property taxation".

Proposed mechanism will be more efficient in case of transparency and system of checks and

balances not only between central and regional/local governments, but between subnational

government and local taxpayers to avoid corruption level increase and strengthen incentive of

taxpayers to contribute to regional development.

Bahl: Linn (1994) see grants as a consensus between the power to increase revenues and

expenditure responsibilities, with central government retaining its authority to "tax productive

resource bases" while local governance has a guarantee of revenue flow. In accordance with the

structure of grant system, local government can plan their budget, thus local government can

finance provision of local services, while central government can control the degree of autonomy.

This can be an important step in transition to decentralization. Needless to say, that there should

be one common methodology to regulate fiscal policies regarding transfer allocation and its

amount. In most of selected in this research countries but Poland delegation of transfer amount

depends on negotiation with Ministry of Finance, and has "gap-filling" character. Transfer in

Kazakhstan is realized by withdrawing money from the richest regions and reallocating to the

poorest. Poland implements transfer in accordance with transparent formula (Dabla-Norris,

2006).

The first argument in favor of decentralization described in given research states that taxpayers

have incentives to contribute to the increased level of services provided by local government by

paying more taxes.

Figure 1 Grants from Central to Local governments, % of GDP
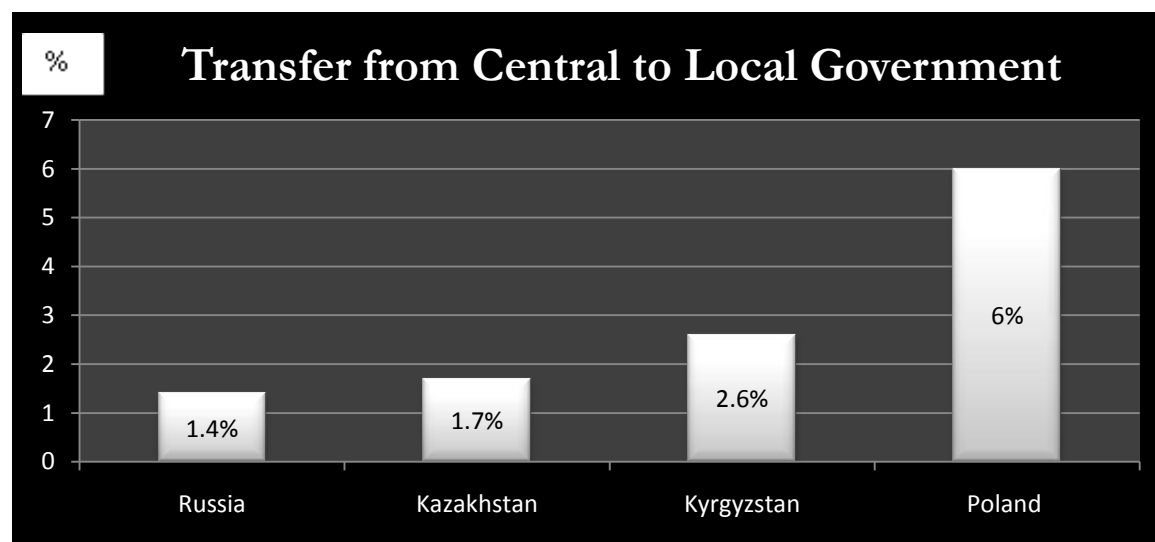
Source: Government Finance Statistics (IMF), 2001

Transfer system in Kazakhstan increases the risk that in given conditions Moral Hazard can take place when poorest states will have no incentives to contribute to economic efficiency of the region, fully relying on intergovernmental transfers. Consequently, there is a probability for the richest region to lose incentives to broaden its tax base, thus maximal efficiency will not be achieved.

The last indicator to measure decentralization level used in this chapter will focus on the relationship between own revenues of subnational government and tax sharing, using IMF approach and data. (Ela Dabra-Norris, 2006) defines the case of tax sharing when "revenues from taxes shared on a derivation basis, whose structures can only be changed at the central level, accounting for the largest share of regional revenue receipts."

Table 2 Sources of finance for subnational government

Country	Tax sharing	Own-financing
Kazakhstan	100	0
Kyrgyzstan	64.6	35.4
Russia	60	40
Poland	57.7	42.3

Source: Era Dabla-Norris, 2006

It is interesting to notice, that all of presented countries highly rely on intergovernmental tax-sharing and have limited opportunities to rely on own revenues. Poland, as a country who was a front-runner in transition to decentralization, has the lowest tax sharing degree among Kazakhstan, Kyrgyzstan and Russia, still prevailing over own-financing.

Ela Dobra-Norris (2006) analyzes impact of present structure of financial sources of subnational government on formation of potential risk of informal revenue generating as a result of limited abilities for self finance by subnational government stating that "in many countries, limited formal revenue autonomy has encouraged the widespread use of informal revenue generating mechanisms, such as tax offsets and extra budgetary funds".

Intergovernmental transfers in many countries, especially Central Asian Countries, depend on country's GDP growth and budget. In case of budget deficit number of grants can decline, thus causing deficit in subnational budgets or reduction of services provided by local government. Inconsistency of allowances flow to subnational government can result in reduced economic efficiency and growth of the region.

2.6 Conclusion

Industrialized countries are more successful in transition to decentralization, while developing countries with budget deficit and small population can consider to keep centralized form of governance to respond on external shock like financial crisis, inflation and natural disasters. Besides, central government has more competencies to mobilize revenues.

Decentralized form of governance results in better allocation of resources, transparency and provides system of checks and balances.

Proper management of taxes distribution plays important role in transition to decentralization.

Local governments doesn't have variety of formal tax revenues, central government provides intergovernmental transfers and grants for equalization. In many countries the amount of grants and transfers depends on certain factors with no transparent formula to estimate the amount for next year. Given situation leads to Moral Hazard and questions decentralization efficiency for developing countries.

Following Chapter Three will start with assumption that broadening the scope of the local tax and increasing the degree of self-finance, with reduction of transfers and grants could lead to sound system of relations between central and local government in Kyrgyzstan, providing incentive mechanism to reach maximal level of the efficiency.

Chapter Three

Data and Methods

The study area consists of urban and regional areas in Kyrgyzstan. Areas were selected as a unit

of analysis as this scope is the most reasonable to evaluate income distribution and the

performance of regions with support of grants and local finance. In addition, actual secondary

data, gathered by ADB group in 2000 is available for further comparison and evaluation. This

study will focus on major revenue sources of local government, its sustainability without

transfers and equalization grants, expenditure assignment by oblasts.

Supplementary country-level data was obtained through internet investigation. Official website

of Kyrgyz Republic Ministry of Finance discloses open budget

(http://portal.infosystema.kg/openbudget/income/main.action) provides data (as of 2011) on

income classification by central and local budgets and less transparent division of country's

expenses by territory. Portal (http://budget.kg) describes state budget's revenues and

expenditures (years 2000-2008) and more importantly, inter budgetary relations between oblasts

(Chui, Talas, Osh, Naryn, Issyk-Kul, Jalal-Abad, Batken), Osh and Bishkek cities as of 2008.

Portal on Kyrgyz budget gives some clarity on total revenues and official transfers by regions,

income generated from various taxes and several types of grants and transfers.

In general, Kyrgyzstan consists of seven oblasts and two cities: Bishkek and Osh, who have more autonomy in decision making and tax collection. Bishkek is located in Chui Oblast; Osh geographically is the part of Osh Oblast.

1- City of Bishkek; 9- City of Osh

2- Batken Oblast

3- Chui Oblast

4- Jalal-Abad Oblast

5- Naryn Oblast

6-Osh Oblast

7- Talas Region

8-Issyk-kul Region
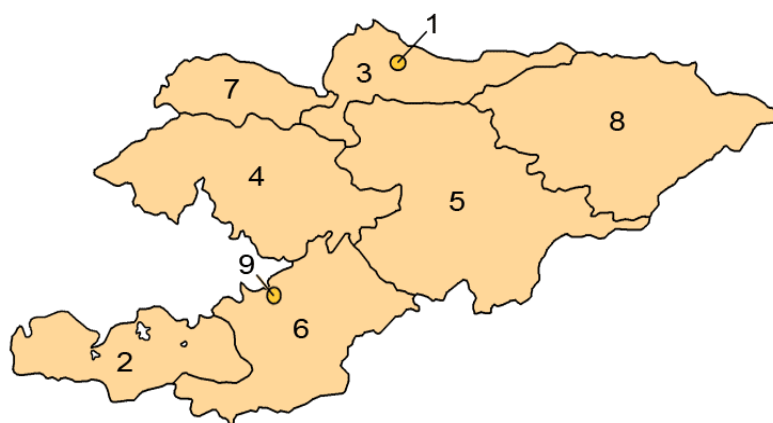
Absence of transparent formula in estimating amount of grants for next year to be received by subnational government, discussed in previous chapter hinders efficient regional development and planning by subnational authorities. ADB (2000) suggest formula for estimating the amount of grants for each region depending on its level of economic development and other factors:

$$(E^r)_{pc} = \alpha P^r$$

$(E^r)_{pc}$ - per capita annual amount of equalization grant to be received by Rayon "r"

P^r - indicator of poverty in Rayon "r"

α   -parameter to distribute equalization grants to each rayon in the country

        the amount of total equalization grants to be distributed should be clear in order to

        calculate α

Presented formula is user-friendly; moreover, it can solve problems of uncertainty, corruption.

Information, needed to make calculations according to given formula, might be limited on lowest

levels, therefore ADB (2000) assumes regional government get equalization grants and further

manages distribution to the lower levels, taking accountability for this action.

Given information assists in testing the assumption previously raised in conclusion of Chapter

Two that by reducing the amount of transfers, grants and broadening the scope of local taxes it

could lead to financial stability of the regions and provide more incentives for subnational proper

management, while increased amount of transfers leads to decline of subnational resources

generation due to lack of incentives and fear to lose high amounts of intergovernmental transfers.

Intergovernmental finance relationship matrix is used as the main analytical tool to evaluate

intergovernmental fiscal relations, when transfers are used to secure vertical and horizontal fiscal

imbalances.

Intergovernmental finance relationship matrix
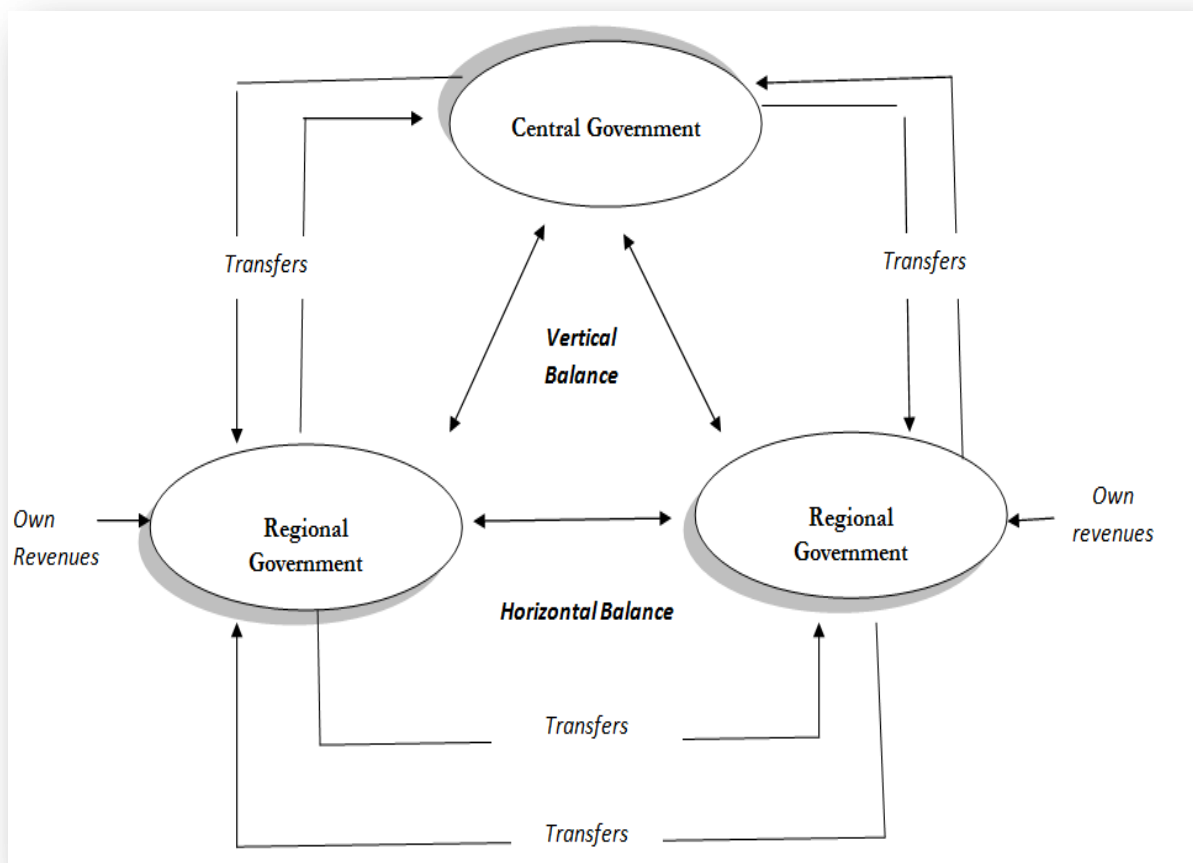
Tax administration brings revenues flow to central government and not necessarily expenditures.

Grants are filling vertical imbalances to fix the gap between subnational expenditures and

revenues. In majority of cases the revenue of subnational government, generated from the

collection of local taxes is not sufficient to meet the expenditure side. Transfers from central to

subnational government can solve the problem of vertical imbalance when subnational

government's expenses exceed actual revenue.

This research focuses on correlation between increase/decline of transfers from central to

subnational governments and financial performance of subnational government resulting in

increase/reduction of own sources of revenues over years.

Another type of intergovernmental transfers- transfers from one subnational government to

another, can solve the problem of horizontal imbalances so that all subnational governments

could provide "similar levels of local service" (ADB, 2000).

Given paper elaborates further discussions on long-term efficiency and feasibility of this

particular approach in Kyrgyz conditions in Chapter Four.

In order to approach second Research Question aiming to identify the areas related to fiscal

decentralization principles that hinder efficient service delivery and economic performance

within the country information, previously gathered in Chapter Two (limited scope of

subnational government's formal tax revenues, dependency of the amount of grants and transfers

on certain factors with no transparent formula to estimate the amount for next year and thus

failure to effectively plan activities on local level, little authority in fiscal decision making

delegated to subnational government) are going to be analyzed and tested against the main

assumption that Kyrgyzstan, as a small country in transition stage, with unstable economy is

more efficient in centralized form of governance at given period of time.

Flowchart of analytical framework provided in Chapter Four, shows the logic in answering

second research question and defines key issues that need to be analyzed in following chapter.

Chapter Four

Analysis and Discussions

Analysis and discussion presented in this chapter are derived from the secondary data analysis, mainly from Kyrgyz Republic Ministry of Finance portal on open budget (data available for the year 2008) and ADB country report on fiscal decentralization from 2001, focusing on revenue distribution by oblasts and cities of Bishkek and Osh, spending by function, major sources of revenue for local governments, and sustainability of local revenues.

The purpose of analysis of given data is to point out the importance of own revenues and reduced amount of transfers for incentives to achieve increased efficiency of local governance.

4.1 Analysis for the first research question

Figure 2 shows major revenue sources for local government in Kyrgyzstan compared by regions, including revenues from equalization grants, categorical grants, taxes and non-tax revenues.

It can be clearly seen from Figure 2 that major sources of finance for subnational government are transfers from national government. Next important source of finance for subnational government is derived from taxes (both shared and locally collected). For ayil okmotu level, land tax is the only type of tax.

Figure 2 Major Revenue Sources for Local Government (as of 1999)
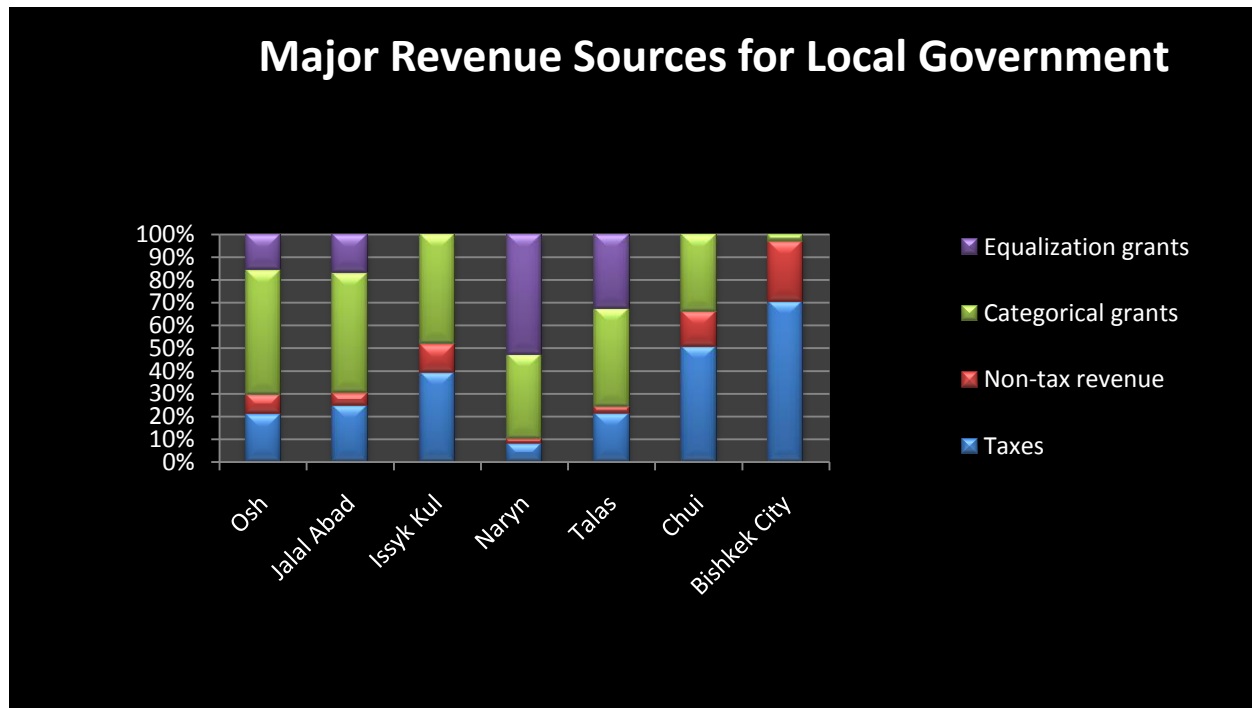
Source: ADB country report 2000

Bishkek, with special status assignation to be independent from oblast and rayon as a city, has

the highest revenue share from taxes and non-tax revenues, with non-existing or negative

equalization grants, is awarded small share of categorical grants (less than 5%). Fiscal

sustainability of Naryn Oblast, with lowest own revenues among other regions and highest share

of equalization and categorical grants, is highly dependent on equalization grants and categorical

grants, having small capacity to generate profit from collection of local taxes and non-tax

revenues. It mainly happens to the relatively small and poor population of Naryn.

Despite of its relatively small population, Issyk Kul region revenue is comprised of more than

50% of local taxes collection and non-tax revenue due to operation in this Oblast of Gold mining company Kumtor, which raises average wage for the region.

Following *Table 3* shows total revenues and grants (in percentage), received by subnational governments as categorical and equalization grants compared with local revenues without the support of grants. It also gives comparison in share of subnational government revenues compared to national revenues and grants.

Table 3 Relative Importance of Local Revenues

	1997	1998	1999
	In percentage terms, compared to republican budget		
Local Revenues and Grants compared to Republican Revenues and Grants	53.4%	47.2%	41.7%
Local Revenues without Grants	**27.7%**	**26.2%**	**21.8%**
Local Taxes Compared to Republican Taxes	23.4%	25.3%	21.5%
Local Non-tax revenue compared to Republican Non-tax revenue	**56.9%**	**33.0%**	**25.1%**
Other	Local revenues as % of total local revenues		
Grants	46.2%	47.4%	50.1%
Categorical grants	41.1%	35.9%	35.7%
Equalization grants	**5.1%**	**9.6%**	**11.8%**

Table compiled from Ministry of Finance data files, published in ADP country report in 2000.

Even though the data is covers the period from 1997 to 1999 we can observe the tendency and the relationship between local government's own revenues decline and increase in equalization grants to compensate the difference. The main reason in decline of local revenues is the decline

of non-tax revenues (sudden drop from 60% in 1997 to 25% in 1999) and decline in local taxes collection.

Main **Conclusion** made from given information is that the performance of subnational government in local tax collection as well as non-tax revenues significantly declined over the years, while the amount of grants (categorical and equalization) increased.

Non-tax revenues include foreign and intergovernmental aid, revenues from state-owned enterprises, rents from goods and services given to private corporations, etc. Severe drop in non-tax revenues of subnational government gives a certain signal of warning that subnational government loses its incentives for the efficiency or the level of corruption of local authorities increased. Decline of non-tax revenues down to 50% from 1997 to 1999 caused the increase of equalization grants from 5% in 1997 up to 12% in 1999 (more than 50%). Thus, the subnational government, being aware of given pattern, has no incentives to increase their local profits and fully rely on grants transferred from national government.

Figure 3 demonstrates expenditure assignments by region and function. Regional data is compared with Bishkek data.

Previous Figure 2 showed that Bishkek, with the special status and higher authority delegated in the use of its budget resources, has nearly 70% of tax revenues and above 25% of non-tax revenues. Nevertheless, it has the lowest expenditure delegation on education, health and state

administration bodies among other regions, while these areas are central government-mandated

spending. At the same time, it has the highest "other" expenditure, which includes capital or

investment projects as well as other development projects.

Figure 3: Oblast Spending by Function
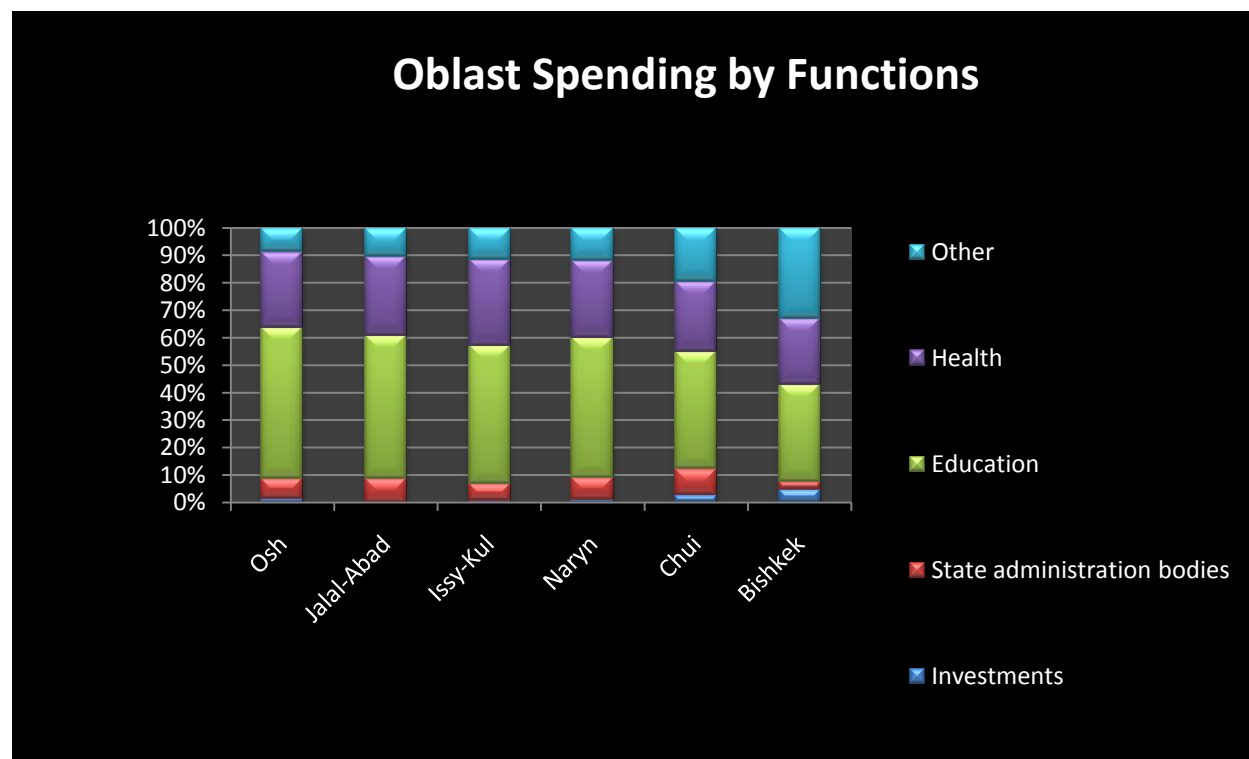
Chui region has analogical expenditure delegations and is considered to be the richest oblast

(excluding Bishkek, which is located in Chui region, as an independent city).

Proposal introduced by Bahl (1994) in Literature Review of this research, on diversification of

local tax base seems to be a good opportunity for local government to increase own finance.Thus,

delegation of grants to subnational government could be reduced, and regional spending re-

considered. *Table 4* provides us with additional more recent information on inter budgetary relations and the amount of income delegated to each region. Given information is compared with Bishkek city that has a special status of a capital. It is interesting to notice that Bishkek and in some cases Osh have more privileges due to more diverse sources of revenue, and lesser flow of transfers and grants. That means that they are more flexible in resource usage and allocation. And thus, those factors will later result in regional economic performance and improvement of public service delivery compared to other regions which have little fiscal authority and act more like central government agents or administrators. Similar to previously used data as of 2000 described in ADB country report, open budget portal as of 2008 shows that Bishkek has no revenue flow from grants to local budget, categorical or leveling grants, but received official transfers and transfers of general government. From another hand, Bishkek and Osh cities have privilege to collect income and profit taxes and have higher revenues compared with other regions, on other types of taxes.

For the poorest oblasts Naryn and Batken, transfers and grants are the main sources of finance, several times exceeding revenue collected from local tax and non-tax sources of finance. At the same time, Naryn is assigned a high level of expenditure in health and education that could probably be reduced to foster fiscal development and certain degree of autonomy in those regions.

Table 4 inter budgetary relations

| Inter budgetary relations, soms	Republic	Chui	Talas	Osh	Naryn	Issyk-Kul	Jalal-Abad	Batken	Osh city	Bishkek city
Total revenue, official transfers	10 281 234,70	1 325 047,80	243 952,60	1 235 281,10	540 951,00	561 390,10	1 091 209,30	467 165,70	552 330,40	4 263 906,60
Revenue + Assets	5 808 325,80	599 477,40	599 477,40	255 934,00	45 033,00	199 151,70	165 954,70	53 078,40	371 824,10	4 068 330,00
Revenues	5 405 093,40	575 026,90	49 483,50	245 217,00	44 998,40	195 797,50	163 839,20	51 146,00	362 114,50	3 717 470,40
Tax revenues	4 232 567,40	441 588,80	39 523,40	191 612,40	34 599,50	171 712,60	114 515,40	34 233,50	262 515,40	2 942 266,40
Tax on income paid by individuals	1 038 103,30	54 803,30	3 126,10	65 282,30	7 534,10	10 729,60	18 324,60	4 798,40	70 774,10	802 730,80
Income tax from resident individuals	858 035,00	52 977,00	3 126,10	65 282,30	7 534,10	10 729,60	18 324,60	4 798,40	70 045,40	625 217,50
Income tax from nonresident individuals	178 242,00	0	0	0	0	0	0	0	728,7	177 513,30
Tax on income and profit paid by legal entities	771 719,70	0	0	1 082,90	808,3	0	0	0	10 954,60	758 873,90
Tax on profit of domestic organizations	770 635,40	0	0	0	806,9	0	0	0	10 954,60	758 873,90
Tax on income from foreign organizations	0	0	0	0	1,4	0	0	0	0	0
Other taxes on income	138 041,00	14 031,00	287,6	2 361,60	85,7	1 086,40	211,6	325,2	6 465,70	113 186,20
Property taxes	759 297,30	201 931,30	28 331,80	71 719,70	17 800,70	107 773,20	68 771,90	21 128,40	28 675,30	213 165,00
Taxes on goods and services	1 525 406,10	170 823,20	7 777,90	51 165,90	8 370,70	52 123,40	27 207,30	7 981,50	145 645,70	1 054 310,50
Received official transfers	4 460 812,30	713 473,80	194 410,10	979 347,10	495 918,10	362 238,40	925 254,60	414 087,30	180 506,30	195 576,60
Transfers of general govnt	4 460 812,30	713 473,80	194 410,10	979 347,10	495 918,10	362 238,40	925 254,60	414 087,30	180 506,30	195 576,60
Grants to local budget	2 652 227,60	428 280,80	127 712,90	609 250,80	293 521,40	217 352,40	610 663,40	251 221,30	114 224,60	0
Categorical grants	2 482 021,80	415 774,20	123 860,20	563 006,90	261 914,30	209 709,40	560 087,00	233 445,20	114 224,60	0
Leveling Grants	170 205,80	12 506,60	3 852,70	46 243,90	31 607,10	7 643,00	50 576,40	17 776,10	0	0
Funds received by mutual settlements	1 802 707,90	279 316,20	66 697,20	370 096,30	202 396,70	144 886,00	314 591,20	162 866,00	66 281,70	195 576,60

Inter budgetary relations, 2008
Source: Open Budget portal

4.2 Analysis of second research question

To address the second research question which aims **to identify areas that hinder efficient service delivery and economic performance within the country,** Flowchart of Analytical Framework is applied and further explained.

Flowchart of Analytical Framework
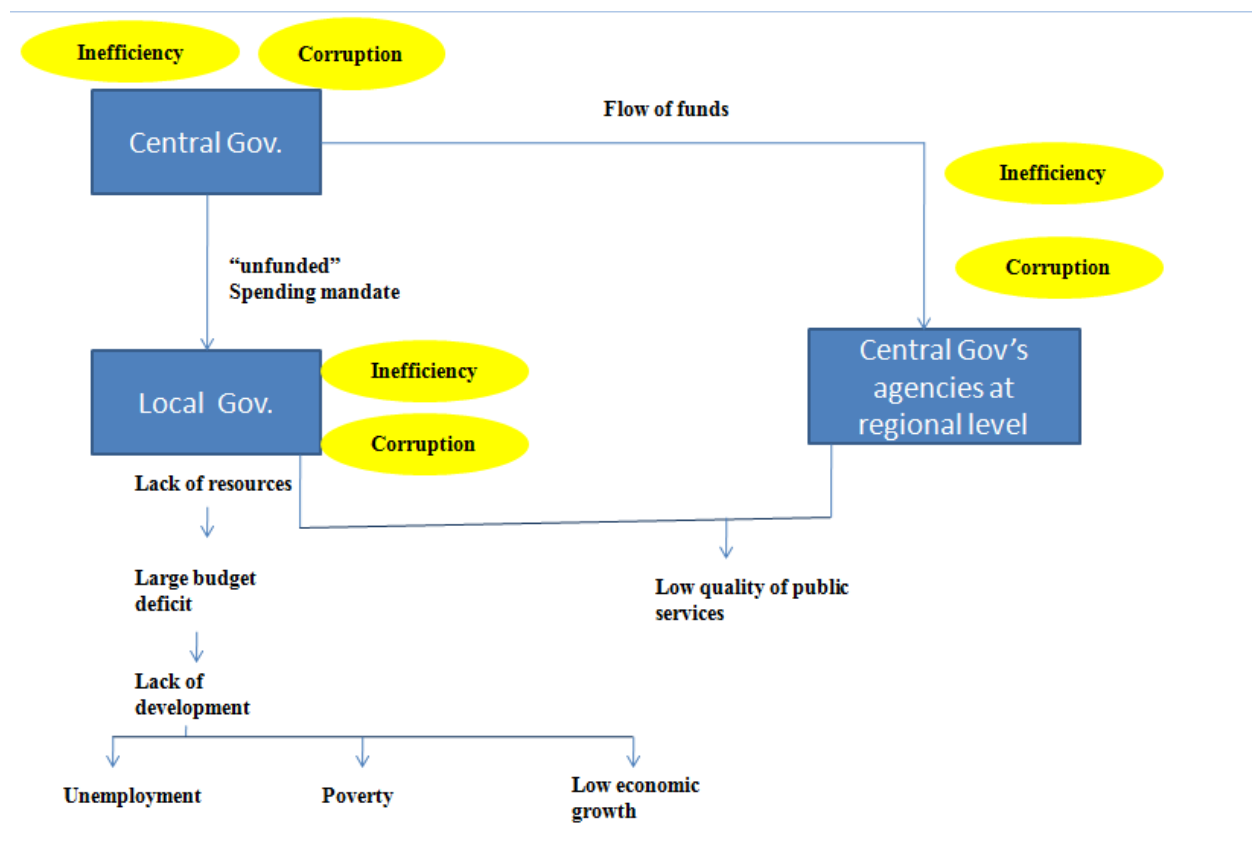
The main problem in transition of Kyrgyzstan to decentralized form of governance was caused by lack of resources and time to support fiscal decentralization. Central government informally keeps higher authority in budget distribution and expenditure planning as well as it approves local budget and decides the level of grants and transfers. Very often the budget approval is

based on negotiation bases, causing some regions to remain unfunded. Inefficiency influences

the quality of public services and willingness of tax payers to contribute to regional development.

Lack of connection between tax code and laws and their controversial positions (discussed in

first chapters) makes it easier for governmental authorities to apply either one or another

depending on each situation and own interest. Thus, if we look at the example of "unfunded"

spending mandates delegated from regional level to municipal level, etc. we can get an idea.

Chart of State Functions Distributions

Security (Civil Defense)	**Central Level** Central Government
Health (hospital, dentist, family doctors, sanatoriums, etc.)	**Regional Level** Local State Administrations (oblast) Mayors' offices
	Local representatives of central government
Secondary School **Higher Education**	**"Raion" Level** Local state administrations
	Municipal Level Ayil okmotu, town and village councils Villages

Chart of State Functions Distribution gives information on assignment of certain governmental

level to provision of certain public services. For example, hospitals (Health) are included in the

regional level budget. When regional government faces the problem of budget deficit, due to unclear legislation about transfer of spending mandates, it can transfer hospital to municipal level, thus increasing local budget deficit.

The problem is that by increasing the deficit and transferring unfunded spending mandates, not only the local budget deficit occurs, but it hinders the entire development process, lowering the level of service (healthcare, education, etc.)

Legislation mentions the importance of local government, but in practice, local government takes a role of central government's agent as well as administrative role, but their decision-making authority is limited and fiscal decisions are determined by regional administrators (who act as local representatives of central government) and the Ministry of Finance. For lowest level of government (aiyl okmotu), grants are the major source of finance, which is predetermined to be spent on funding central government programs on health and education, as we could see from Figure 3: Oblast spending by function.

Local tax is the main source of revenue for local government, with land tax taking the largest share. Local taxes are administrated by the State Tax Inspectorate (central government agency). Unclear delegation of powers between levels of government makes it less transparent, with higher probability of corruption to take place.

4.2.1 Summary of the factors, hindering efficient service delivery and receipt of benefits brought with transition to decentralization:

Transition to decentralized form of governance in Kyrgyzstan was quite rapid and not supported with financial resources. Due to mismatch in legislation, central government maintains high authority on local level, including local tax gathering and expenditure planning. Higher levels of government can transfer "unfunded" mandates to lower levels of government, thus not only increasing local budget deficit, but lowering the quality of public services delivered. Usage of grants, transferred from central to local government, is predetermined to be spent on funding central government programs on healthcare, education, etc.

Chapter Five

Conclusions and Recommendations

The last chapter aims to conclude main points raised in this research by summarizing key points, review research questions and results received. Two previously raised assumptions on impact of local revenues and amount of grants and transfers on incentive of key stakeholders as well as discussion on efficiency of current form of governance in Kyrgyzstan are further elaborated.

5.1 Incentive mechanism that could be applied for sound system of relations between central and local government in Kyrgyzstan

Conceptual framework and Analysis sections demonstrated a number of weaknesses of current, so-called "decentralized" form of governance. It is still questionable whether Kyrgyzstan has decentralized form of governance, or it is still centralized, as decentralization involves not only the expenditure assignment and revenue responsibilities, but also the extent of subnational policymaking autonomy. Even though subnational government is responsible for its own revenues and expenditure, central government maintains its authority in budget approval, controlling fiscal policies of subnational government through grants and transfers. Moreover, local authorities cannot determine tax rate for locally collected taxes, and National Tax Inspectorate administers all forms of taxes.

Data analysis included comparison of Bishkek city, which has a special status, with remaining regions, that supported first assumption raised in this research that there is a strong relationship between regional economic performance and level of own revenues in comparison with amount of grants and transfers. The lesser the opportunity for the region to increase own funds due to

limited scope of local tax, the more it depends on national grants and transfers. Chapter Four

provided good evidence when non-tax revenue declined twice, causing amount of transfers to

increase for more that 60%. That leads to the fear of local authorities to increase efficiency of the

region, as the amount of grants will be reduced. Moral Hazard includes lost of incentives of other

regions to generate good income through collection of local tax, as leveling grants will be

applied to solve horizontal imbalances. Higher degree of national spending (healthcare,

education) is also a burden on regional government, as grants are spent for national spending and

not regional development and sustainability. As a result, most oblasts and rayon face legal and

financial imbalances between expenditures and revenues.

Absence of transparent formula to estimate amount of transfers for next year is also causing

some problems with budget planning, which effects overall efficiency of the region.

Thus, steadily broadening the locally collected tax base, delegation of local authorities to

determine interest rate and collect local taxes through local tax offices, but not through National

Tax Inspectorate and slow reduction of national transfers and grants could be the first step

towards sound system of relations between central and local governments in Kyrgyzstan.

Municipal level of government should not be dependent on regional government, but receive

autonomy and freedom to budget their own resources, receiving predictable transfers and grants

based on clear formula.

Due to the large number of ayil okmotu and villages (2341, as mentioned in fiscal structure of Kyrgyzstan), there might be a coordination problem, problem to collect taxes and data from municipal level (villages, towns), therefore rayon's role could include data collection, as well as collection of local taxes through regional offices as it requires certain knowledge and skills.

Rayon should perform linking role between central and local governments, without additional financing, except administration costs.

As in practice Regional government (Oblast) are local representatives of central government (chart of state function distribution), they should officially act like central government agents and should not get transfers and be funded from central government budget. Regional government can be responsible for supervision or implementation of certain central government programs on a regional level. That would prevent a case of delegation of "unfunded" mandates to municipal level by regional level and increase of local budget deficit.

By reducing the number of tires and clarification of rayon's and regional government role, central government gets closer to local government, and overall accountability of government will increase.

5.1.1 Obstacles for given recommendations

There are some obstacles hindering implementation of proposed plan. As previously described in first part of the research, there is a *lack of qualified managers* on local levels, *budget deficit* and *ethnic tensions* between Uzbek and Kyrgyz nationalities, who usually live in communities and in case if poorest region gets grants to solve horizontal imbalances, that might cause a conflict between these two nationalities.

High level of corruption and high influence of informal institutes can be a big obstacle for proper decentralization. If the laws can be amended, reforms introduced, it is much more difficult to deal with corruption and ruling elites as well as highly influential informal institutes. It might take another generation of managers with different attitude to bring a change.

Therefore, efficient transition to decentralization requires commitment, certain time, budget allocation, well-planning and development of SME on local levels to foster sustainable growth of the region.

5.2 Identification of areas of fiscal decentralization principles that hinder efficient service delivery and economic performance within the country

Identification of areas of fiscal decentralization principles that hinder efficient service delivery and economic performance within the country puts a big question mark on feasibility of proposed reforms. And the long-term cost on inefficient transition to decentralization is too high,

causing the decline in quality of public services delivery, burden on central government to provide higher amounts of grants and transfers and loss of motivation on behalf of local government to generate good revenues.

Bahl (1994) made related comment about the preference of the country in selection its form of governance, taking into consideration its economy, population, size, historical background, etc. Kyrgyzstan is a small country with its population of 5 million, with weak economy. Centralized form of the governance might be more efficient for Kyrgyzstan, compared with current level of decentralization, to buffer external shocks, world prices increase, natural disasters, dry climate, etc. As given system makes certain individuals take their interest in their own interpretation of decentralization principles (central government continuous involvement into fiscal issues of subnational government, transfer of "unfunded" mandates to municipal level, unclear legislation that hinders transparency and clear separation of powers) going back to centralized form of governance will be more beneficial for the country's economy, until the time when system is ready to take another change, taking more steady and planned approach.

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Appendices

Total Expenses by the territory

Код	Economic Classification	Budgetary Funds (in Thousands som)	Special funds (in thousands som)
11111100	Income tax paid by a tax agent	-70,39	0,00
11123100	Tax on special funds of budgetary organizations	0,00	89,40
13321400	Funds transferred between levels of local budgets	2 113,50	0,00
14235900	The fee for the provision of other services	0,00	0,00
21111100	The basic wage	4 862 338,62	415 681,07
21111200	Surcharges	1 037 515,00	109 623,94
21111300	Additional benefits and compensation	637 410,41	171 274,00
21112100	Part-time or contract employees	5 183,46	58 873,66
21211100	Pension fund payments	929 434,07	95 016,69
21211200	health insurance payments	101 491,59	10 638,58
22111100	Transportation costs	45 060,25	21 464,84
22111200	hotel costs	16 466,56	6 100,54
22111300	per deem costs	16 425,57	6 457,79
22112100	Transportation costs	22 900,61	9 034,06
22112200	hotel costs	16 914,85	6 460,92
22112300	per deem costs	13 010,54	5 146,05
22121100	water bills	35 119,73	6 489,27
22121200	electricity bills	285 912,74	21 994,15
22121300	heating bills	252 694,32	25 060,75
22121400	gas bills	2 230,11	3 465,01

22121900	other services bills	6 547,55	724,09
22122100	landline bills	63 494,29	10 550,28
22122200	mobile bills	9 906,80	1 885,30
22122300	communication services	514,73	144,95
22122400	postal services	3 316,01	243,33
22122500	fees for TV programs broadcasting	74 091,92	19,53
22122900	Other types of services	11 697,50	6 319,48
22131100	rental of offices	77 298,92	3 177,67
22131200	equipment rental	115,35	140,79
22131300	vehicles rental	648,65	132,90
22131900	other types of rental	3 169,02	126,62
22141100	gasoline, etc	92 399,09	25 808,36
22141200	spare parts purchasing	27 052,38	9 708,91
22141300	vehicles maintenance	6 269,97	1 834,99
22141900	transportation costs (other)	34 547,64	3 662,11
22151100	services of the lawyers	290,72	197,84
22151200	consultants fees	699,48	196,80
22151300	defense fees	25 626,09	6 474,21
22151400	IT fees	1 568,92	1 245,39
22151900	other fees mentioned by contract	15 668,64	11 245,19
22152100	repairment of offices	144 900,25	22 197,39
22152200	repairment of other buildings	8 680,35	2 765,77
22152300	maintenance of equipment	2 217,19	2 673,38
22153100	sanitary services	8 108,27	5 306,63
22153200	maintenance of memorial and historical objects	15,00	0,00
22153900	other services bills	1 951,75	1 341,19

22154100	training of governmental servants	596,94	839,87
22155300	purchasing of equipment	29 727,53	10 849,97
22155400	uniform purchasing, maintainance	3 983,42	1 529,62
22155500	purchasing of coal	10 067,32	436,86
22155600	purchasing of other fuel	9,00	0,00
22155900	other purchasing	70 674,04	73 419,33
22156100	representation costs	6 168,49	2 627,44
22156200	costs for blans design	5 734,92	15 070,80
22156900	other costs	971 502,03	119 770,04
22157100	State securities costs	8,10	0,00
22157200	banking costs	42,38	0,00
22157300	banking costs	30,70	0,00
22157400	treasury banking costs	29 562,71	0,00
22161100	health care costs	1 424 456,04	54 572,23
22171100	purchasing of medical devices	117 232,84	9 416,02
22171200	purchasing of medical devices	19 307,88	0,00
22181100	purchasing of food items	583 159,45	123 452,16
22181200	subsidies for food items	73 021,39	27 614,44
24111100	banking costs	1 104 830,29	0,00
24211100	banking costs	131 690,84	0,00
24211200	banking costs	325 231,92	0,00
24221100	financial costs	60,32	0,00
25111100	subsidies	968 028,86	465,33
25121100	subsidies for financial institutions	9 273,00	12 098,21
25211100	subsidies for private entrepreneurs	66 562,42	0,00
26211100	payment for international organizations	22 656,05	1 478,10

26211200	other payments	67 524,39	0,00
26311100	**CATEGORIAL GRANTS**	2 349 339,60	0,00
26311200	**LEVELING GRANTS**	582 884,00	0,00
26312100	**Transfers to local budgets**	716 817,30	0,00
26312300	**increase of salaries**	1 500 610,50	0,00
26312400	**horizontal transfers**	27 528,46	0,00
27111100	pensions for social insurance	1 256 722,44	0,00
27111200	other pensions	349 766,51	0,00
27111300	pensions for war participants	563 150,00	0,00
27111400	social pensions	568 720,00	0,00
27112100	military pensions	12 500,00	0,00
27113100	payment assistance to eldery people	872 549,46	0,00
27113200	other compensations	25 654,89	0,00
27114100	assitance for disabled	39 778,32	0,00
27114200	other pensions	106 563,67	0,00
27115100	health insurance for kids	54 001,56	0,00
27115200	health insurance for eldery	65 646,91	0,00
27115300	other health insurance	2 906,03	sis
27211100	other social payments	423 314,95	189,52
27211200	payment after child birth	13 812,64	83,05
27211300	mother's assistance	185 257,49	0,00
27211400	unemployment benefits	3 203,17	0,00
27211500	social compensations	625 415,56	15,00
27211600	social compensations	1 319,91	0,00
27212100	unemployment benefits	268,57	0,00
27212200	maternity benefits	45 970,44	-91,16

27212300	assistance in funerals	6 116,14	139,10
27213100	other assistances	1 461 505,91	691,58
27214100	training expenses	12 188,38	0,00
27214200	other expenses	18 022,23	159,19
27214300	microcredit expenses	3 428,60	0,00
27215100	health expenses	1 056,60	0,00
27216100	**assistance for victims of earthquakes, etc**	23 494,49	0,00
28211100	scholarships	49 490,95	6 725,58
28212100	court expenses	29 542,06	617,13
28213100	other expenses	9 391,80	482,67
28215100	insurance reserves	23,00	0,00
28215200	insurance reserves	63 295,07	0,00
28216900	pension funds	5 418,20	0,00
28217100	program of state investments	114 935,43	0,00
31111210	purchasing and construction of apartments	1 380,00	14 793,68
31111290	purchasing of other construction items	141 531,98	2,00
31111390	reparment of construction items	1 022 276,32	855,00
31112110	sale of production items	0,00	697,50
31112120	sale of buildings	50,00	0,00
31112210	purchasing and repair of administrative equipments	5 500,00	0,00
31112220	purchasing and repair of administrative equipments	0,00	13 560,00
31112290	purchasing and repair of administrative equipments	30 768,46	5 140,54
31112310	repair of construction items	1 038,76	253,46
31112320	Repair of construction items	581,00	6 775,78
31112330	repair of construction items	220,40	0,00

31112390	repair of construction items	105 411,22	7 504,87
31113190	sales of other buildings	0,00	52,10
31113210	construction of production sites	2 479,00	0,00
31113220	road building	95,00	0,00
31113290	other purchasing	27 590,86	8 586,94
31113310	repair of construction items	58 511,75	0,00
31113320	road repair	387 151,30	13 183,39
31113330	bridge repair	895,85	0,00
31113390	repair of other items	112 758,10	7 270,03
31121210	purchasing of vehicles	882,00	0,00
31121230	purchasing of vehicles	771,19	0,00
31121290	purchasing of vehicles	2 447,10	20,00
31121310	repair of vehicles	92,00	50,00
31121330	repair of vehicles	4,00	0,00
31121350	Repair of boats	1 589,00	0,00
31121390	Repair of vehicles	100,00	4,00
31122210	purchasing of production equipment	611,46	4,00
31122220	purchasing of agricultural equipment	1 025,00	71,00
31122290	purchasing of other equipment	14 225,28	2 932,00
31122310	Repair of equipment	0,00	3,00
31122390	repair of equipment	633,39	93,30
31123110	sales of furniture	0,00	81,48
31123120	sales of office equipment	-10,00	57,00
31123130	sales of computer equipment	12,00	431,95
31123210	purchasing of furniture	3 060,69	5 724,81

31123220	purchasing of office equipment	1 064,22	1 057,74
31123230	purchasing of computer equipment	9 626,73	23 014,20
31123240	purchasing of tools	397,60	462,78
31123250	purchasing of books, etc	102,00	3 807,84
31123290	purchasing of other equipment	10 566,68	7 410,09
31131210	purchasing of seeds	0,00	34,20
31131220	purchasing of plants	628,66	16,20
31131230	purchasing of animals	0,00	43,30
31131290	purchasing of cultivated actives	200,00	0,00
31132110	sales of copyrights	0,00	20,00
31132290	purchasing of other actives	18,70	1,35
31412220	purchasing of land for production	0,00	0,00
31412290	purchasing of land for other purposes	35,00	0,00
32141110	repayments by subnational government	200,00	0,00
32141190	repayments by subnational government	598,80	0,00
32141290	loans for subnational government	11 772,72	0,00
32142130	other repayments	1 625,00	0,00
32142220	loans for financial institutions	630 000,00	0,00
32142230	other loans	80 932,37	0,00
33131210	repayments of mutual agreements	1 569 521,71	0,00
33131290	repayments of mutual agreements	50 000,00	0,00
33132210	repayments of mutual agreements	578 600,00	0,00
33141110	repayments of mutual agreements	-4 900,00	0,00
33141210	repayments of mutual agreements	238,12	0,00

33241210	repayments of mutual agreements	191 732,01	0,00
33242210	repayments of mutual agreements	672 377,10	0,00
	total	32 864 723,04	1 677 661,44

Classification of Revenues (1 January-26 June, 2011)

code	Economic Classification	Central Budget	Local Budget	Total
11111100	income tax paid by income agency	1 277 793 695,75	677 505 189,71	1 955 298 885,46
11111200	income tax by tax declaration	952 364,21	581 765,40	1 534 129,61
11112100	non-resident income tax	229 359 266,13	0,00	229 359 266,13
11113100	income tax	1 537 905 669,54	0,00	1 537 905 669,54
11311200	real estate tax	0,00	266 071 838,03	266 071 838,03
11312100	transportation tax	0,00	6 401 315,78	6 401 315,78
11312110	transportation tax of juridical bodies	0,00	62 204 821,16	62 204 821,16
11312120	personal transportation tax	0,00	192 256 852,74	192 256 852,74
11321100	land tax	0,00	59 755 836,77	59 755 836,77
11321200	land tax in the disposal of farmers	0,00	80 367 745,85	80 367 745,85
11321300	land tax in urban areas	0,00	217 597 413,88	217 597 413,88
11411100	VAT for products and services made in KR	2 193 496 175,66	0,00	2 193 496 175,66
11411200	VAT for imported goods	5 838 151 775,93	0,00	5 838 151 775,93
11412100	Sales tax	907 052 698,44	907 052 724,57	1 814 105 423,01
11413100	road tax	1 553 854,20	0,00	1 553 854,20
11414100	payments for social security	1 776 736,46	0,00	1 776 736,46
11421000	other tax	290 042 032,19	0,00	290 042 032,19

11422000	other tax	613 401 299,61	0,00	613 401 299,61
11441100	fuel	859 181,42	0,00	859 181,42
11441200	metal	185 953 058,80	0,00	185 953 058,80
11441300	non-metal natural resources	1 771 128,45	0,00	1 771 128,45
11441400	underground waters	1 432 095,55	0,00	1 432 095,55
11442100	fuel	16 450 294,98	0,00	16 450 294,98
11442200	metal	13 275 702,00	0,00	13 275 702,00
11442300	non-metal natural resources	17 164 362,75	0,00	17 164 362,75
11442400	underground waters	20 812 983,51	0,00	20 812 983,51
11511100	duty tax	915 103 517,77	0,00	915 103 517,77
11511200	duty tax	1 649 045 957,87	0,00	1 649 045 957,87
11512100	duty tax	-1 947 861,34	0,00	-1 947 861,34
11513100	duty tax	4 160 337,27	0,00	4 160 337,27
11514100	other duty taxes	143 360,00	0,00	143 360,00
11611000	other taxes	0,00	1 403 367,98	1 403 367,98
14111100	national bank deposit tax	25 884 256,46	0,00	25 884 256,46
14112100	interest rates	201 270 807,89	0,00	201 270 807,89
14121100	dividents	2 335 369 278,01	0,00	2 335 369 278,01
14122100	revenues of national bank	1 103 992 940,00	0,00	1 103 992 940,00
14152110	payment for rental of buildings and land	0,00	100 768 115,24	100 768 115,24
14152120	payment for rental of pastures	0,00	0,00	0,00
14152121	payment for rental of pastures	0,00	828 661,30	828 661,30
14152122	payment of rental of pastures	0,00	252 326,80	252 326,80
14152123	Плата за аренду отгонных пастбищ	0,00	816 853,00	816 853,00
14153900	payment for rent other items	0,00	17 604 912,69	17 604 912,69

14221100	licensing profit	143 295 526,28	0,00	143 295 526,28
14221200	revenue from giving certificates	54 012 282,15	0,00	54 012 282,15
14221300	lottery patent	1 175 081,56	0,00	1 175 081,56
14221400	payment for vehicles registration	149 117 136,07	0,00	149 117 136,07
14221500	other payment	1 325 154,00	0,00	1 325 154,00
14221600	payment for accounts services	120,00	0,00	120,00
14221700	collection of personal payments	0,00	27 290 524,51	27 290 524,51
14221800	parking revenue	0,00	9 326 804,00	9 326 804,00
14221900	other payments	0,00	2 814,00	2 814,00
14222100	Governmental duty for imported goods	1 997 520,86	0,00	1 997 520,86
14222200	Governmental duty for imported goods	0,00	121 833 572,31	121 833 572,31
14222300	Governmental fee for legislation	10 398 652,37	0,00	10 398 652,37
14222400	Other governmental fees	15 647,00	0,00	15 647,00
14235100	vehicle fees	2 062 657,41	0,00	2 062 657,41
14311100	administrative fines	108 218 466,11	49 959 988,94	158 178 455,05
14311200	fines for non-licenses trading	33 489 672,00	0,00	33 489 672,00
14311300	fines for non-licenses trading	1 126 852,00	0,00	1 126 852,00
14311400	fines for non-licenses trading	12 357 054,55	1 625 326,91	13 982 381,46
14311500	reimbursement for economic crime	4 044 433,32	1 335 637,50	5 380 070,82
14511100	nationalized property	53 495 957,98	2 331 015,89	55 826 973,87
14511200	other non-tax revenues	474 964,65	15 914 516,37	16 389 481,02
14511300	loss	-49 491 820,50	0,00	-49 491 820,50
31111110	apartment sales	0,00	54 566 947,03	54 566 947,03
31111120	house sales	18 000,00	0,00	18 000,00
31111190	other buildings sales	0,00	3 740 910,00	3 740 910,00

31112190	other buildings sales	0,00	1 527 065,00	1 527 065,00
31113190	other buildings sales	9 680,00	128 440,00	138 120,00
31121110	vehicles sales	156 090,00	47 593,00	203 683,00
31121130	vehicles sales	21 285,00	0,00	21 285,00
31122120	agricultural equipment sales	0,00	69 170,00	69 170,00
31122190	other equipment sales	0,00	230 000,00	230 000,00
31131120	plants sales	0,00	71 500,00	71 500,00
31211110	fuel sales	176 176 471,57	0,00	176 176 471,57
31411110	agricultural land sales	0,00	7 650 236,00	7 650 236,00
31412110	non-agricultural land sales	0,00	50 345 024,64	50 345 024,64
32141190	payment of debts by other governmental units	491 919,00	2 458 500,00	2 950 419,00
33141110	borrowing from other governmental units	0,00	6 872 715,00	6 872 715,00
	Total	24 430 742 949,58	3 699 680 406,57	28 130 423 356,15

Source: http://portal.infosystema.kg/openbudget/income/main.action

Population in Poverty Urban/RURAL (
(Poverty Portal)

population	
rural	65
urban	35

	population	poverty
total	5 321000	2015000
rural	3250000	1718000
urban	2711000	297000
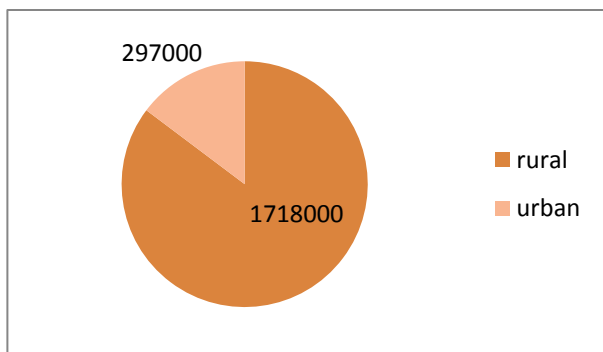
total	2015000
rural	1718000
urban	297000