Report No. 61791-LA

The Lao People's Democratic Republic
Public Expenditure and Financial Accountability (PEFA)

Public Financial Management Assessment

June 2010

Poverty Reduction and Economic Management Unit
East Asia and Pacific Region

The report was prepared by the World Bank with financing support from the MDTF contributed by AusAid, EC, SDC, and Sida

Currency Unit = Lao Kip
US$ = 8,276 (as of May 2010)

ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank
AUSAID	Australian Agency for International Development
BOL	Bank of Lao PDR
COA	Chart of Accounts
DIC	Department of International Cooperation
DMFAS	Debt Management and Financial Analysis System
DSA	Debt Sustainability Analysis
EC	European Commission
EFD	External Finance Department (of MoF)
FDI	Foreign direct investment
FMCBP	Financial Management Capacity Building Project
GDP	Gross domestic product
GFIS	Government Financial Information System
GFS	Government Financial Statistics
GOL	Government of Lao PDR
IC	PFMSP Implementation Committee
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
LDC	Least-developed country
LPRP	Lao People's Revolutionary Party
MDG	Millennium Development Goal
MDTF	Multi-Donor Trust Fund
MOF	Ministry of Finance
MOH	Ministry of Health
MPI	Ministry of Planning and Investment
MTEF	Medium-Term Expenditure Framework
MTFF	Medium-Term Fiscal Framework
MU	PFMSP Management Unit
NA	National Assembly
NPV	Net present value
NSEDP	National Social-Economic Development Plan
NT2	Nam Theun 2
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PACSA	Public Administration Civil Service Authority
PEFA	Public Expenditure and Financial Accountability
PER	Public Expenditure Review
PETS	Public Expenditure Tracking Survey
PFM	Public financial management
PFMPR	Public Finance Management Performance Report
PFMSP	Public Finance Management Strengthening Program
PI	Performance Indicator
PMU	Project Management Unit
PrMO	Procurement Monitoring Office
PRSO	Poverty Reduction Support Operation
SAO	State Audit Organization
SDC	Swiss Agency for Development and Cooperation
SC	PFMSP Steering Committee
Sida	Swedish International Development Cooperation Agency
SME	Small and medium enterprises
SOE	State-owned enterprise
TIN	Taxpayer Identification Number
TIMS	Treasury Information Management System
TMA	Treasury Main Account
TSA	Treasury Single Account
UN	United Nations
UNCTAD	United Nations Conference for Trade and Development
VAT	Value-added tax
WB	World Bank

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ACKNOWLEDGMENTS

This report was prepared in partnership with the Ministry of Finance, the Development Partners, and the World Bank.

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Background

1. The Lao PDR (current population 6 million) is on the United Nations' (UN) 2008 list of least-developed countries (LDCs), with average per-capita income of approximately US$850. The Government of Lao's (GOL) objective is that economic growth should lift the country out of this status by 2020. The economy has been growing rapidly in the most recent period: over 2000–08, GDP grew by 7 percent a year on average. Development of the economy has depended particularly on the growth of mineral and energy exports and of tourism, and on the development of light manufacturing whose products are sold primarily in South East Asian markets. The output of agriculture, which continues to account for approximately 75 percent of employment, has been growing but more slowly. The most developed parts of the country are the flatter lands of the Mekong valley, which also provide the bulk of tax revenues. The remoter hill country areas remain engaged primarily in subsistence agriculture and forestry activities.

2. While remaining a one-party state, Lao PDR has become a relatively open economy. Its recent growth has reflected foreign direct investment (FDI) in mining and manufacturing combined with investment in infrastructure financed mainly on concessionary terms by development partner institutions. Although most utility services are provided by state-owned enterprises (SOEs), most economic activity is in the private sector. Because Lao PDR has been less integrated in the economy of the Organization for Economic Cooperation and Development (OECD) countries, it has been relatively less affected by the current world recession. Nevertheless, despite the good performance of recent years, the country's economic situation remains precariously dependent on continued capital inflows from private investors and multilateral development partners.

Integrated Assessment of Public Financial Management Performance

(a) Credibility of the Budget

3. Because of the narrow tax base, in recent years, general government consumption and investment in the Lao PDR have amounted to less than 20 percent of GDP. (In 2008–09, the government consumption and investment absorbed 21 percent of GDP). Despite the persistence of a public sector deficit averaging 3 percent of GDP over the last 4 years, the government has managed to maintain sufficient cash flow. It has drawn on external finance on favorable terms and with better control over revenue collection to execute its budget broadly as planned. Thus, the budget has become more credible. At the same time, GOL has achieved a continuing reduction in the net present value (NPV) of (almost entirely external) public sector debt as a proportion of GDP. These results are a substantial improvement on the position during the years up to 2005, when cash rationing was in force and there were significant arrears in relation to salaries and utility bills.

4. However, the budget has been heavily skewed toward investment expenditure (reflecting some donors' greater willingness to finance specific projects than to provide ongoing budget support for current expenditure). Scant resources have been available to support the current consumption of goods and services associated with the provision of health, education, and other public services. Available resources will need to be allocated very carefully if the assets created in recent years are to be maintained and operated. Tax revenue has been rising but is vulnerable to falls in metal prices as well as to demand for manufactured exports. Meanwhile despite its success in reducing the burden of debt relative to GDP, Lao PDR remains at risk of "debt distress," as measured by debt stock in relation to GDP and revenue. Although some outstanding residual amounts due for electricity supplies remain, the bulk of such arrears are being paid off. There are apparently no other arrears on current expenditure at the central level—a great improvement over the situation five years ago. However, at the provincial and district levels, there also are arrears owed to utility suppliers that are being paid off, as well as amounts owed to contractors that are, in effect, expenditure arrears but are not reported as part of government debt.

(b) Comprehensiveness and Transparency

5. Presentation of the budget (the fiscal year runs from 1 October to 30 September) is in a format that reflects administrative practices rather than a clear indication of the GOL's expenditure priorities. The budget is a unitary budget, covering all of the expenditure of the provinces and districts as well as the expenditure of central government. Under the 2006 Budget Law, donor assistance is treated as part of the budget. The expenditure of most of the central ministries is separately distinguished (but military and police expenditure is aggregated with a number of other services). In contrast, the 40 percent of expenditure under the control of the 17 provinces is shown by province rather than by function. It thus is impossible to obtain a comprehensive picture of the functional allocation of general government expenditure at either budget presentation or budget execution stage. The introduction of a new Chart of Accounts (COA) combined with improvements to the operation of the GOL Financial Information System (GFIS) in FY2009–10 should make possible an approximate functional reporting of expenditure. However, the first steps toward functional planning of expenditure are only just beginning to be taken through the requirement for at least minimum allocations at the province level for education and health services.

6. Although the Lao PDR is a unitary state without representative institutions in the lower tiers of government, much authority has been delegated to the governors of the 17 provinces. Until recently, the governors were responsible to collect 60 percent of the national revenue and to allocate their expenditure to their administrative units. Central control is being established over the tax and Treasury functions in each province. Meanwhile, the central government has begun to take steps to insist that at least minimum levels of expenditure per person for education and health services are provided by each province. This step offers the prospect that the disparities in the level of public service provision among different provinces will be reduced.

Simultaneously, work has begun to devise a formula based on population, area, and relative poverty that will be used to apportion among the provinces the 50 percent of those revenues that are shared with central government. However, this new revenue-sharing arrangement has not yet been put into operation, nor has any transparent basis been devised for the allocation of whatever additional central government funding may be needed (over and above each province's own revenues and share of shared revenues) to finance at least a minimum level of public services throughout the country.

7. In addition to the budget as narrowly defined, there are eight extra-budgetary funds that are reported alongside the budget but are managed outside the Ministry of Finance (MoF) Treasury system. Two of these funds (roads and forestry) are included in the budget aggregates presented in this report, but the others are excluded. The inclusion of the roads fund is important because the expenditure is substantial, and there is also significant hypothecated revenue. The expenditures of the other funds are relatively small so it does not appear that their inclusion would significantly change the overall picture.

8. The proceeds of user charges are included as revenue in the budget only if the respective fees have been included in the budget plan and are transferred to the Treasury upon instructions from the Tax administration. An earlier Prime Ministerial decree, however, has allowed the relevant line ministers to decide not to include such amounts in the budget and to manage the proceeds outside the Treasury. Specifically, educational institutions would collect and transfer to the Treasury the revenues from the education certificate fee, which is included in the budget.

9. In contrast, the funds for improving and refurbishing school buildings are regarded as a local initiative. Communities are permitted to manage that revenue stream separately with some contribution provided from the budget funds allocated to the provincial Education department. The Ministry of Public Health manages revenue from charges and purchases items necessary for medical treatment through a Revolving Fund outside MoF control. Thus, in practice, it appears that much of these amounts remains entirely outside the budgetary system. This exclusion is contrary to the requirements of the Budget Law and to the apparent intention of a recent instruction from the Prime Minister. The total revenues not included might add 5 percent or more to aggregate recorded expenditure. Action is being taken to bring these "technical" revenues and their associated expenditures within the budget.

10. Apart from the impact of directed lending by state-owned commercial banks, there had been no indication in recent years of other "quasi-fiscal" activities. However, the wish to maintain the level of economic activity during the recession and the construction of the facilities required for the December 2009 South East Asian Games have resulted in substantial expenditure (on the order of 2.7 percent of GDP) being financed outside the budget through the issue of kip and US$ bonds by the Bank of Lao (BOL) held by the banking system.

11. The Government provides the National Assembly (NA) with forecasts of growth, inflation, and the exchange rate, together with detailed budget proposals for revenue (including grants) and expenditure, and a list of approved investment projects in the course of execution during the year ahead. Information is also provided about deficit

financing but not about the overall debt position. This information is made available to the public only after a long delay, if at all. Thus, information was published early in 2010 about the administrative allocation of expenditure in 2007–08. No information is published about the financial performance of SOEs.

(c) Policy-Based Budgeting

12. Budget planning is the joint responsibility of MoF and the Ministry of Planning and Investment (MPI). MoF is responsible for determining the overall fiscal envelope, taking into account the availability of external grants and the scope for external and domestic borrowing. MPI is responsible for setting the objectives for the development of the economy, for macroeconomic forecasts, and for the choice of investment projects to be undertaken, whether externally financed or financed from the budget's limited volume of domestic finance for investment. The overall shape of the budget should be consistent with the objectives of the current (2006–10) 5-year National Social and Economic Development Plan. However, these objectives are not expressed in a way that can be translated directly into numbers for a particular budget year. There is no explicit requirement in the Budget Circular to document any connection or to provide information on likely outputs, outcomes, or impacts. The circular contains only a general requirement to prioritize and allocate resources to various (undefined) sectors and localities.

13. The facts that the provinces have enjoyed a substantial measure of independence in the functional allocation of expenditure and that staffing allocations are determined by a process unrelated to the budget have further weakened the budget as an instrument of government policy. Nevertheless, a start has been made in reasserting central control through the insistence in 2008–09 that all provinces must allocate at least a minimum of resources to health and education services. Meanwhile, the National Assembly (NA) has been pressing for the introduction of norms for the allocation of province/district expenditure, which would ensure that overall expenditure priorities were respected.

14. Preparation of the budget by MoF and the line ministries/provinces apparently takes place against a background of sufficient political understanding across the government of the real underlying circumstances. On the other hand, the Budget Law timetable has not so far been respected. No ceilings have been given to spending agencies in budget circulars. In addition, the application of the prescribed amounts for standard costs results in unrealistic proposals that are overridden by MoF in putting its consolidated proposals to the NA. The Economic Committee of the NA has taken the initiative in seeking to ensure that the Budget Law calendar is respected, and that there is detailed consultation in the course of budget preparation with MoF on expenditure allocation and with MPI on investment priorities. Despite the requirement for this in the new (2006) Budget Law, the budget has not yet been presented in the context of a clear medium-term fiscal framework that shows the financial resources prospectively available and their broad allocation, functional and economic. This lack reflects the fact that although the Asian Development Bank (ADB) has financed some initial work on the preparation of a medium-term fiscal framework, work is only just beginning in a few line ministries on articulated planning of the development of public services. This planning should also take into account both the physical resources (human capital, materials, facilities) prospectively available and the outputs/results to be achieved over time in

improvements in, for example, health and education standards. Analyses of future debt sustainability have been made each year in the context of successive International Monetary Fund (IMF) Article IV consultations. The results are used to inform decisions about the amounts and terms of new external government borrowing to support current and capital expenditure. However, medium-term fiscal planning will be fully effective only when current and investment expenditures, which hitherto have been treated separately by MoF and MPI, are brought together within an integrated framework.

(d) Predictability and Control

15. At its current stage of development, Lao PDR lacks the banking, accounting, and IT infrastructures needed for the operation and enforcement of an advanced tax system. Total tax revenue in 2008–09 was expected to amount to some 12.5 percent of GDP divided roughly equally between income and profit taxes, domestic sales and excise taxes, and customs and other duties on imports. The first two categories are the responsibility of the Tax Department of MoF. The third is the responsibility of the Customs Department. The vast bulk of tax revenue is received from fewer than 5,000 large taxpayers, with the remaining 80,000 taxpayers contributing small amounts. Tax law is often expressed in rather general terms, and Lao PDR has no tradition of consultation with taxpayer representatives on the administrative arrangements for tax assessment and collection. Neither have the tax authorities previously devoted much effort to taxpayer education, although a campaign was conducted in the run-up to the introduction of the value-added tax (VAT) in January 2010.

16. Because of the imprecision of tax legislation, tax advisors find different interpretations of the same point being given by different tax offices as they insist on following their (different) established practices. To date, the Tax Department has done nothing to insist on consistency. Important tax exemptions of varying extent and duration may be given under the control of MPI as inducements to inward investments of different kinds in different parts of the country. These exemptions have significant revenue costs and sometimes distort competition. The circumstances of the relatively numerous small taxpayers make it difficult to avoid an element of negotiation between the tax collectors (who until recently were mostly under the authority of the provincial authorities) and taxpayers. Even substantial taxpayers find themselves in effect negotiating with tax offices about the way their accounts should be interpreted in determining their tax liability. There is no dedicated independent mechanism to resolve disputes between taxpayers and the authorities, and there have been no cases of appeals to the courts apart from one concerning customs duties.

17. As yet there is no single registry of all taxpayers. However, work as part of preparations for the introduction of VAT in January 2010 is expected to provide the basis for the general introduction of unique Taxpayer Identification Numbers once the necessary IT infrastructure is in place throughout the country. This is not expected before 2012–13. Over time, placing the provincial Tax, Customs and Treasury offices under direct central supervision, together with the developing an IT communications infrastructure, should make an important contribution to the security of revenue flows. Indirect taxes must be paid monthly, and profit tax quarterly on account (that is, in advance of the final assessment for the period in question). There are penalties for late

payment, and tax offices make particular efforts toward the end of each financial year to collect arrears of taxes due. Information provided by MoF Tax Department indicates that arrears are fairly small, amounting at the end of each of the last three years to approximately 1.25 percent of revenue collected in the year. However, in the absence of clear assessments based on good records, arrears apparently are defined in a limited way. According to the Customs Department, there are no arrears of customs duties, since duty must be paid before goods are released.

18. Once the budget for the next year has been set, the Budget Department sets quarterly ceilings on each budget line for payment authorizations by the Treasury. There is no separate control of commitments. There have been no cash shortages at the central level in recent years that have required the reduction or postponement of expenditure. Ministries can now be confident of the availability of cash within the ceilings, which are fixed six months in advance. In addition, there have there been no centrally imposed in-year reductions in budget allocations. Rather, increases have been made via mid-year budget revisions, as revenue (until 2008–09) had exceeded initial estimates.

19. Prior to the 2008 implementation of the revised Budget Law and Treasury centralization, much of the government's cash remained outside the central Treasury in the hands of the provinces or line ministries. Since then, the policy has been that all revenue should be paid directly into Treasury accounts, from which disbursements can be made only with Treasury authorization, or at least with the Treasury being fully informed. Nevertheless, the regulatory framework still has loopholes. Budget units at the central and provincial levels have been able, with little restriction, to open and operate bank accounts for collecting revenues, receiving grants, and making payments outside the budget framework and without reporting to the fiscal authorities. Line ministries' operations and centrally collected tax revenues are centralized in the Treasury Main Account (TMA) at the BOL. Provincial revenues are remitted every two weeks to the TMA from the commercial bank accounts in which they are initially deposited. Accounts designated for expenditure are replenished as required from the TMA to meet approved expenditures. However, the centralization of the Treasury function, including the banking arrangements, remains incomplete. Although all Treasury staff in the provinces were put under central control by December 2009, it appears that appreciable amounts of revenue from the provision of services are still being retained in bank accounts outside Treasury control. As noted above, work is underway to identify all government bank accounts, both at the center and in the provinces, in preparation for consolidating the balances in them in the TMA.

20. The Fiscal Policy Department is responsible for the consolidation of overall data on government debt, domestic and external. The Treasury Department deals directly with domestic borrowing (significant in 2008–09 for the first time in recent years). However, most borrowing is the responsibility of the External Finance Department, which controls foreign borrowing by government and SOEs. The Ministry of Planning and Investment takes the lead in coordinating grants from development partners. Systems for contracting loans appear to be adequate. There are some problems of precision in the debt data resulting from changes in the exchange rates between the US$ (in which the records are kept) and other currencies in which some Lao PDR debts are denominated. There have also been cases of loans by banks for the construction of public facilities that have been

guaranteed by provincial governments, with the subsequent repayments to contractors financed either from the budget or from the proceeds of subsequent asset sales. Apart from provision for the repayment of arrears through the budget, these transactions have not been recorded in the budget or in aggregate debt statistics.

21. Personnel records of all permanent public servants (including those employed in health and education but excluding police and armed forces) are kept by the Public Administration and Civil Service Authority (PACSA). The authority is notified of all salary advancements and promotions and sets annual limits for new hirings, in consultation with MoF, which fixes the overall salary grid. MoF then allocates funds for salary payments to each ministry and province based on the approved staff numbers and positions within the grading structure. The Treasury keeps a detailed database of all staff (other than police and armed forces), which is updated twice a year to record details of promotions and advancements as notified by ministries and provinces to PACSA. The total payments to individuals in each payroll must be consistent with the aggregate staff numbers, grades, and incremental steps notified quarterly by PACSA. Most staff are paid directly through the banking system, which removes most of the risks inherent in cash payments. The system thus provides for an element of cross-checking between personnel and payroll records and ensures an audit trail from personnel records that are updated. Nevertheless, since the last census of government employees in 2006, there have been only limited physical verifications of the existence and characteristics of the officials concerned. Partial verifications in the health and education sectors in 2007 led to the identification of cases in which salaries were still being drawn for teachers who had left their posts. PACSA intends to organize a full census of all civilian employees in 2010.

22. Procurement legislation is generally in accordance with best international standards, including publication of information about tenders and contract awards. However, the legislation excludes any provision for independent mechanism to deal with complaints. Furthermore, institutional arrangements for dissemination and enforcement of the legislation have been inadequate, suffering from shortage of staff and resources. In addition, a central database of actual procurements that would confirm the appropriate use of fully competitive procurement methods is only now being put in place. There appears to have been widespread use of procurement methods that fell short of open competition, and no mechanism yet has been established to deal with complaints. A start has been made to train staff in the correct procurement procedures. At this point, this training needs to be rolled out throughout the country, and action is needed to see that these procedures are consistently applied.

23. As noted above, there are no specific controls over the commitment of expenditure. Controls apply only at the payment stage. The Treasury system ensures that payments are made only when they fall within approved allocations, and the rules for processing and recording transactions are generally observed. Internal audit as a service aimed at helping managers to improve the functioning of their systems remains to be developed. Inspection services hitherto have focused on compliance by officials with applicable rules, including on occasion dealing with citizens' complaints.

(e) Accounting, Recording, and Reporting

24. Data are entered manually into the GOL Financial Information System (GFIS) on the basis of payment instructions from line ministries and provinces. These data are the source of monthly and quarterly in-year budget execution reports, which have not yet been published in any form. From October 2009, this information should have been transmitted electronically from all central ministries and provinces, based on a revised Chart of Accounts, which should greatly facilitate ongoing reporting of revenue and expenditure. However, in practice, the system was not yet working fully in all provinces in March 2010. Nevertheless, confidence was expressed by MoF that the difficulties would be overcome by the end of the current (2009–10) financial year. The fact that the provinces will be reporting their expenditure in much more detail than ever before should make possible monitoring of their compliance with agreed priorities for the use of the new revenue stream from the Nam Theun 2 (NT2) hydroelectric project. However, payment instructions from the Treasury to BOL and to commercial banks in the provinces will continue to be transmitted on paper (by mail or by fax**).** There are monthly reconciliations between the Treasury Ledger and bank account records of payments and receipts. Only relatively small amounts of Treasury funds are paid as advances to persons or held in suspense accounts at banks outside the Treasury system. Although these amounts should be regularly cleared, the SAO Report on Budget Execution in 2007–08 identified cases in which Treasury advances were not cleared or repaid.

25. Apart from the salaries of teachers and medical personnel, the 2006 Public Expenditure Tracking Survey found that (1) few resources for materials, equipment, or maintenance reach schools or primary health units and (2) little information is available locally about the resources to be expected. In the last 2 years, Annual Financial Statements of revenue and expenditure (but not financial assets and liabilities) prepared in accordance with national accounting standards have been submitted for audit 7–8 months past the end of the fiscal year. SAO has raised additional concerns about the completeness of these statements because of their omission of expenditure financed from fees and charges and the associated revenues.

(f) External Scrutiny and Audit

26. SAO, whose remit extends to SOEs and the execution of projects as well as government finance, is at an early stage of development. A peer review of its development needs has been carried out by the Office of the Auditor-General of New Zealand, and support for its work is now included in the Public Financial Management Strengthening Programme (PFMSP) (see below). So far, SAO's work on government finance has been restricted to an examination of budget execution and a compliance audit each year of a sample of line ministries and provinces. SAO aims to follow international auditing standards and to develop its work on performance audit. Its report on budget execution is submitted to the National Assembly within three months of receipt of the Financial Statement from MoF. Some publicity is given to elements of this report, which is considered in detail by the Economic and Standing Committees of the NA, with recommendations formulated for endorsement in a plenary session. However, SAO's annual activity report, and its reports on the ministries and provinces selected for compliance audit are submitted only to the Prime Minister and the members of the NA

Committees. SAO acknowledges that it does not yet have sufficient resources to provide for an early and consistent follow-up of all its recommendations. Nevertheless, it does aim to follow up its more significant recommendations in all subsequent audits.

27. The submission of the detailed line item budget to the NA at its June/July session follows detailed consultations between its Economic Committee and MoF and MPI on budget allocations and investment priorities. These consultations enable the NA to formulate recommendations to the government which are taken into consideration before the budget is formally approved. Any significant in-year revision of the budget must be approved by the NA at its November/December session.

(g) Donor Practices

28. As already noted, Lao PDR regards all externally funded expenditure, whether by grant or loan, as part of budget expenditure. Direct budget support is only a small fraction of total external financing. Donors provide indications of the amount of support to be expected each year but do not provide a quarterly schedule of payments for the year. In some cases, actual payments have deviated from the amounts foreshadowed. Most donors give indications of the expected disbursements of project and program aid by the middle of each calendar year, in formats reflecting their practices rather than the requirements of the Lao PDR budget. They also report most actual disbursements, but there may be significant delays before reports are submitted. Direct budget support, which by definition uses national procedures, represents only a small proportion of total external financing. So far as the rest of external financing is concerned, as just noted, most donors still use of their own procurement and payment procedures, even though, in principle, the expenditure is included in budget proposals and Execution statements, and is formally within the scope of SAO's audit.

Assessment of the Impact of PFM Strengths and Weaknesses

29. This section considers the impact of the findings summarized above on the maintenance of macrofiscal discipline, strategic allocation of resources, and efficiency of service delivery.

(a) Aggregate Fiscal Discipline

30. In recent years, the public financial management (PFM) system described above has been reasonably effective in maintaining macrofiscal discipline. This consistency has made possible some improvement in Lao PDR's external debt position, although risks of debt distress remain. Cash rationing has been avoided, and it has not been necessary to impose substantial in-year expenditure reductions. Excessive decentralization of authority to the provinces is being corrected. Nevertheless, there are still indications that significant expenditure financed by users' fees and charges remain outside the budget and that commitments are being undertaken on domestically financed investment projects without any effective central control. In 2008–09 significant off-budget expenditure on facilities for the SE Asian Games was financed through the banking system, but this practice has not continued. Although future debt sustainability has been regularly reviewed in

cooperation with the IMF and World Bank, a stable medium-term fiscal framework within which budget planning could take place each year has not yet been established

(b) Strategic Allocation of Resources

31. The PFM system hitherto has not been well adapted to secure the optimum allocation of scarce resources to contribute to both the growth of the economy and the improvement of public services. The absence of a consistent functional/sectoral allocation of resources across general government as a whole has made it difficult to assign clear overall priorities for the development of the main public services consistent with the National Socio-Economic Development Plan (NSEDP). However, this year the government has begun to take steps to ensure that the provinces implement its priorities for health and education. Effective central control of the functional allocation of resources will be needed if the GOL is to be able to demonstrate to the NT2 hydroelectric project development partners that the revenues really are being spent on new and additional programs in basic education, primary health care, and road communications.[1] The separate planning of current and capital expenditures, and the absence of any articulated programs for the development of most public services that would take into account both the resources—current and capital—prospectively available, and the specific outputs to be achieved, both illustrate the need to get a better grip on the strategic allocation of resources. The current work by the Ministry of Health to plan the development of services in six broad program areas represents an important first step in the required direction. The Ministry of Education is understood to be developing comparable plans. However, in neither case has the ministry's plan been prepared within the given total of resources allocated to the sector. The fact that SOEs do not publish audited accounts consistent with International Financial Reporting Standards (IFRS) obstructs the attraction of investment in these activities, which would contribute to the growth of the economy.

(c) Efficient Service Delivery

32. The development of public services in Lao PDR continues to experience numerous constraints. They are the lack of resources, weak policy-based budgeting, mediocre procurement practices, lack of information to front-line service providers and the general public about resources provided for service delivery, and a general lack of information about or scrutiny of the results achieved. Greater clarity in budgeting, and a much clearer medium-term resource allocation framework of themselves would contribute to more efficient service delivery. Other improvements in government administration also should yield significant benefits. Greater assurance of effective competition in public procurement should enable better standards of service within the same financial envelope. Moreover, better planning and sequencing of investment projects should reduce the risk that contractors will inflate their tenders to offset the impact of subsequent payment delays. Improvements in the operation of the tax system should yield more resources available for the delivery of front-line services. Similar effects should result from improvements in the efficiency of other government operations

[1] Many remote districts that should have priority in social and economic development and in the improvement of public services are inaccessible in the wet season due to road conditions.

(through better staff training and human resources management and through automation of recording, accounting, and payment processes). Greater clarity about the government's objectives and greater transparency in accounting for its activities could help to build public support for necessary changes, and reduce the scope for obstruction by vested interests. Most of these issues are being addressed, in one way or another, through the PFMSP described next.

Prospects for Reform Planning and Implementation

33. Lao PDR already has embarked on a very ambitious plan for PFM improvement: the Public Financial Management Strengthening Program (PFMSP), which addresses many of the problems identified in this assessment. With the support of the World Bank, ADB, and a number of other development partners, and the help of a range of international consultancy expertise, Lao PDR is reforming budgeting, taxation (the introduction of VAT), the Treasury function, financial reporting and accounting, public procurement, and the functional allocation of resources at the provincial level. Every quarter, progress on all of the different actions that form part of the PFMSP is comprehensively reviewed by the PFMSP Implementing Committee to keep them on track. However, due to limited implementation capacities and capabilities, the complexities of reform measures, and difficulty in interagency and central-local coordination, the government agencies often appear to find it difficult to take the detailed follow-up actions to ensure that new legislation or Prime Ministerial decrees are implemented in the intended timetable. Some areas seem to lack a strong commitment to push for faster implementation of the reform. As a result, progress on some reform aspects has been slower than hoped. For example, it was only in the third quarter of 2009 that the operational manual, information recording system, and associated training originally foreseen for 2007 to underpin the improved legislation on public procurement started to be rolled out. In addition, VAT, which was the subject of 2006 legislation, finally took effect in January 2010. Nevertheless, these various reform efforts—including the completion of the centralization of Treasury, Tax, and Customs and the progressive introduction of the improved GFIS reporting system based on an improved COA from October 2009—represent very important progress.

MAIN REPORT

1. INTRODUCTION

1.1 Objective of the PFMPR

1.1.1 The purpose of the Public Expenditure and Financial Accountability (PEFA) Assessment is to provide the Government of Lao PDR (GOL) with a concise, standardized, objective, Indicator-led assessment of the country's public financial management (PFM) systems to provide a benchmark against which to measure the further strengthening of Lao PFM. Partial assessments have been made in the past.[2] However, this is the first comprehensive diagnosis covering the overall PFM system in Lao PDR.

1.1.2 This Public Financial Management Performance Report (PFMPR) was prepared in the context of the ongoing work of the Public Financial Management Strengthening Program (PFMSP), which GOL is implementing with the assistance of the ADB, World Bank, and other development partners. The PFMSP embodies a wide range of actions in a defined timetable covering improvements in budget formulation, reporting, and accounting in the Treasury function, including the necessary IT infrastructure; in taxation (including the introduction of VAT); and in external public audit. It also includes the development of medium-term fiscal and expenditure frameworks that would facilitate the allocation of resources to the provision of different public services and the articulation between investment planning and the associated ongoing recurrent expenditure requirements. The PFMSP is supported by a Multi-Donor Trust Fund cofinanced by EC, AusAID, Sida (Sweden), and SDC (Switzerland) and administered by the World Bank. This fund supports GOL's additional costs directly incurred in developing new systems and procedures and training staff in their use. Other non-MDTF donors such as ADB, Japan, and Singapore also support the implementation of the PFMSP.

1.1.3 The first step in the preparation of this assessment was a workshop in April 2009 for the main stakeholders in GOL/MoF and other ministries, with the principal development partners, at which the purpose and methodology of the assessment were presented. Next, the Fiscal Policy Department of MoF assembled a team drawn from different departments of MoF and certain other stakeholders (MPI, SAO, BOL). Their task was to collect the evidence needed to make a self-assessment of the current Lao PFM system that followed the standard PEFA methodology and criteria. This self-assessment material, although not complete, formed the starting point for the preparation of this draft report by the World Bank team. A first draft was given to MoF at the end of

[2] Notably, an initial attempt at a PEFA assessment sponsored by the European Commission in 2006, which sought to rate 21 of the 31 Performance Indicators (PIs); and a 2006 World Bank Public Expenditure Review.

August 2009 and also was the subject of peer review within the World Bank and by the PEFA Secretariat. The draft report was subsequently revised to take account of all comments received and to reflect further discussion among the review team, MoF, and other officials engaged in the self-assessment work, as well as discussions with officials responsible for aspects of the assessment that were not covered by the material prepared by the MoF self-assessment team. The final draft was circulated for comments to the GOL Team, the Development Partners active in the PFM areas in Lao PDR, the peer reviewers, and the PEFA Secretariat. The current report was finalized taking into account comments received during the last round of review.

1.1.4 The preparation of this assessment has involved detailed discussions with representatives of a wide range of GOL ministries and agencies to review and assess the documentary and other evidence needed. MoF discussions were held with the Fiscal Policy, Budget, Treasury, Tax, Accounting, External Finance, State-Owned Enterprise Finance Management Department and the Procurement Monitoring Office under the MOF Cabinet, as well as with a number of international consultants working with GOL on different aspects of the PFMSP. In addition, the team met with representatives of MPI, BOL, the Ministry of Health and the Secretariat of the National Assembly. The team also benefited from information collected by the Treasury Single Account (TSA) advisor, Janis Platais, from his field trip to Champasak, Saravan, Xekong, and Savankhet provinces.

1.2 Methodology

1.2.1 The PEFA methodology is set out in the Public financial management Performance Measurement Framework (www.pefa.org). It is based on 28 indicators covering all aspects of a country's PFM system, and on three indicators that measure the interaction between the government concerned and its development partners. It should be emphasized that PEFA is essentially a backward-looking process based on evidence about actual current public sector financial management practice. The assessment takes into account statistical information about different aspects of revenue and expenditure over the most recent 2–3 years. Each indicator is scored on a scale from A to D. The bases for these ratings are the minimum requirements set out in the methodology. Many Indicators include two or more dimensions, which are "added" using PEFA-specific methods M1 or M2. For method M1, the weakest link is decisive, that is, the overall rating is based on the lowest score. For M2, the average of the subratings is used to derive the score for the overall indicator (see the PEFA Framework instructions on Scoring Methodology).

1.2.2 Apart from the self-assessment material already described, the main sources of information that have been used for this PFMR are (a) official GOL documents and statistics; (b) external evaluations and reports (WB, IMF); and (c) interviews with users and providers of PFM information (government officials and professional advisors on aspects of the tax and legal systems). To the limited extent possible, the review team sought to triangulate information by seeking information from spending ministries as well as from MoF, and from taxpayers as well as tax collectors. Despite its efforts, the review team was not able to obtain any information directly from provincial administrations, and only very limited discussion was possible with the spending ministries.

1.3 Scope of the Assessment

1.3.1 The PEFA assessment focuses primarily on the national level of a country's PFM system. At the national level, it seeks to cover the entire PFM system, including cross-cutting and overall issues, the revenue side, and the budget cycle from planning through execution to control, reporting, and audit. A number of the Indicators are designed to probe how the national level interacts with subnational governments and with public service providers at local level. Each country has its own arrangements concerning these matters. In some federal countries, lower-tier governments may be completely independent of the central government in how they finance themselves and in deciding what public services they should provide, and on what terms. In the most centralized countries, administrations at the regional level may simply be part of central government and under its direct authority.

1.3.2 Lao PDR is a unitary government, in which the 17 provinces/city and 141 districts remain part of the central government and do not have any representative institutions to which the provincial and district administrations could report. Nonetheless, provincial governors exercise considerable authority independent of central government line ministries. Thus, they have been in a position to make their own decisions about the functional allocation of their budgetary resources that may not be fully in line with the declared priorities of the central government for the development of public services. Therefore, despite the absence of representative institutions at lower levels of government, the way in which the volume of resources available to each province and district is determined and the way that these resources are allocated to the different services necessarily have been reviewed as part of this assessment.

1.3.3 In addition to the government revenue and expenditure included in the budget, there are eight extra-budgetary funds directed toward particular purposes (such as roads, forestry, public sector social benefits). These funds are managed by particular ministries or agencies and are wholly or partially financed by specific revenues (such as taxes on road transport, social security contributions). MoF has included the revenue and expenditure of the Roads and Forestry Development funds in the budgetary aggregates presented in this report, but for the other funds only the amount of any budgetary contribution is shown. A complete picture of central government revenue and expenditure is required to determine the government's overall financing needs. However, such a picture can be given only if the extra-budgetary funds and other extra-budgetary spending are taken into account. To cover the financing needs of the public sector as a whole, the assessment must review available information on these points as well as take into account net borrowing by state-owned enterprises (SOEs). The assessment takes into account statistical information related to revenue and expenditure during the most recent three fiscal years for which information is available, in this case, 2005–06, 2006–07, and 2007–08 (the fiscal year in Lao PDR runs from 1 October to 30 September). When possible, information about progress in improving PFM available up to the time of the final mission in March 2010 (when the revised report was presented to MoF officials and representatives of other donor organizations) has been taken into account. Out-turn figures for 2008–09 were not available at that time.

2. Country Background and Information

To enable sufficient understanding of the core characteristics of the PFM system and the wider context in which PFM changes would take place, this section provides information on the country and economic contexts of Lao PDR.

2.1 Context and Economic Situation

2.1.1 The Lao PDR has a total surface area of 236,000 square kilometers (km) and a population of approximately 6 million, approximately 25 percent of whom live in urban areas. It was an independent country before becoming a French colony in the late nineteenth century. It recovered its independence in 1955. There followed 20 years of conflict resulting from the Indochina war, which concluded when the Lao Peoples' Revolutionary Party (LPRP) assumed complete control of the country in 1975. The country is landlocked; it is bordered by Thailand, China, Myanmar, Vietnam, and Cambodia. Per capita income at US$850 (2008) is approximately 25 percent of the level in Thailand, but only a little behind Vietnam, and significantly ahead of Cambodia and Myanmar. Economic growth has averaged 7.1 percent a year since 2003, based particularly on mining, hydroelectricity, manufacturing, and tourism. Nonetheless, Lao PDR remains primarily an agricultural country, with 75 percent of the labor force still engaged in agriculture. The incidence of poverty has been falling rapidly, from approximately half of the population in 1995 to approximately 27 percent in 2008. Lao PDR remains on the United Nations' (UN) list of the least developed countries. The GOL has set the objective of graduating above this status by 2020.

Table 2.1 Lao PDR: Selected Economic Indicators, 2005–09

	2005	2006	2007	2008	2009
GDP (nominal, US$ mil)	2,761.0	3,577.0	4,170.0	5,374.0	5983.0
GDP per capita (current US$)	493.0	594.0	679.0	859.0	986.0
% changes over the previous year					
Real GDP	7.1	8.4	7.5	7.2	7.0
Consumer prices	7.2	6.8	4.5	7.6	0.1
% of GDP					
General government balance (year to Sept.) incl. grants	-4.6	-3.0	-2.9	-2.0	-4.6
External grants	1.7	2.0	1.7	1.3	1.7
Current account balance	-17.8	-10.3	-15.8	-16.5	-6.6
FDI, net	8.9	9.4	18.7	16.9	12.8
Public sector domestic debt				2.1	2.7
Public sector external debt	63.1	59.1	53.1	54.5	54.5
Poverty incidence (national definition) (%)			28.0		

Sources: WB Economic Monitors, IMF, MoF.

2.1.2 Lao PDR's growth in recent years has resulted primarily from opening up the country to foreign direct investment (FDI). Investment has represented approximately 33 percent of GDP in recent years, of which 75 percent was in the private sector. Approximately 80 percent of public sector investment has been externally financed on concessional terms.

2.1.3 The substantial inflow of investment finance has been matched by a continuing high current account deficit of 15.8 percent of GDP in 2007 and 12.5 percent in 2008. After rising rapidly up to 2008, export revenues from mining, manufacturing, hydroelectricity, and tourism fell back by approximately 7 percent in 2009. However, the fall in import prices of fuel and capital goods during the recession more than counteracted this drop, so that the current account deficit fell to less than 8 percent of GDP in 2009. Because exports account for less than approximately one-third of GDP (as compared with two-thirds in Thailand), and go mainly to countries in the region rather than to the Northern Hemisphere markets most seriously affected by the recession, Lao PDR has been relatively less affected by the global difficulties.

2.2 Overall System of Government and Government Development Strategy

2.2.1 Lao PDR remains a one-party State under the LPRP. The country is divided into 16 provinces and Vientiane, the capital city. However, there are no representative institutions at the lower levels of government. Each province is divided into a number of districts, which are made up of numerous towns and villages. Provincial governors and the heads of districts and villages are appointed by the central government.

2.2.2 In contrast, although the ministries and provinces are all part of the central government and financed through the national budget, much executive authority has been delegated to provincial governors, who have been able to decide how to spend the resources that they receive from the budget. Although the LPRP remains the supreme authority, legislation and the budget now must be approved by the 115-member NA, which exercises some oversight over the GOL. Elections to the NA take place every five years, the most recent were in 2006. Only two members of the current NA are not members of LPRP. The judiciary also remains under the effective control of the Party. The work of the State Audit Organization (SAO) is now founded on the 2007 Audit Law,[3] and reports are made to the NA as well as to the Prime Minister. SAO's budget was substantially increased in 2009–10 at the insistence of the NA.

2.2.3 Social and economic development in Lao PDR falls within the framework of successive five-year plans. The current version is the 2006–10 National Socio-Economic Development Plan (NSEDP). This plan focuses on the development of the economy and the strengthening of public financial management (PFM). The country has been making fair progress toward achieving the United Nations' various Millennium Development Goals by 2015, but the NSEDP does not set a defined path for progress or allocate resources year by year to specific purposes. The government's efforts are supported by a network of development partners (World Bank, Asian Development Bank, European

[3] SAO's remit is not specified in the Constitution.

Commission and various bilateral donors) who are contributing to the successive phases of the Poverty Reduction Support Operation (PRSO) as well as lending on concessional terms to finance investments and providing a Multi-Donor Trust Fund to meet the costs of the Public Financial Management Strengthening Program (PFMSP).

2.2.4 Strengthening PFM is fundamental to the successful development of Lao PDR. Current tax revenue amounts to only approximately 12 percent of GDP, severely limiting the government's ability to finance the provision of public services. It is thus essential to make taxation as efficient and effective as possible, and to make sure what spending the government is able to undertake supports the highest possible level of public services. Spending on health and education has been particularly low, partly as a result of the overall shortage of finance and partly as a result of provinces' deciding to give other services higher priority. The 2006 World Bank Public Expenditure Review (PER) found that Lao PDR's public expenditures on health and education as percentages of GDP were at less than 1 percent and less than 2 percent, respectively—near to the lowest in the world. Nor is there any general provision of social security benefits. With the help of the major donors, GOL is seeking to address the most serious deficiencies in basic education, primary health care, and road communications, particularly in the "priority districts" in which the incidence of poverty is highest. To improve services in these areas, the Government has committed itself to use the revenues from the Nam Theun 2 Hydroelectric project, which started to come on stream in 2010 and eventually will approach 2 percent of current (2009) GDP.

2.3 DESCRIPTION OF BUDGETARY OUTCOMES

Fiscal Performance

2.3.1 Over 2005–06 to 2007–08, Lao PDR's general government operations were in deficit in the range of 2 percent–3 percent of GDP. (In contrast, the deficit for 2008–09 is estimated to have increased approximately 6.8 percent as a result of revenue shortfalls associated with the global recession, with the additional off-budget spending including the costs of hosting the 2009 SE Asian Games). Capital expenditure accounted for a relatively high proportion of total expenditure throughout this period, partly reflecting the high proportion of donor finance directed to investment projects. External grants as a proportion of GDP were declining during this period, although they have now reverted to the higher level experienced in 2005–06. Tax revenue was on a rising trend as a proportion of GDP until the end of 2007–08. The increase reflected the growing importance of resource revenues from mining and hydroelectricity. This rising trend should resume from 2009–10 as metal prices recover and additional hydroelectric capacity comes on-stream.

Table 2.2 Lao PDR: Consolidated Budget Indicators, 2005-06 to 2007-08 *(% GDP)*

	2005-06	2006-07	2007-08
Total revenue and grants	14.5	15.8	15.6
• Tax revenue	10.6	12.1	12.5
• Nontax revenue	1.8	1.9	1.8
• External grants	2.0	1.7	1.3

Total expenditure	17.4	18.6	17.7
• Current expenditure	9.1	8.9	10.3
• Capital expenditure	7.2	8.1	7.0
Overall Balance (including off-budget)	-3.0	-2.9	-2.0
Domestic financing (net)	-1.1	-0.9	-1.0
External financing (net)	4.0	3.8	3.0

Source: IMF.

Allocation of Resources

2.3.2 The normal presentation of budgetary outcomes in a PEFA report includes a table of the functional allocation of resources during the previous three years. Doing so in the case of Lao PDR is not possible for two reasons: (1) the available information about the central government does not distinguish expenditure in some major COFOG categories (notably defense and public security) from a large "miscellaneous" category, and (2) information about the functional allocation of expenditure at province and district levels is not readily available.

2.3.3 The increasing proportion of current expenditure absorbed by public sector wages and salaries is shown in the following table of actual budgetary allocations by economic classification.

Table 2.3 Actual Budgetary Allocations by Economic Classification *(% GDP)*

	2005-06	2006-07	2007-08
Total	17.4	18.6	17.7
Current expenditure	9.1	8.9	10.3
• Wages and salaries	3.7	3.9	4.6
• Purchases of goods and services	2.7	2.1	2.6
• Transfers	2.0	2.1	2.3
• Interest payments	0.8	0.7	0.8
• Carry-over and arrears	1.2	1.7	0.3
Capital expenditure	7.2	8.1	7.0

Source: IMF 2009 Article IV Consultations Report.

2.4 DESCRIPTION OF THE LEGAL AND INSTITUTIONAL FRAMEWORK FOR PFM

Key Actors in Lao PDR's PFM Process: Roles and Responsibilities

2.4.1 The main responsibility for PFM rests with the Ministry of Finance (MoF) and the Ministry of Planning and Investment (MPI). MoF is responsible for revenue, expenditure, financing, accounting, reporting, and the overall fiscal stance. MPI prepares the five-year National Socio-Economic Development Plan (NSEDP). This ministry is responsible for economic forecasting and planning capital expenditure, including determination of the list of capital projects approved for the following year presented to the National Assembly as part of the budget.

2.4.2 Within MoF, coordination of the overall fiscal stance is the responsibility of the Fiscal Policy Department. The Budget Department allocates expenditure provision to ministries and provinces. The National Treasury manages the cash flow, including receipts and payments and is in charge of domestic borrowing. External borrowing (and the servicing of external debt) is the responsibility of the External Finance Department of MoF. The Department of International Cooperation (DIC) of MPI coordinates the receipt of external grants. Revenue is mainly the responsibility of the Tax Department (profit tax, income tax, turnover taxes, VAT,[4] and excise taxes) and the Customs Department (customs duties, and VAT, excise and turnover taxes collected on imports). The State-owned Enterprise (SOE) Department monitors the finances of SOEs, while the State Assets Department is in charge of revenues from the exploitation or sale of state property. The Accounting Department sets the accounting standards for both private and public sectors but is not responsible for government financial reporting (which is undertaken by the Budget and Treasury Departments). The Inspection Department has the remit to inspect financial management and financial operations in both MoF and line ministries, particularly when problems arise.

2.4.3 MPI has the responsibility to prepare the economic forecasts that provide the context for the budget preparation. Its Planning Department collects and prioritizes the investment projects to be approved by the GOL. In carrying out these functions, MPI takes into account the scope for external borrowing (determined by MoF External Finance Department in accordance with debt sustainability criteria), and the domestic finance that MoF considers can be made available for investment given the overall fiscal stance. The selection of projects should also reflect the objectives of the NSEDP and the GOL's objectives to reduce poverty.

2.4.4 Responsibility for actually carrying out government activities is shared between the line ministries and the provinces. The ministries are responsible for central functions of government and for national institutions such as universities and specialist hospitals. On the other hand, most public services are delivered to the citizens by provincial and district administrations. Provincial budgets are allocated directly by MoF without discussion with the relevant line ministries. Thus, provinces have been free to determine their own priorities, sometimes ignoring stated government priorities for preference to be given to the priority districts or, for example, to particular medical services. To establish some effective control over these priorities, the National Assembly has been pressing the government to introduce norms for the allocation of expenditure at province/district level. The provinces have also been in charge of the collection of most revenues and of Treasury operations in their areas, but these functions are being recentralized. The objective is to establish central Treasury control over all government revenues (including charges for services) and over all government bank accounts, and, eventually, to consolidate the bulk of the government's cash in the Treasury Main Account (TMA) at the Bank of Lao (BOL). Substantial progress already has been made with controlling tax and custom revenue despite the lack of effective automated interbank clearing

[4] VAT is from January 2010 on.

arrangements and of a computerized Treasury Information Management System. These lacks cause delays in consolidating government cash resources in the TMA.

2.4.5 External audit is the responsibility of the State Audit Organization (SAO) operating in accordance with the 2007 audit law, with the duty to report to the NA as well as to the Prime Minister. SAO is only now building up its capacity, and so far has made reports on budget execution for only 2006–07 and 2007–08. Its remit extends to SOEs and the audit of investment projects. Although publicity is given to some aspects of its budget execution reports, which are discussed extensively in the NA, it publishes no details of its other reports. Internal audit in the sense of a service to advise managements on improvements to administrative systems does not exist. The activities of inspection departments (State Inspection Authority at Prime Ministerial level, MoF, line ministry and provincial inspection departments) may have some over the character of internal audit, but these bodies are essentially instruments of control.

Budget Process and Budget Calendar

2.4.6 In principle, the budget process is determined by the 2006 Budget Law, which prescribes the procedures and the calendar to be followed in preparing the budget for submission to the NA. The law envisages the issue of a MoF circular early each (calendar) year with instructions on the rules to be applied by ministries, provinces, and districts in preparing the following year's budget. Dissemination of the circular should be followed by consultations with members of the NA and other stakeholders before submissions are made to MoF in February. MoF then consolidates the submissions into a draft budget to be submitted to the GOL in April. Once approved collectively by ministers, the budget should be submitted to the NA 15 days before the opening of its June/July session.

2.4.7 Actual practice has deviated sharply from this legal framework, although there have been consultations between MoF, line ministries, and provinces on the overall shape of the budget. However, the standard cost norms to be used in preparing budget submissions are those set out in Instruction 2348 (2008). No ceilings have hitherto been issued by MoF to guide ministries in the preparation of their budget bids. In fact, in 2009 no budget circular was issued. In the view of the Ministry of Health, for example, compliance with the currently applicable standard costs for particular activities as laid down by Instruction 2348 would justify a budget of 154 billion KIP for 2009–10. However, the actual prospect in July 2009 was that MoH would receive less than half this amount. The amount it would get from MoF in September 2009 would be broadly the same as that submitted by MoF to the NA and recently approved by it. However, this amount would bear little relation to MoH's submission. MoH recognized the reality of this situation, and informally made internal plans based on the assumption that it would receive a moderate increase of the amount (63 billion KIP) allocated to it for 2008–09.

2.4.8 It appears that actual PFM practice in Lao PDR often diverges in additional respects from the requirements stated in the law. Decree 381 (2005) envisages the establishment of a system to record the revenues from fees and charges received by health and education institutions and the associated expenditures. Prime Ministerial Decree 03/09 requires that all such revenue be paid into Treasury bank accounts (as the

Budget Law already had envisaged). However, neither instruction yet has been implemented. The institutions are reluctant to surrender control of funds essential to the maintenance of their operations for fear that they would then be diverted to other purposes. It may well be necessary to make arrangements whereby these revenues and associated expenditures would be included in the budget, with receipts and payments reported through GFIS, but the funds in question would remain under the effective control of the institutions collecting the revenues.

2.4.9 Tax advisors state that tax offices in different parts of the country adopt different interpretations of provisions of tax law,[5] and the center so far has failed to enforce a single interpretation. The recent centralization of tax and customs administration should facilitate more uniform and consistent interpretations of tax law provisions.

Box 2.1 PFM Legislation

Lao PDR's main PFM legislation comprises:

- Budget law, 2006
- Tax law, 2004
- Value-added tax law, 2006
- Audit law, 2007
- Accounting law,2007
- Decree 35/PM (2007) and implementing Decree 2160/MOF on gradual centralization of treasury, tax, and customs
- Decree 25/PM (2008) on implementation of Budget Law, again requiring charges for services to be included in the budget.

[5] For example, on the interpretation of the 2-year period for which losses may be carried forward to reduce liability to profits tax, and on the details of the personal income tax exemption for expatriate staff working in Lao PDR for less than 180 days a year.

3. ASSESSMENT OF PFM SYSTEMS, PROCESSES, AND INSTITUTIONS

SUMMARY OF PERFORMANCE MEASUREMENT FRAMEWORK

		Score
A. PFM outturns: Credibility of the budget		
PI-1	Aggregate expenditure out-turn compared to original approved budget	**B**
PI-2	Composition of expenditure out-turn to original approved budget	**NR**
PI-3	Aggregate revenue out-turn compared to original approved budget	**A**
PI-4	Stock and monitoring of expenditure payment arrears	**C+**
B. Key cross-cutting issues: Comprehensiveness and transparency		
PI-5	Classification of the budget	**C**
PI-6	Comprehensiveness of information included in budget documentation	**B**
PI-7	Extent of unreported government operations	**D+**
PI-8	Transparency of intergovernmental fiscal relations	**D**
PI-9	Oversight of aggregate fiscal risk from other public sector entities	**D+**
PI-10	Public access to key fiscal information	**C**
C. Budget execution		
C. (i) Policy-based budgeting		
PI-11	Orderliness and participation in the annual budget process	**C+**
PI-12	Multiyear perspective in fiscal planning, expenditure policy, and budgeting	**D+**
C. (ii) Predictability and control in budget execution		
PI-13	Transparency of taxpayer obligations and liabilities	**D+**
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	**C**
PI-15	Effectiveness in collection of tax payments	**NR**
PI-16	Predictability in the availability of funds for commitment of expenditures	**B+**
PI-17	Recording and management of cash balances, debt, and guarantees	**D+**
PI-18	Effectiveness of payroll controls	**C+**
PI-19	Competition, value for money, and procurement controls	**D+**
PI-20	Effectiveness of internal controls for nonsalary expenditure	**D+**
PI-21	Effectiveness of internal audit	**D**
C. (iii) Accounting, recording, and reporting		
PI-22	Timeliness and regularity of accounts reconciliation	**C**
PI-23	Availability of information on resources received by service delivery units	**D**
PI-24	Quality and timeliness of in-year budget reports	**C+**
PI-25	Quality and timeliness of annual financial statements	**D+**
C. (iv) External scrutiny and audit		
PI-26	Scope, nature, and follow-up of external audit	**D+**
PI-27	Legislative scrutiny of the annual Budget Law	**C+**
PI-28	Legislative scrutiny of external audit reports	**C+**
D. Donor practices		
D-1	Predictability of Direct budget Support	**D+**
D-2	Donor information for budgeting and reporting on project/program aid	**C+**
D-3	Proportion of aid managed by national procedures	**D**

3.1 Budget Credibility

3.1.1 The credibility of the budget matters to citizens, investors, and all those who will implement the budget. The difference between the initially approved budget and the actual expenditures and revenues measures the budget deviation, which provides a measure of the overall performance of the PFM system at a high level.

PI-1: Aggregate expenditure out-turn compared to original approved budget

Indicator	Brief explanation	Score
PI-1 Aggregate expenditure out-turn compared to original approved budget (Scoring method M1)	Actual expenditure deviated from the initially approved amount by more than 10 percent in only 1 of the last 3 years.	B

Source: GOL Official Gazettes for FY05–06 to FY07–08.

3.1.2 Aggregate expenditure out-turns compared to the original approved budget for 2005–06 to 2007–08 is shown in table 3.1. The approved budget is taken to be the budget as approved by the NA excluding debt interest and capital repayments, and also excluding donor funded project expenditure. By decision of MoF, revenue and expenditure of the Road Maintenance and Forestry Funds are included in the aggregates for the performance indicators, PI-1 and PI-3. For the other extra-budgetary funds, only the government contribution for the year in question is included. However, it does not appear that these other funds have significant revenue sources independent of the budget, so their incomplete integration into the consolidated budget arithmetic should not give a seriously misleading picture of the overall situation.

Table 3.1 Aggregate Expenditure Out-Turn Compared to Original Approved Budget

Year	Original budget *(KIP bil)*		Expenditure out-turn *(KIP bil)*		Amount of deviation *(KIP bil)*	Deviation from approved total *(%)*
2005–06	3,100		3,250		150	4.85
2006–07	3,714		4,011		297	7.99
2007–08	4,613		5,250		637	13.81

Source: GOL Official Gazettes for FY05–06, FY06–07, FY07–08

PFMSP Efforts Underway: The ADB-sponsored support for MTEF is providing training in expenditure and revenue forecasting techniques that may strengthen the reliability of these estimates in the future.

PI-2: Composition of expenditure out-turn to original approved budget

Indicator	Brief explanation	Score
PI-2 Composition of expenditure out-turn compared to original approved budget (Scoring method M1)	The aggregation of several major spending ministries into a single “Other” heading, and the fact that provincial expenditure is broken down only by province and not by function make it impossible to assess whether there have been significant in-year changes in the expenditure mix.	NR

3.1.3 Table 3.2 presents such information as is available. This Indicator seeks to measure whether there were significant changes in the allocation of budget expenditures to administrative units in the course of budget execution, which would not be shown by the aggregate comparison. In practice, the aggregation of several major ministries into a single “Other” category and the aggregation of different functional expenditures in the total for each province cause the numbers to present an unsatisfactory basis for the assessment, since there is no assurance that there was not significant variance within these aggregates. In practice, the high proportion of expenditure allocated to public service pay, with stable numbers employed by each administrative unit, restricts the scope for in-year reallocations. However, the evidence does not enable a firm judgment to be made in accordance with the PEFA criteria.

Table 3.2 Variance in Expenditure Composition of the Budget

Category	2005–06				2006–07				2007–08			
	Budget *(KIP mil)*	Executed *(KIP mil)*	%	Deviation	Budget *(KIP mil)*	Executed *(KIP mil)*	%	Deviation	Budget *(KIP mil)*	Executed *(KIP mil)*	%	Deviation
Central level	**1,793,473**	**1,708,935**	**-4.71**	**(84,538)**	**2,173,611**	**2,424,504**	**11.54**	**250,893**	**2,469,547**	**3,053,655**	**23.65**	**584,108**
Ministry of Foreign Affairs	108,499	108,215	-0.26	(284)	128,774	124,505	-3.32	(4,269)	158,572	148,843	-6.14	(9,729)
Ministry of Justice	10,386	5,280	-49.16	(5,106)	6,207	6,152	-0.88	(55)	10,993	10,993	0.00	0
Ministry of Planning and Investment	4,667	-	-100.00	(4,667)	-	6,363		6,363	7,618	7,707	1.17	89
Ministry of Finance	77,339	17,982	-76.75	(59,357)	68,185	68,236	0.07	51	39,651	39,698	0.12	47
Ministry of Agriculture and Forestry	29,580	30,009	1.45	429	38,359	29,713	-22.54	(8,646)	27,443	32,391	18.03	4,948
Ministry of Public Works and Transportation	129,825	125,602	-3.25	(4,223)	139,748	172,037	23.11	32,289	79,386	164,620	107.37	85,234
Ministry of Commerce	16,946	8,375	-50.58	(8,571)	5,727	5,344	-6.69	(383)	-	-		-
Ministry of Industry and Handicraft	5,283	5,215	-1.29	(68)	18,865	10,747	-43.03	(8,118)	-	-		-
Ministry of Information and Culture	16,555	16,212	-2.07	(343)	17,810	17,722	-0.49	(88)	23,186	22,563	-2.69	(623)
Ministry of Labor and Social Welfare	24,928	24,126	-3.22	(802)	28,187	28,087	-0.35	(100)	65,810	100,422	52.59	34,612
Ministry of Education	92,113	85,677	-6.99	(6,436)	101,308	97,063	-4.19	(4,245)	65,289	106,163	62.60	40,874
Ministry of Public Health	28,924	28,551	-1.29	(373)	31,367	31,698	1.06	331	53,683	49,963	-6.93	(3,720)
Other Line Organizations	1,248,428	1,253,690	0.42	5,262	1,589,074	1,826,837	14.96	237,763	1,937,916	2,370,293	22.31	432,377
Local level	**1,306,527**	**1,541,487**	**17.98**	**234,960**	**1,540,390**	**1,586,196**	**2.97**	**45,806**	**2,143,453**	**2,196,587**	**2.48**	**53,134**
Vientiane Capital	138,432	132,724	-4.12	(5,708)	159,550	158,230	-0.83	(1,320)	226,825	225,434	-0.61	(1,391)
Oudomxay Province	59,601	60,233	1.06	632	74,875	75,809	1.25	934	101,304	104,645	3.30	3,341
Luangprabang Province	105,845	105,265	-0.55	(580)	123,930	121,821	-1.70	(2,109)	169,743	173,279	2.08	3,536
Sayabouly Province	79,966	83,280	4.14	3,314	96,330	94,442	-1.96	(1,888)	128,718	124,826	-3.02	(3,892)
Xiengkhouang Province	98,393	94,152	-4.31	(4,241)	83,550	92,584	10.81	9,034	126,146	121,672	-3.55	(4,474)

Category	2005–06				2006–07				2007–08			
	Budget *(KIP mil)*	**Executed** *(KIP mil)*	**%**	**Deviation**	**Budget** *(KIP mil)*	**Executed** *(KIP mil)*	**%**	**Deviation**	**Budget** *(KIP mil)*	**Executed** *(KIP mil)*	**%**	**Deviation**
Viengchan Province	96,174	142,958	48.64	46,784	127,650	127,403	-0.19	(247)	168,984	168,660	-0.19	(324)
Khammouan Province	79,690	93,040	16.75	13,350	95,478	105,014	9.99	9,536	131,054	138,730	5.86	7,676
Savannakhet Province	139,160	196,954	41.53	57,794	161,050	166,998	3.69	5,948	220,805	229,020	3.72	8,215
Champasack Province	111,787	156,556	40.05	44,769	131,532	137,905	4.84	6,373	187,569	191,834	2.27	4,265
Phongsaly Province	48,909	40,829	-16.52	(8,080)	55,930	53,945	-3.55	(1,985)	76,305	80,223	5.14	3,918
Luangnamtha Province	46,832	48,454	3.46	1,622	62,745	66,761	6.40	4,016	89,573	96,345	7.56	6,772
Borkeo Province	39,624	44,883	13.27	5,259	53,250	55,424	4.08	2,174	73,206	76,261	4.17	3,055
Houaphan Province	64,877	93,539	44.18	28,662	75,430	82,606	9.51	7,176	109,250	112,585	3.05	3,335
BOLikhamxay Province	58,201	69,103	18.73	10,902	69,500	75,366	8.44	5,866	101,595	105,509	3.85	3,914
Saravanh Province	55,000	64,943	18.08	9,943	67,770	70,677	4.29	2,907	96,260	102,579	6.56	6,319
Sekong Province	36,400	48,656	33.67	12,256	45,000	49,028	8.95	4,028	62,531	67,169	7.42	4,638
Attapeu Province	47,636	65,920	38.38	18,284	56,820	52,184	-8.16	(4,636)	73,585	77,815	5.75	4,230
(% coverage)	**60**	**61**			**57**	**54**			**58**	**55**		
Total expenditure	**3,100,000**	**3,250,422**	**4.85**	**150,422**	**3,714,001**	**4,010,700**	**7.99**	**296,699**	**4,613,000**	**5,250,242**	**13.81**	**637,242**
Total expenditure deviation *(%)*				**4.85**				**7.99**				**13.81**
Total absolute variance *(%)*				**11.87**				**10.04**				**14.86**
Variance over expenditure deviations				**7.02**				**2.05**				**1.05**

Source: GOL Official Gazettes for FY05–06, FY06–07, FY07–08

PI-3: Aggregate revenue out-turn compared to original approved budget

Indicator	Brief explanation	Score
PI-3 Aggregate revenue out-turn compared to original approved budget (Scoring method M1)	Actual domestic revenue collection exceeded the budgeted amount in each of the last three years.	A

3.1.4 Table 3.3 shows budget estimates and out-turns for each major type of revenue accruing to the budget for the period 2006–08. Actual revenue substantially exceeded the budgeted amount in all 3 years, by as much as 12.6 percent in 2006–07 and by smaller percentages in the other 2 years.[6] It appears that the 2008–09 shortfall resulting from the recession was smaller than might have been feared and that it was more than offset by additional grant receipts.

Table 3.3 Revenue Out–Turn Compared to Original Budget *(KIP bil)*

	2005–06		**2006–07**		**2007–08**	
	Budget	**Actual**	**Budget**	**Actual**	**Budget**	**Actual**
Tax revenue	1,670.0	1,795.1	2,033.0	2,584.1	2,670.0	3,190.1
Customs revenue	1,294.0	1,360.6	1,470.0	1,572.8	1,820.0	1,891.5
Revenue from state assets	943.0	1,042.1	1,144.0	1,042.3	1,390.0	1,342.8
Land management	43.0	41.0	53.0	48.7	-	77.9
Timber royalties	150.0	57.2	150.0	212.2	150.0	105.2
Total	4,100.0	4,411.3	4,850.0	5,460.1	6,030.0	6,617.5
Deviation from budget *(%)*		7.6		12.6		9.7

Sources: GOL Official Gazettes for FY05–06, FY06–07, FY07–08.

PI-4: Stock and monitoring of expenditure payment arrears

Indicator	Brief explanation	Score
PI-4 Stock and monitoring expenditure payment arrears (Scoring method M1)	(i) Apart from some outstanding payments for electricity, for which most of the accumulated arrears have been paid off, the Treasury Department is not aware of any arrears of current expenditure at central level. Action is being taken to provide for paying off arrears owing to contractors and utility suppliers at province and district level, and to prevent additional such arrears from being incurred (B) (ii) Specific initiatives have been undertaken to obtain information about arrears, which is not generated by routine expenditure returns. (C)	C+

[6] According to the PEFA Secretariat Instruction, this Indicator is asymmetric. Collecting significantly less revenue than the budget estimate results in a lower score, but collecting significantly more revenue than indicated in the budget still scores A.

(i) Stock of expenditure payment arrears

3.1.5 Since the National Treasury would reject payment requests if they exceeded approved budget, in the past, provincial and district treasury officers experiencing shortage of funds have deferred payments for utilities. Provinces have given guarantees for bank lending to contractors for public construction works, the costs of which then would be met out of future year budget allocations or from the sales of public land. Specific enquiries have established that the total arrears to electricity suppliers currently amount to approximately 2 percent of total public expenditure in 2008–09. Action has been taken to (1) provide for utility arrears to be paid off by the central Government in installments by the end of 2010–11 and (2) prevent future off-budget financing of public investment through the issue of guarantees for bank lending to contractors. Dimension score: B.

(ii) Availability of data for monitoring the stock of expenditure payment arrears

3.1.6 The normal expenditure execution system does not automatically generate information about utility payment arrears, and about off-budget financing of public investments through the issue of bank guarantees. However, arrangements are in place to monitor the situation, now that the amount of the arrears has been established. Dimension score: C.

3.2 Comprehensiveness and Transparency

PI-5: Classification of the budget

Indicator	Brief explanation	Score
PI-5 Classification of the budget (Scoring method M1)	The cash budget is set using administrative and economic classifications broadly consistent with GFS 1986, although some major repairs may be classified as investment, and some purchases of office equipment may be treated as current expenditure. However, hitherto there has been no functional classification.	C

3.2.1 The intention of this Indicator is to assess whether all expenditure is budgeted and reported according to all applicable classifications, including a GFS-consistent economic presentation and, where applicable, its place in a program directed toward a specific policy objective. In Lao PDR, very detailed information is given in the cash budget presentation about the economic and administrative classification of most of the expenditure for which the approval of the National Assembly is sought. (However, when this information is eventually published, the expenditure details of a number of important activities will be omitted.) Until now, the administrative breakdown of budget execution by each province has been available only after a long delay. The introduction of a new Chart of Accounts as from October 2009 should enable an approximate functional analysis of expenditure out-turns covering both central government and province/district levels for some of the main sectors. Meanwhile the requirement that all provinces should allocate at least minimum amounts to health and education services represents a first step toward the functional planning of expenditure. Dimension score: C.

PFMSP Efforts Underway: An upgraded Government Financial Information System (GFIS) is being implemented during the 2009–10 Fiscal Year along with revisions to the Chart of Accounts. The reporting capabilities of this system are designed to produce reports by functional classification through mapping existing administrative budget classification into an approximated function.

PI-6: Comprehensiveness of information included in budget documentation

Indicator	Brief explanation	Score
PI-6 Comprehensiveness of information included in budget documentation (Scoring method M1)	The budget documentation is stated to include full information on five of the Benchmarks specified by the PEFA Frameworks.	B

3.2.2 The assessment reviews how information in accordance with each benchmark is incorporated in the budget documentation.

1. *Macroeconomic assumptions,* including *at least estimates of aggregate growth, inflation, and exchange rat*e.

   Information about the outlook for growth, inflation, and the exchange rate is presented alongside the budget. (Satisfied)

2. *Fiscal deficit, defined according to Government Financial Statistics* (*GFS) or other internationally recognized standard.*

   This information is provided. (Satisfied)

3. *Deficit financing*

   The budget includes information about gross new external and domestic borrowing as well as information about interest payments and capital repayments. (Satisfied)

4. *Debt stock*

   It does not appear that information is given about the totals of outstanding domestic and external public debts, including the amounts of capital repayments and interest due during the budget year. (Not satisfied)

5. *Financial assets, including at least details for the beginning of the current year*

   It does not appear that information is published with the budget about the stock of financial assets held by the government. (Not satisfied)

6. *Prior year's budget out-turn, presented in the same format as the budget proposal*

This information is provided. (Satisfied)

7. *Current year's budget* (either the revised budget or the estimated out-turn) presented in the same format as the budget proposal.

   Information is provided only about actual budget execution during the first eight months of the financial year. Estimated out-turn for the year as a whole is not provided. (Not satisfied)

8. *Summarized budget data* for both revenue and expenditure according to the main heads of the classifications used, including data for the current and previous year.

   Aggregate information is provided showing the comparison of the proposed budget with the estimated and actual out-turns for the current and previous years. (Satisfied)

9. *Explanation of budget implications* of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/or some major changes to expenditure programs.

   It does not appear that specific information is given about the revenue impact of changes in taxation (for example, the introduction of VAT as from January 2010) or about the expenditure impact of new policies in the area of public services. (Not satisfied)

PI-7: Extent of unreported government operations

Indicator	Brief explanation	Score
PI-7 Extent of unreported government operations (Scoring method M1)	(i) Except for the Road Maintenance and Forestry Development Funds, whose revenues and expenditures are included in the budget, revenue and expenditure of the extra-budgetary funds (other than payments to them included in the budget) are neither reported to the National Assembly nor published. Revenue from charges for the delivery of public services, and the associated expenditure are neither reported nor published. Such expenditure could be of the order of 5 percent–10 percent of reported budgetary expenditure. In 2008–09 expenditure amounting to 2.7 percent of GDP (more than one-eighth of budgeted expenditure) was financed outside the budget through the Bond issuance. Dimension score: D. (ii) In principle, complete information is included in fiscal reports about expenditure on loan-financed projects, although there may be some inconsistencies in the data. Most expenditure on grant-funded projects is covered as well. Dimension score: B.	D+

(i) The level of extra-budgetary expenditure not included in fiscal reports

3.2.3 Significant expenditure takes place outside the budget through the eight extra-budgetary funds. Most of these funds receive money from the budget each year, but they may have additional revenue sources and/or income from charges. Road Maintenance Fund and Forest Development Fund operations are included in the budget and in reporting on the budget performance. Road Maintenance Fund revenues are included in the overall figures for tax revenue. In addition, there has been a more detailed publication of the income and expenditure of the Road Maintenance Fund for each year since 2001–02. However, no reports of the operations of these funds have been published.

3.2.4 In addition to these explicitly extrabudgetary operations, there are various charges made for the delivery of public services, notably for education and health. According to the Ministry of Health, approximately two-thirds of the total costs of hospital and other health services are met by charges for services or drugs. The 2006 World Bank Public Expenditure Tracking Survey (PETS) found that most schools charge registration fees. Extrapolating from this information, total expenditure on health and education services financed from charges might correspond to 5 percent–10 percent of aggregate reported expenditure. Neither the revenue nor the expenditure is shown in the budget. Furthermore, contrary to Article 6 of the Budget Law, the revenue has been kept in cash and in accounts outside the Treasury system. This omission was the subject of criticism in the SAO report on FY2007–08 budget execution, which was publicly endorsed by the NA. In addition to this longstanding issue, a new problem arose in 2008–09 as a result of the nontransparent financing of substantial expenditure (on the order of 2.7 percent of GDP, or approximately 14 percent of budget expenditure) by means of bonds issued through the Central Bank, mainly regarding the provision of facilities for the December 2009 SE Asian Games. Furthermore, it appears that there also has been some bank-financed expenditure in the provinces that similarly was excluded from the normal budgetary process. Dimension score: D.

(ii) Extent of inclusion of information on donor-funded projects included in fiscal reports

3.2.5 External finance, grants, and loans together account for approximately 25 percent of total expenditure and thus are of prime importance for the Lao PDR budget. These payments are tracked by the MoF External Finance Department, although there may be some inconsistencies in the data. Before FY09–10, grants that were managed by donors without MoF involvement—but engaging government units in the center and provinces directly—were not incorporated in the budget and fiscal reporting. Donors, however, reported disbursement of these grants to MPI through a foreign aid reporting system. Since FY09–10, these grants have been included in the budget and fiscal reporting. MPI claims that its reporting system can now capture 97 percent of all official direct assistance (ODA) to Lao PDR. Domestic grants and donations are not part of the budget and accountability arrangement. Because some grant-funded expenditure is not included in the budget or reports, Dimension score: B.

PI-8: Transparency of intergovernmental fiscal relations

Indicator	Brief explanation	Score
PI-8 transparency of inter-government fiscal relations (Scoring method	(i) The allocation of spending power to provinces and districts (grants plus revenue share) is not based on transparent rules. (D) (ii) Provinces’ (and districts’) budget proposals are submitted to MoF in	D

M2)	the same timetable as ministries,' but as in the case of the line ministries the actual budgets eventually fixed by MoF may differ considerably from these proposals (see PI-11 below). (D) (iii) No reports have been made showing the sectoral/functional breakdown of aggregate central and provincial government expenditure. (D)	

(i) Transparency of the allocation of resources to provinces and districts

3.2.6 In Lao PDR the yields of certain taxes (personal income tax, land tax) are assigned 100 percent to the provinces from which they are collected. The yields of some other taxes are assigned to the center. The yields of yet other taxes are shared between center and provinces. Hitherto, the receipts of each province have reflected its actual tax collection. However, now that authority over tax collection is being recentralized, each province's share is intended to be determined by a formula related to population, area, and relative poverty. A draft decree on this was prepared in 2008, but it has not yet been approved by the Prime Minister. Nonetheless, even when this formula is put into effect, the resources available to provinces will not be sufficient to meet their needs. Thus, as it has done prior, the central government will need to continue to provide additional grant finance to enable provinces and districts to maintain their services. The amounts of such grants have been set through negotiation between MoF and each province, with no explicit criteria. The result is wide disparities among provinces in expenditure on different services. In 2008–09 the government insisted for the first time on a minimum allocation by each province for health and education. The need to find a basis for allocating total spending power, rather than just the yield of certain taxes, to the provinces has not yet been addressed. Dimension score: D.

(ii) Timeliness of reliable information to lower-tier governments on their available resources

3.2.7 The arrangements for the preparation of the budget provide for provinces to receive information from MoF about the parameters within which they should prepare their submissions, in the same way that central ministries receive such parameters. However, just as in the case of the line ministries, the provincial budgets eventually fixed by MoF do not bear much relation to the parameters. Dimension score: D.

(iii)Extent of consolidation of fiscal data for general government according to sectoral categories

3.2.8 No comprehensive data have been produced on the functional/sectoral allocation of aggregate general government expenditure. The introduction of a new COA in October 2009 should eventually make possible an approximate functional/sectoral reporting. Dimension score: D.

PFMSP Efforts Underway: To implement Budget Law requirements, efforts are underway to develop budget norms that clarify the allocation of funds for the health and educations sectors. Additionally, with the implementation of GFIS, improved data on the actual sectoral/functional breakdown of expenditure at the provincial as well as central level should become available.

PI-9: Oversight of aggregate fiscal risk from other public sector entities

Indicator	Brief explanation	Score
PI-9 Oversight of aggregate fiscal risk from other public sector entities (Scoring method M1)	(i) State-owned enterprises (SOEs) make quarterly reports to MoF's SOE Financial Management Department on their financial performance, but no consolidated report is produced. External borrowing is effectively controlled by MoF. (C) (ii) Provinces and districts are required to balance their budgets and have no power to borrow independently outside the government. However, there are indications that they have in effect been borrowing from contractors and suppliers. (D)	D+

(i) Extent of central government monitoring of autonomous government agencies and state owned enterprises

3.2.9 As noted, most economic activity in the Lao PDR is in the private sector, with SOEs largely, but not wholly, confined to the utilities sector, and probably accounting for less than 5 percent of overall economic activity. SOEs make quarterly returns on their financial position to the SOE Financial Management Department at MoF, which acts as a rather passive shareholder. In other respects, they remain under the management of the ministry that covers their activities. Directors are appointed jointly by MoF and the ministry concerned. Accounts are submitted to MoF Tax Department in a form specified by that department, which assesses SOE tax liabilities. These accounts do not conform to International Financial Reporting Standards (IFRS) and are not published. SOEs are not required to meet published financial or other targets. MoF aims to collect 60 percent of post-tax profits as dividends without regard to the investment needs or profit opportunities of the SOE in question. The Business Promotion Office under the Prime Minister has responsibility for securing the rationalization of loss-making SOEs, adding to the complexity of coordinating government policy toward SOEs. External borrowing is effectively controlled by MoF and, in any event, would be possible for only a very few major enterprises. It appears that some SOEs borrow, without an explicit government guarantee, from both state-owned and other commercial banks. This practice could present some risk to the government if the loans became nonperforming, and some recapitalization of the banks became necessary. The dimension score reflects this point as well as the absence of a clear government policy to improve SOE financial performance to make it transparent to external investors. Dimension score: (C).

(ii) Extent of central government monitoring of lower-tier governments' fiscal positions

3.2.10 Provinces and districts are required to balance their budgets and have no power to give guarantees regarding borrowing by enterprises in their areas. Nevertheless, there is evidence that provinces have been in the habit of financing capital projects by relying on prefinancing by contractors (with the provinces guaranteeing bank lending to the contractors). This practice is, in effect, a form of uncontrolled borrowing. Payment arrears for public utilities, including electricity, water, and telephone, add to this implicit financing but are not reflected in government accounts prepared on cash basis. Special arrangements have been made to establish the amounts of outstanding utility arrears and to provide for them to be paid off by the end of FY2010–11. There also are indications that some provincial expenditure has been financed outside the budgetary process by the Central Bank, despite the prohibition on borrowing by lower-tier governments. Score for this Dimension: D

PI-10: Public access to key fiscal information

Indicator	Brief explanation	Score
PI-10 Public access to key fiscal information (Scoring method M1)	General public has full access to information covering 1 of the 6 PEFA benchmarks.	C

3.2.11 Six elements of information to which the public should have access are considered:

(i) Annual budget documentation (as in PI 6):

Much of the budget documentation presented to the NA is inaccessible to the general public. (Benchmark not satisfied)

(ii) In-year budget execution reports.

There is no publication of in-year budget execution reports. (Benchmark not satisfied)

(iii) Year-end financial statements.

Financial statements concerning budget execution are published within six months of completed audit. (Benchmark satisfied)

(iv) External audit reports.

No reports by the State Audit Organization (SAO) have been published, although some elements of the annual reports on budget execution have been disclosed in the course of discussions in the National Assembly. (Benchmark not satisfied)

(v) Contract awards.

There so far has been no publication of the awards of contracts. (Benchmark not satisfied)

(vi) Resources available to primary service units.

Information is not available about the budgets provided to primary service units and costs of operating particular hospitals, clinics or schools. (Benchmark not satisfied)

PFMSP Efforts Underway: These issues are being addressed by a number of PFM-strengthening measures:

- GFIS should improve the reliability of producing in-year budget execution reports, but policy decisions must be made to publish them.
- Support for the State Audit Organization includes commitments to publish the audit report of the final account of the state budget and possibly others.
- The newly established procurement website is intended to provide information on actual procurements, which will address element (vi).
- The GFIS should provide improved, ex-post information on resources to at least some service-delivery units.

3.3 Budget Cycle

C (i) Policy-based budgeting

PI-11: Orderliness and participation in the annual budget process

Indicator	Brief explanation	Score
PI-11 Orderliness and participation in the annual budget process (Scoring method M2)	(i) An annual budget calendar exists, at least by custom and practice, although the requirements of the Budget Law have not been followed. Although spending agencies have generally had time to prepare budget submissions, it is not clear that they all have been able to satisfactorily complete their submissions. (C) (ii) There probably is sufficient political understanding across government about the sustainable level of aggregate expenditure. Nevertheless, this understanding has not translated into realistic ceilings for each agency under which it could plan how best to use the prospective provision. (D) (iii) For each of the last three financial years, the NA has approved the following year's budget before the start of the year. (A)	C+

3.3.1 Given the main responsibility of MoF in the annual budget formulation process, this Indicator seeks to assess whether the political leadership (the Cabinet) and the ministries and provinces participate effectively in the process that determines macroeconomic, fiscal, and sectoral policies.

(i) Budget calendar

3.3.2 The Budget Law sets out a calendar, which generally has not been followed rigorously. Although ministries and provinces have generally had at least 4 weeks to prepare their budget submissions, it is not clear that all were able to complete their submissions in time. Dimension score: C.

(ii) Priority setting and political foundation for instructions in the Budget Circular

3.3.3 The general shape of the budget and the macroeconomic assumptions to be used in determining aggregate expenditure are set by collective government decisions at the beginning of the process. There are additional consultations with Ministers and provincial Governors before budget submissions are prepared. However, although there may be a general political understanding of the real circumstances underlying the budget, no expenditure ceilings were issued to guide the preparation of the budget submissions. Moreover, the standard cost norms that are supposed to be used in the submissions have not provided an appropriate basis for discussions between MoF and spending agencies. The reason is that, in the latter's view, applying the standard cost norms would require total expenditure far beyond the amounts they could realistically expect. Dimension score: D.

(iii) Timely budget approval by the Parliament

3.3.4 In each of the last three years the NA has approved the budget well in advance of the beginning of the year to which it relates. Dimension score: A.

PI-12: Multiyear perspective in fiscal planning, expenditure policy, and budgeting

Indicator	Brief explanation	Score
PI-12 Multiyear perspective in fiscal planning, expenditure policy, and budgeting (Scoring method M2)	(i) No forward estimates of fiscal aggregates have been prepared in the context of formulating each successive year's annual budget. (D) (ii) Debt sustainability analysis has been undertaken annually, the lead being taken by the IMF/World Bank. (A) (iii) No strategies yet have been prepared for the medium-term development of any of the main public services. (D) (iv) Budgeting for investment and recurrent expenditure are separate processes. There are no arrangements for considering the future recurrent costs of maintaining and operating the assets/facilities created as a result of decisions on specific investments. (D)	D+

3.3.5 The question addressed by this Indicator is (a) whether effective and sufficiently detailed medium-term plans are made to make best use of available resources in the development of the economy and the provision of public services and (b) whether these plans actually guide the annual budget ceilings and allocations.

(i) Multiyear projections of revenue and expenditure

3.3.6 Work is ongoing and supported by ADB via the Public Sector Management Strengthening Program (PFMSP) to prepare a medium-term fiscal framework. Although Article 27 of the 2006 Budget Law requires the National Assembly to adopt medium- and long-term fiscal plans as well as annual budgets, this law has not yet been taken into account in the preparation of the annual budget proposals. Furthermore, no multiyear forecast has been presented to the NA with the annual budget, as required by the Budget Law. Dimension score: D.

(ii) Scope and frequency of Debt Sustainability Analysis (DSA)

3.3.7 The External Finance Department of MoF has participated in the annual reviews of debt sustainability undertaken by the IMF and World Bank in the context of Article IV consultations. Given the need not to increase the future burden of debt service in relation to either GDP or aggregate budget revenue, the conclusions are used to determine the ceiling amounts of new MoF external borrowing each year. According to the latest DSA, the current domestic public debt is small and comprises mainly Treasury bills and bank recapitalization bonds. At end-2008, the stock of recorded domestic public debt amounted to 2.1 percent of GDP. Therefore, in this context, domestic debt is negligible. Dimension score: A.

(iii) Sector strategies and multiyear costing of recurrent and investment expenditure

3.3.8 The government recently sought to require at least minimum levels of expenditure per head of population across the country on the provision of health and education services. However, there has been no overall central control over provinces' expenditure priorities and no accessible information about the functional allocation of general government expenditure. Although some steps have been taken to develop sectoral strategies for health and education, this elaboration has not been done within an overall medium-term resource framework with preset overall allocations for each main service. Some overall guidance may be obtained from the National Social and Economic Development Plan 2006–10. However, the plan does not fix precise targets and timetables for the improvements intended for different areas. Dimension score: D.

(iv) Linkages between investment budgets and forward expenditure estimates

3.3.9 Given the volume of domestic resources that MoF considers can be made available for investment, and the amount of new external borrowing that can be undertaken within the constraints of debt sustainability, it is the responsibility of the Ministry of Planning and Investment (MPI) to select the projects to be initiated each year. There is as yet no established medium-term fiscal framework and nor any consistent articulated plans for the development over time of the main public services. As a result, no systematic consideration so far has been given to the ongoing recurrent costs of maintaining and operating the assets/facilities resulting from MPI's selection of investment projects. This lack persists despite the provisions of the Budget Law that require budgets to be planned within a medium-term framework. Dimension score: D.

PFMSP Efforts Underway: As mentioned above, an ADB-sponsored project has been improving the central capacity for the development of medium-term expenditure forecasts at the sectoral level. This development recently was expanded to facilitate a comprehensive medium-term expenditure framework (MTEF) to accompany the budget.

C (II). PREDICTABILITY AND CONTROL IN BUDGET EXECUTION

PI-13: Transparency of taxpayer obligations and liabilities

Indicator	Brief explanation	Score
PI-13 Transparency of taxpayer obligations and liabilities (Scoring method M2)	1. Tax legislation lacks precision in some areas and is not in line with international accounting and reporting standards. Significant discretionary exemptions are given, which may distort competition among taxpayers. (C) 2. Some efforts are made to provide taxpayers with appropriate information, but it is not always user friendly, and the Tax and Customs Departments' websites are not yet operational. (C) 3. Although there are administrative procedures within the Tax Department for taxpayers to question their tax assessments, the last word remains with the authorities. No dedicated independent appeals mechanism has been established, and there is very limited national experience of appeals to the courts, and then, only in the case of customs duties. (D)	D+

(i) Clarity and comprehensiveness of tax liabilities

3.3.10 Lao PDR does not yet have a fully developed market economy nor an established tradition of an independent court system arbitrating on occasion between the citizen and the authorities. Total tax receipts are less than 12 percent of GDP (other countries in the region collect 18 percent–20 percent of GDP or more). Relatively few enterprises are large enough to be fully liable to profits and turnover taxes, and now, VAT.[7] Small and medium enterprises (SMEs) with some form of accounting system may pay a "minimum" (turnover) tax in place of profits tax (but in addition to the normal turnover tax). The smallest enterprises pay a lump sum tax in place of both profits and turnover taxes. These arrangements inevitably give rise to a situation in which the provincial tax collector (who hitherto has been under the control of the provincial governor, not the central Tax Department) negotiates the amount of tax to be paid. The central government may also exercise discretion to give exemption or partial exemption from customs duties and/or profits tax as inducements to new investments. These informal, improvisational arrangements can create inequities among different taxpayers. Dimension score: C.

(ii) Taxpayers' access to information on tax liabilities and administrative procedures

3.3.11 The Tax Department takes some steps to disseminate information and runs media campaigns to inform the public of tax changes. A substantial campaign was run in preparation

[7] VAT's rules are reasonably clear, although in some cases doubtfully consistent with international accounting and reporting standards because of restrictions on what may be set against gross revenues in arriving at taxable profits.

for the introduction of VAT in January 2010. The results of this campaign were not yet clear as of March 2010. Despite these efforts, taxpayers may face difficulty in obtaining consistent information on particular points. Furthermore, the country has no tradition of consultation with taxpayers about the operation of different taxes. The Tax and Customs Departments' public information websites are still under development. Dimension score: C.

(iii) Existence and functioning of a tax-appeal mechanism

3.3.12 Apart from customs duties, there are no specific provisions for appeals to any authority outside the tax administration system. There was one recent customs appeal to the People's Supreme Court. Dimension score: D.

PI-14: Effectiveness of measures for taxpayer registration and tax assessment

Indicator	Brief explanation	Score
PI-14 Effectiveness of taxpayer registration and tax assessment (Scoring method M2)	(i) Separate registration systems are maintained in each province and have no links among them. In the context of the introduction of VAT in January 2010, a start has been made toward the introduction of a unique Taxpayer Identification Number (TIN). The same TIN also will apply to customs duties. However, it is likely to take some years before the TIN is applicable to all taxes throughout the country. Businesses cannot operate bank accounts until business, enterprise, and tax registration obligations have been fulfilled. (C) (ii) The Tax Department states that it is difficult to enforce registration and declaration obligations against small taxpayers, so the department is obliged to devote much effort to the supervision of these obligations. On the other hand, the department is able to impose fines and penalties on delinquent taxpayers and thus has a degree of coercive power. Recorded arrears apparently are relatively low. Given the country's long and porous land borders, the Customs Department has difficulty in enforcing revenue collection. However, once duties have been assessed, payment must be made before goods are released. (B) (iii) Tax audits were stated by the Tax Department to be planned taking account of risk factors (including previous noncompliance), although some audits are based on random selection of taxpayers. Few Customs Department staff are engaged in audit work. The focus of those who are is checking the consistency of documentation rather than examining the substance of transactions. (D)	C

3.3.13 This Indicator seeks to assess the functioning of the tax system from the standpoint of the authorities. What is sought is whether the authorities are well informed about the identity and character of taxpayers, whether the former are able to enforce compliance with obligations, and whether the authorities have effective arrangements for countering tax fraud. To a considerable extent, the relatively favorable picture of tax assessment and enforcement given by PIs-14 and -15 may reflect the imprecision concerning the definition of tax liabilities and the scope for negotiation between taxpayers and tax collectors. Moreover, the performance target for a tax office may be to collect X percent more revenue than last year rather than to collect a very high proportion of correctly assessed taxes due. Total tax revenue in Lao PDR as a percentage of GDP (approximately 12 percent) is low both absolutely and in comparison with other countries in the region.

(i) Controls in the taxpayer registration system

3.3.14 At present, separate registration systems operate for different taxes, and there are no links between the registers at the center and in the provinces. As noted above, the unique TIN, together with necessary communication links, was created for the purposes of VAT. However, VAT applies only to a small number of relatively large taxpayers and collection is relatively centralized. It is likely to take several years before the IT infrastructure is in place to support unique TINs for each taxpayer applicable to all taxes countrywide. Meanwhile, the fact that regulations prohibit the operation of bank accounts until businesses have complied with all business, enterprise, and tax registration obligations serves as an essential link between tax and other registration systems. Dimension score: C.

(ii) Effectiveness of penalties for noncompliance with registration and declaration obligations

3.3.15 The Tax Department considers enforcement of registration and declaration obligations to be difficult. This enforcement absorbs a large portion of available staff effort. (The roughly 1,336 total staff of the department is relatively a large number in relation to the 85,000 registered taxpayers.) However, these staff do have coercive powers to fine delinquent taxpayers, who may prefer to comply with tax collectors' demands to avoid having a bad tax record or facing further investigation. Dimension score: B.

(iii) Planning and monitoring tax audit programs

3.3.16 Only 10 percent of Tax Department staff were said to be engaged in tax audit. Some taxpayers were selected for audit on the basis of risk factors, including previous delinquency; others were selected at random. Only 5 percent of Customs Department staff were stated to be auditing customs declarations; and, as noted above, they are focused on the consistency of documentation rather than on the substance of the transactions. It appears that there is much scope for making tax audit more systematic, and coordinated between the two departments, at least in the case of large taxpayers. Now that VAT has replaced turnover tax for large taxpayers, a review of the most effective use of staff could prove useful. Dimension score: D.

PFMSP Efforts Underway: As mentioned, efforts are underway to develop a revised and properly structured taxpayer identification number (TIN). Additionally, with the introduction of the VAT in 2010, new taxpayer modules are being developed to register and capture the tax liabilities of VAT taxpayers and match these liabilities with the payments made by each taxpayer.

PI-15: Effectiveness in collection of tax payments

Indicator	Brief explanation	Score
PI-15 Effectiveness in collection of tax payments (Scoring method M1)	(i) Over the last 3 years, tax arrears at year end have not exceeded approximately 1.25 percent of tax collected during the year. The Customs Department states that there are no arrears because tax must be paid before goods are released into circulation. On the other hand, the definition of arrears is very limited due to lack of clear assessments. (Not Rated, or NR) (ii) All tax revenue is paid directly into Treasury accounts, although revenue collected in the provinces is remitted to the center only every two weeks. (A) (iii) There is full monthly reconciliation between Tax Department records of receipts and Treasury bank records. The Tax Department tracks actual payments against assessments on a running basis to chase late payers toward the end of the financial year. (C)	NR

(i) Collection ratio for gross tax arrears

3.3.17 According to MoF's Tax Department, tax arrears at the end of 2005–06 amounted to 22.5bn KIP, compared with the year's tax receipts of 1,795.1bn KIP. The corresponding figures for the next 2 years were arrears of 28.75bn KIP and 40.27bn KIP, compared with total receipts of 2,584.1bn KIP and 3,190.1bn KIP, respectively. Tax arrears at year-end thus amounted to 1.25 percent, 1.11 percent, and 1.26 percent of annual receipts for the 3 successive years. However, given the absence of clear assessments to be used in calculating them, the definition of arrears is very limited. Customs stated that there were no arrears of assessed duties because payment must be made before goods are released into circulation. Dimension score: Not Rated (NR) due to the absence of satisfactory information about assessments against which arrears can be measured.

(ii) Immediate transfer of tax collections to the Treasury

3.3.18 Under arrangements recently introduced, all tax revenue is paid immediately into Treasury accounts at the BOL in Vientiane and into commercial banks in the provinces. Amounts collected in the provinces are remitted to the center every two weeks. Dimension score: A.

(iii) Frequency of accounts reconciliation among tax assessments, collections, arrears, and transfers to the Treasury

3.3.19 The Tax Department states that there are (a) daily reconciliations of their records of revenue collected at the center with Treasury bank account records at BOL and (b) complete monthly reconciliation of records of taxes collected throughout the country with bank account records. Reconciliations between assessments and payments are undertaken by the Tax Department toward the end of each year to pursue late payers. Dimension score: C.

PFMSP Efforts Underway: The National Treasury is in the early stages of developing a Treasury Single Account (TSA). This single account should facilitate the daily consolidation of tax receipts (even at the provincial level) to support nation-wide expenditure requirements.

PI-16: Predictability in the availability of funds for commitment of expenditures

Indicator	Brief explanation	Score
PI-16 Predictability in availability of funds for commitment of expenditures (Scoring method M1)	(i) Once budgetary provision for the year has been determined, the Budget Department, in consultation with the Treasury, sets cash ceilings for each budget line for the two subsequent quarters. These ceilings are updated quarterly. (B) (ii) Since FY 2009–10, ministries and provinces have not experienced problems in making payments, so long as they remained within the cash ceilings set by MoF for the coming six months. (A) (iii) A major revision of the budget may be made only once a year and requires NA approval. Under the Budget Law, ministers can reallocate expenditure from one line to another within the same chapter of their budgets. However, reallocation among chapters requires the approval of the Minister of Finance. Reallocation among ministries or provinces requires the approval of the Prime Minister. Reallocations are not published. (B)	B+

(i) Extent to which cash flows are forecast and monitored

3.3.20 Once the detailed budget has been approved, the Budget Department, in consultation with the Treasury, sets ceilings for expenditure on each budget line for the next two quarters. The ceilings are updated quarterly. Dimension score: B.

(ii) Reliability and time horizon of information to spending authorities on cash availability

3.3.21 In recent years, spending authorities have not experienced difficulties with the availability of cash to meet payments falling due so long as the payments remained within quarterly ceilings. Since FY09–10, the Budget Department has provided a measure of assurance of cash availability covering the six months immediately ahead. Dimension score: A.

(iii) Frequency and transparency of adjustments to budget allocations notified to spending authorities

3.3.22 The Budget Law (Article 65) gives ministers the authority to reallocate funds from one budget line to another within the same chapter. Reallocation among chapters requires the authority of the Minister of Finance, whereas reallocation among ministries or provinces can be done only with the approval of the Prime Minister. Only one major revision may be made to the budget each year, and the revision requires the approval of the National Assembly. Lao PDR has experienced no recent significant changes being imposed on ministries'/provinces' budgets by the GOL or the Minister of Finance. Although made in an orderly manner, reallocations are not published, which diminishes their transparency. Dimension score: B.

PFMSP Efforts Underway: The TSA efforts mentioned under PI-15 should also further strengthen the ability of the national Treasury to have available the cash to support expenditures when needed.

PI-17: Recording and managing cash balance, debt, and guarantees

Indicator	Brief explanation	Score
PI-17 Recording and managing cash balances, debt, and guarantees (Scoring method M2)	(i) Domestic and external public debt data are complete and reasonably reliable, but discrepancies can arise because of exchange rate fluctuations. Internal reporting is ad hoc. (Information is published annually only by the IMF following Article IV consultations.) (C) (ii) Although the MoF has prepared a plan to consolidate separate bank accounts into a Treasury Single Account (TSA), numerous accounts remain open with commercial banks. An inventory of these bank accounts has been conducted, and action is expected to begin in second half of 2010 to close these accounts and consolidate the balances in the TSA. (D) (iii)MoF's External Finance Department ensures that external loans are contracted within preset annual ceilings and meet preset criteria for their terms. Domestic borrowing is managed by the Treasury to ensure cash availability Nevertheless, there has been uncontrolled issuing of guarantees for domestic borrowing by provinces. (D)	D+

(i) Quality of debt data recording and reporting

3.3.23 External loans are managed by MoF's External Finance Department, which keeps track of loan draw-downs, capital repayments, and interest payments. Data problems can arise as a result of changes in exchange rates between the US$ (in which currency accounts are kept) and other currencies in which some Lao PDR debts are denominated. Overall debt data are consolidated by the Fiscal Policy Department. The Treasury is responsible for domestic borrowing, usually undertaken to ensure cash availability. The PFMSP includes a plan to install an improved debt management system (DMFAS) in the near future, for which the contractual arrangements were recently finalized. Previously, publication of debt data was undertaken only by the IMF in the context of the annual Article IV consultations. Dimension score: C.

(ii) Extent of consolidation of government cash balances

3.3.24 The central Treasury recently was put in control of all provincial and district Treasury employees. Nevertheless, there are many government accounts in commercial banks controlled by ministries and spending units outside the purview of the national Treasury. At the level of individual spending units, expenditures may be financed directly from revenues collected in cash, which never reach any bank account. An inventory of all government bank accounts has been conducted by commercial banks under the supervision of the Bank of Lao in preparation for creating the TSA, into which all of these accounts will be consolidated. Dimension score: D.

(iii) Systems for contracting loans and issuing guarantees

3.3.25 The External Finance Department manages the contracting of external loans (including loans to SOEs for which a government guarantee is given) in accordance with criteria for limits on total borrowing and the related terms. These in turn reflect the requirements of debt sustainability. Thus, total new borrowing should not exceed $300m a year, and the interest rate should not exceed 2 percent. (Profitable SOEs would be allowed to borrow externally for investments whose internal rate of return was higher than 12 percent, so long as there was a guaranteed income stream to service the loan.) Domestic borrowing is managed by the Treasury, while Fiscal Policy Department consolidates overall debt statistics. However, in response to the recession and the facilities requirements of the South East Asian Games in December 2009, BOL undertook substantial borrowing outside the normal framework through bond issues (in both KIP and US$). This borrowing totaled approximately 14 percent of current total budget expenditure. The associated expenditure was not included in the budget. Moreover, provinces have been financing investments by guaranteeing borrowing by contractors with the costs of the investments repaid over a period, in some cases through the land concessions. This practice of giving guarantees does not appear to be under clear control, and these investments have not been included in the budget. (Unguaranteed borrowing by SOEs is discussed under PI-9 above.) Dimension score: D.

PFMSP Efforts Underway: MoF's External Finance Department will be installing UNCTAD's Debt Management and Financial Analysis System during the 2010, which should improve dimension (i) of this performance indicator (PI). In addition, the previously mentioned TSA effort is completing a review of the inventory of government bank accounts and determining which are, or are not, proper to consolidate into the TSA. Procedures for operating the TSA have been drafted, so more progress on element (ii) should be anticipated in the near term.

PI-18: Effectiveness of payroll controls

Indicator	Brief explanation	Score
PI-18 Effective-ness of payroll controls (Scoring method M1)	(i) The Public Administration and Civil Service Authority (PACSA) keeps a central database of all public servants (including those working in health and education, but excluding police and armed forces). MoF has a database of the payroll in each ministry/province (police and armed forces again excluded). Twice annually (Quarters 2 and 4), PACSA gives a fresh authorization of approved staff numbers, grades, and incremental steps for each ministry/province payroll and notifies recorded changes to these authorizations. The actual payroll payments by MoF must be consistent with these authorizations. PACSA also controls benefits and entitlements, terminations, and transfers. Rating, reflecting the partial nature of this reconciliation: C. (ii) Personnel change decisions are approved by PACSA twice annually: in Quarters 2 and 4. Processing for the changes can be done at the line ministry level in Quarters 1 and 3. However, changes to the payroll record cannot be made until Quarters 2 and 4, when PACSA approves them. Given that the entitlement is effective from the date of change processed at the line ministry level, this practice results in frequent retroactive payments. (C) (iii) Responsibilities for changes to personnel and payroll records are clear, and there are both separation of functions and firm hierarchical supervision. The	C+

	requirement for central notification of promotions ensures an audit trail. (A) (iv) The State Audit Organization (SAO) has not yet carried out any directed payroll audits, but in the past, PACSA has arranged for censuses involving physical verification of all civil employees and, in 2007, for partial inspections covering education and health sectors. (C)	

3.3.26 The numbers, pay, and grading of civil servants and other government employees are tightly controlled by PACSA in respect to numbers of new hires and the grading of individual employees. The MoF controls pay scales and the detailed monthly payroll allocations to each ministry/province based on precise calculations of numbers and grades. However, there is one striking omission. The police and armed forces, who could account for 25 percent of the total government payroll, are excluded from these arrangements, and no information is available about any aspect of this large area of expenditure.

(i) Linkages between personnel records and payroll operations

3.3.27 PACSA keeps records of each public servant (including those employed in health and education services). PACSA must be notified of every individual promotion, salary advancement, change in benefits and entitlement, termination, and transfer. (The only exceptions are small numbers of contract staff, who account for less than 2 percent of the payroll.) MoF fixes pay scales and keeps a detailed database of the payroll of each ministry/province, taking into account limits on new hiring set by PACSA.

3.3.28 PACSA issues instructions twice a year on aggregate staff numbers, grading, and incremental steps , with which the provinces must comply in operating the payroll. Thus, there is an aggregate reconciliation between the payroll and personnel records. PACSA is piloting the development of an electronic personnel database in which all the elements determining an individual's pay would be recorded. MoF's database eventually could be automatically linked to this database. Given that ministries/provinces have no discretion over the amounts of increments or allowances, such a system could eventually determine the amounts of payments to each individual. Dimension score: C.

(ii) Timely updating of personnel and payroll databases

3.3.29 There are two times in the year that personnel changes decisions are approved by PACSA: the second and the fourth quarters. Processing for the changes can be done at the line ministry level in the first and third quarters. However, changes to the payroll record cannot be made except in the second and four quarters, when PACSA approves them. Given that the entitlement is effective from the date of change processed at the line ministry level, the current practice results in frequent retroactive payments. Dimension score: C.

(iii) Internal controls of changes to personnel records and payroll

3.3.30 The requirement for central notification for all promotions, salary advancements, benefit changes, and terminations serves to ensure the existence of an audit trail whenever changes are made in personnel and payroll records. Hierarchical supervision of changes to both personnel and payroll records is strong. The facts that the recent study team on Pay and Compensation was able to inspect detailed records of the make-up of individuals' total compensation and that PACSA must notify MoF of authorized payroll amounts demonstrate that actual payments do conform to the rules and that there is an audit trail. Dimension score: A.

(iv) Effective operation of payroll audits

3.3.31 In the past, PACSA has arranged complete censuses of civilian government employees that have identified instances of ghost workers. Some testing of this kind was done in 2007 in the health and education sectors. This testing found cases of salaries still being drawn for teachers who had left their posts. PACSA is planning an additional full census in 2010. Dimension score: C.

PI-19: Competition, value for money, and controls in procurement

Indicator	Brief explanation	Score
PI-19 Competition, value for money and controls in procurement (Scoring method M2)	(i) No data are yet available to assess the extent to which open competition is used to award public contracts. (D) (ii) The applicable legislation provides for the use of less competitive methods in defined circumstances, but the evidence is incomplete that the rules for less competitive methods are applied correctly. (C) (iii)No independent mechanism has been established to deal with complaints about the way in which contracts are let. (D)	D+

3.3.32 The applicable legislation is the Prime Minister's Decree of 9 January 2004 and the Implementing Rules promulgated by MoF on 12 March 2004 (IRR 063/MOF). These two are supplemented by the MoF Charter 2382/MOF of 4 November 2004, which defines the functions of the MoF Procurement Monitoring Office (PrMO). Except for the absence of any independent mechanism to deal with complaints, the legislation broadly meets the requirements for satisfactory procurement arrangements established by the Organisation for Economic Co-operation and Development (OECD) Development Assistance Committee (DAC). A Procurement Manual, which sets out how to apply the Lao PDR legislation, and standard bidding documents were issued in August 2009. These two pieces have formed the basis of a major training effort to improve Lao procurement practice. The training is ongoing. The rules apply to SOEs as well as to ministries/provinces.

(i) Use of open competition for the award of contracts above a threshold value

3.3.33 Notwithstanding the provisions of the PrMO Charter, no information yet has been collected about the use of different (and less competitive) procurement methods. It is intended that this information should be collected consistently from October 2009. Dimension score: D.

(ii) Justification for use of less competitive procurement methods

3.3.34 The legislation calls for documentation of the reasons for not letting contracts by open competition. Reviews have indicated that public authorities and SOEs generally establish some documentation to support their decisions not to procure by open competition. This documentation is archived by MoF State Assets Department. However, no comprehensive information yet has been collected. Thus, there is no overall assurance that these legal provisions are being respected. Dimension score: C.

(iii) Existence and operation of a procurement complaints mechanism

3.3.35 Although the absence of any arrangements to handle procurement complaints has been noted by successive reviews, no steps yet have been taken to deal with this problem. If the PrMO website is successfully established in the near future, and ministries/provinces make the required returns concerning their invitations to tender and award contracts, disappointed bidders will be able to access the information needed to support their possible complaints. However, the legislation does not provide for any independent mechanism to adjudicate such complaints. The only appeal to date is to the Chairman of the Tender Board. Dimension score: D.

PFMSP Efforts Underway: Efforts to strengthen procurement effectiveness have resulted in the creation of a website (procurement bulletin board) designed to provide both prospective information on planned procurements and the results of completed procurements. The Procurement Monitoring Office is training all budget entities in the use of this tool and providing standard documents and procedures. The office also has plans to require procurement performance assessments in all ministries. These assessments would improve the information on future actual procurement compliance.

PI-20: Effectiveness of internal controls for nonsalary expenditure

Indicator	Brief explanation	Score
PI-20 Effectiveness of internal controls for nonsalary expenditure (Scoring method M1)	(i) Lao PDR has not established any controls over expenditure commitments within the current budget year nor those potentially extending beyond the current budget year. Although the MPI's list of approved investment projects submitted to the NA alongside the budget shows the total cost of each project as well as the estimated spending in the year immediately ahead, MoF does not track or control these future obligations. (D) (ii) The Lao PDR system appears to rely more on the threat of compliance testing by inspection bodies (including the State Inspection Authority) than on controls to ensure that rules are obeyed. The only checks before payments are authorized are on the availability of budgetary provision and the prima facie validity of the invoices. (D) (iii) The rules for processing transactions by the Treasury are generally observed, and payment proposals that go beyond applicable cash ceilings (see PI-16) are automatically rejected. Budget rules may widely differ among provinces and districts. However, transactions involving funds that have escaped the Treasury net are not protected in the same way. (C)	D+

(i) Effectiveness of expenditure commitment controls

3.3.36 Although the MPI lists of approved investment projects submitted to the NA alongside the budget gives the total costs of each project as well as the expenditure in the year immediately ahead, these forward commitments are not the subject of any control by MoF. There are indications that, without central approval, provinces have undertaken commitments on investment projects in excess of the amounts available in the current year's budget. Such over-budget projects effectively preempt any domestic investment resources that might have been allocated to them in future years. (See for example the 2008 WB/DFID Case Study on pro-poor agricultural expenditures**.** Dimension score: D

(ii) *Comprehensiveness, relevance, and understanding of other internal control rules/procedures*

3.3.37 It appears that the emphasis in Lao PDR has been on the threat of ex-post compliance testing by the State Inspection Authority and Ministerial Inspection Departments rather than on arrangements to ensure that rules are complied with before payments are made. Thus, to date, no procedures exist to ensure that procurement rules have been observed before the Treasury authorizes payments to contractors or suppliers. Dimension score: D.

(iii) *Compliance with rules for processing and recording transactions*

3.3.38 Concerning payments by the Treasury, it appears that the rules for processing and recording transactions are correctly observed and that the system will automatically reject payment requests that go above the cash ceiling in force on the relevant budget line. The rules may differ slightly in provinces and districts, especially when making expenditure prioritization decisions facing shortage of funds. However, the same assurance does not apply to payments made from bank accounts still under the control of ministries or provinces. Dimension score: C.

PI-21: Effectiveness of internal audit

Indicator	Brief explanation	Score
PI-21 Effectiveness of internal audit (Scoring method M1)	(i) Internal audit does not exist as a separate function in Lao PDR. (D) (ii) No internal audit reports as such have been produced as there is no internal audit. (D) (iii) There being no internal audit reports, there has been no management response to audit findings as such. (D)	D

(i) *Coverage and quality of the internal audit function*

3.3.39 The concept of internal audit as a service to management with the function of identifying ways of correcting and improving systems to improve the efficiency, economy, and effectiveness of the delivery of public services does not exist within the GOL. To date, the Lao administrative culture has emphasized hierarchical control and the enforcement of compliance with rules and instructions. To date, no internal audit function exists as a separate function in Lao PDR. Dimension score: D.

(ii)   Frequency and distribution of reports

3.3.40 There being no internal audit function, there have been no internal audit reports as such. Dimension score: D.

(iii)   Extent of management response to internal audit findings

3.3.41 There being no internal audit reports, there has been no management response to audit findings as such. Dimension score: D.

PFMSP Efforts Underway: Under the sponsorship of the EC, a diagnostic assessment of the internal control and internal audit in the MoF has been undertaken by consultants. Progress in addressing the issues raised now depends on clarifying the institutional arrangement for performing internal audit functions and getting additional outside assistance to develop and implement an action plan for capacity improvements. However, whether internal audit should have a high priority at this stage has yet to be determined.

C (III). ACCOUNTING, RECORDING, AND REPORTING

PI-22: Timeliness and regularity of accounts reconciliation

Indicator	Brief explanation	Score
PI-22 Timeliness and regularity of accounts reconcilia-tion (Scoring method M2)	(i) All Treasury records of payment instructions and receipts are reconciled monthly with bank account records (at BOL at the center, and at commercial banks that hold the Treasury accounts in the provinces). There are no assurances of bank reconciliations for accounts outside Treasury control. (B) (ii) Amounts held by ministries/provinces outside Treasury bank accounts should be subject to regular in-year reconciliation and clearance procedures, as should advances for travel and subsistence. However, the National Assembly Resolution covering Budget Execution (see PI-28 below) takes up SAO criticisms of money advanced from the Treasury not being accounted for or returned to the Treasury account. Moreover, some cash receipts at the province and district level are used directly to finance expenditure without ever passing through any bank account. (D)	C

(i)   Regularity of bank reconciliations

3.3.42 Treasury departments in the center and provinces make regular reconciliations of bank balances and bank statements: with the Treasury Ledger daily and at the end of the month. District treasuries use bank accounts only for cash replenishment if a bank is present in the district. Although the Treasury records payments in the electronic Government Finance Information System (GFIS), payment instructions to BOL and other banks are produced outside that system. There are no assurances of bank reconciliations in the case of bank accounts managed by individual government units. Dimension score: B.

(ii) Regularity of reconciliation and clearance of suspense accounts and advances

3.3.43 It was understood that when the Treasury advances money to ministries/provinces to be held outside Treasury accounts, the administrative units concerned are required to account periodically for such funds. Similarly, individuals are required to account for their use of advances and to return any unspent balances. However, the National Assembly Resolution on FY2007–08 Budget Execution takes up criticism by the State Audit Office of cases in which money advanced by the Treasury had not been accounted for or repaid. Payments made at the province or district level out of cash receipts never paid into any bank account represent an additional source of risk and uncertainty. Releases from the Treasury are recorded in the expenditure accounts by the stated purpose of the release without making adjustments to the expenditure account after acquittal of the advance, even if it is known that the purpose of the spending has been changed after the release. There is no assurance that suspense accounts and advances are fully acquitted. Dimension score: D.

PFMSP Efforts Underway: This is another PI in which performance should improve as a result of a fully implemented TSA. As planned, commercial banks would maintain "zero-balance" accounts in which any positive balance would be swept to the central Treasury account at the end of each day. Thus, reconciliations of these accounts would be straightforward, and the key reconciliation would be of the Treasury main operating account at the BOL, which is being reconciled regularly and properly now.

PI-23: Availability of information on resources received by service delivery units

Indicator	Brief explanation	Score
PI-23 Availability of information on resources received by service delivery units (Scoring method M1)	Recent inquiries at province and district levels indicate that local schools and health clinics have no information about the resources allocated to them other than the salaries of the staff employed.	D

3.3.44 The latest (2006) Public Expenditure Tracking Survey (PETS) carried out jointly with the World Bank indicated that service delivery units at the local level (schools, health clinics) do not receive any information about the resources to be allocated to them other than the salaries of those employed. In practice, they have to obtain funding, sometimes informally, from those receiving their services. This general impression was confirmed in a different sector by a 2008 DFID/World Bank survey of pro-poor expenditure in the field of agriculture. Dimension score: D.

PI-24: Quality and timeliness of in-year budget reports

Indicator	Brief explanation	Score
PI-24 Quality and timeliness	(i) GFIS provides good information on approximately actual payments throughout the year, classified by administrative unit	C+

of in-year budget reports (Scoring method M1)	and economic category, allowing direct comparison with the original budget. However, there is no information on approximate commitments. (C) (ii) Reports are available monthly within four weeks of the end of each month. (A) (iii) The reports are derived directly from Treasury operations and are reliable within the limits of their coverage. However, expenditure financed from receipts not paid into Treasury accounts is not covered. (C)	

(i) Scope of reports in coverage and compatibility with budget estimates

3.3.45 Government payments are made by the Treasury Department of MoF following receipt of instructions from budget holders (ministries and provinces). Payments are made so long as documentation is in order and the amounts are within the six-month ceilings on each budget line currently in force, and are recorded consistently with the budget nomenclature. Thus, a direct comparison with the original budget is readily available for each budget line. When the new Chart of Accounts and electronic transmission of data to the central Treasury, which were introduced in October 2009, are fully in operation (foreseen by the end of 2009–10) the system will become more flexible. In other words, more precise information should be available on the approximate nature and location of each item of expenditure. However, because there are no controls at the commitment stage, the Dimension score must be C.

(ii) Timeliness of the issue of reports

3.3.46 Reports can be made monthly within four weeks of the end of any period, although hitherto this has not been done regularly each month. (When fully operational, the upgraded GFIS will be able to provide real-time budget execution information.) Thus, a report on budget execution during the first eight months of the then-current (2008–09) fiscal year was given to the National Assembly alongside the proposals for 2009–10. However, no in-year Budget Execution reports are published. Dimension score: A.

(iii) Quality of information

3.3.47 The information recorded in the Treasury system is reliable. However, revenues from the provision of services that are not paid into Treasury accounts, and the associated expenditures, are not covered in the reports. Insofar as such expenditures are covered by revenue, their omission does not pose a threat to the government's overall fiscal stance. The omission is nonetheless significant. Dimension score: C.

PFMSP Efforts Underway: As referenced here and in earlier sections, additional improvements are expected with the full and proper implementation of the upgraded GFIS. Furthermore, the inventory of technical revenue bank accounts and process of their consolidation into a TSA should result in progress on element (iii).

PI-25: Quality and timeliness of annual financial statements

Indicator	Brief explanation	Score
PI-25 Quality and timeliness of annual financial statements (Scoring method M1)	(i) A consolidated Budget Execution statement is prepared annually. It covers revenue and expenditure but not financial assets and liabilities. However, the statement excludes revenue from charges for services and the associated expenditure. (D) (ii) The Budget Execution statement is submitted for audit eight months after the end of the year to which it relates. (B) (iii)Statements are presented in a consistent format over time in accordance with national accounting standards, which are not consistent with IPSAS. The fact that the standards have not been published results in Dimension score: D.	D+

(i) Completeness of the financial statements

3.3.48 The consolidated statements of revenue and expenditure exclude revenues from charges for services—which apparently have remained outside Treasury bank accounts contrary to the intentions of Article 6 the Budget Law—and their associated expenditures. These statements do not include any information about financial assets and liabilities. Because of the significant omissions, Dimension score: D.

(ii) Timeliness of the submission of the financial statements

3.3.49 Article 71 of the Budget Law seems to require the State Audit Organization to have certified the financial statements by 31 March each year, that is, 6 months after the end of the financial year in question. This deadline probably is impossible because that the books must not be closed until the previous 31 December. It would be reasonable to interpret the provision as a requirement for the statements to be submitted for audit by 31 March (which would meet one of the conditions for an A rating). In practice, recent statements were submitted for audit only in May. Due to this delay, the rating is B.

(iii) Accounting standards used

3.3.50 National accounting standards are used for reporting purposes. These standards are not consistent with International Public Sector Accounting Standards (IPSAS) but do result in statements which are consistent over time. The standards have not been published. Dimension score: D.

PFMSP Efforts Underway: The Accounting Department is obtaining the assistance of international experts to assist in transitioning the national accounting standards to become consistent with IPSAS, but this transition will be a multiyear effort.

C (IV) External Scrutiny and Audit

PI-26: Scope, nature, and follow-up of external audit

Indicator	Brief explanation	Score
PI-26 Scope, nature, and follow-up of external audit (Scoring method M1)	(i) Apart from its examination of the consolidated Budget Execution statements, at present, SAO lacks the capacity and resources to annually audit in detail more than approximately one-third of ministries, provinces, and SOEs. Apart from the examination of the Budget Execution statement, audit work focuses on compliance. Performance audit has been initiated on procurement. National auditing standards are applied. (D) (ii) The SAO report on the previous year's budget execution has been submitted to the NA within two months of its receipt of the MoF Budget Execution statements. (A) (iii) SAO findings are discussed with auditees, and there is evidence of follow-up action on significant points. However, SAO lacks the resources to undertake early and systematic follow-up of all its recommendations. (B)	D+

(i) Scope and nature of audit, and adherence to auditing standards

3.3.51 At present, SAO has over 100 staff, approximately one-fifth of whom are stationed in two recently opened regional offices. SAO's audit remit extends to SOEs and projects as well as to budget revenue and expenditure. Capacity is gradually being built up, but apart from its examination of Budget Execution statements, SAO's audit of government agencies (ministries, provinces) and SOEs has covered approximately only one-third of them each year. The main focus of audit work is compliance, although some performance audit work has been initiated on procurement. Audit of government agencies should be performed in accordance with national standards that are being submitted to the NA. Development of SAO represents one element of the PFMSP, and assistance is being provided for the further development of SAO capacity. Reflecting the limited range of work, Dimension score: D.

(ii) Timeliness of submission of audit reports to the legislature

3.3.52 In 2008 and 2009 SAO submitted its annual reports on budget execution to the June/July session of the NA within two months of receiving the financial statements from MoF. No information was available about the timeliness of submission of other audit reports to the NA. Dimension score (based on the Budget Execution report only): A.

(iii) Evidence of follow-up on audit recommendations

3.3.53 Audited agencies are required by Article 20 of the 2008 Audit Law to respond in writing to SAO's findings and recommendations. It appears that, for the most part, the agencies comply with this requirement, formally at any rate. SAO states that it is able to have a constructive dialogue with most auditees about its findings. Moreover, there is evidence that some auditees follow up important recommendations such as those concerning the completeness of financial statements. Other auditees, however, are less cooperative, as has been reported publicly in general terms in the context of the presentation of the Budget Execution report to the NA. SAO intends to follow up the responses of government agencies and SOEs to its reports when it next subjects each of them to audit. However, because of capacity limitations, SAO has not yet been in a position to carry out an early and systematic follow-up of all of its recommendations. Dimension score: B.

PFMSP Efforts Underway: An action plan to further strengthen SAO in accordance with the results of a peer review by the New Zealand Audit Office has been approved, and resources are being obtained to carry it out over the medium term. SAO staff levels are being strengthened, and it recently opened a second regional office serving northern Laos.

PI-27: Legislative scrutiny of the annual Budget Law

Indicator	Brief explanation	Score
PI-27 Legislative scrutiny of the annual Budget Law (Scoring method M1)	(i) The following year's budget is presented for approval by the GOL to the NA at its June/July session. Prior to this, the NA Economic Planning and Finance Committee holds detailed consultations with MoF on the fiscal outlook and budget allocations, and with MPI on investment priorities. These consultations form the basis of recommendations by the NA on the shape of the budget, to the extent that the final proposals do not already take into account the views of the committee. (B) (ii) There are procedures for MoF to consult with the Economic Planning and Finance Committee when the general shape of the budget is being set and during the period immediately before it is submitted to the NA. The NA has sought to ensure that MoF actually complies with the calendar and procedural requirements for the preparation of the budget as laid down by the Budget Law. (B) (iii) The NA (through the Economic Planning and Finance Committee) is involved in budget preparations over 3–4 months. However, the committee receives the final proposals only a short time before the session so the NA is not yet able to influence expenditure allocations at the province/district levels to the same extent that it can in the central government ministries. (C) (iv) Only one major revision of the budget may be made each year, for which the NA's approval is required. There are clear rules governing the executive's wide powers to reallocate provision during the course of budget execution. (B)	C+

(i) Scope of the legislature's scrutiny

3.3.54 The Economic Planning and Finance Committee of the NA is consulted early in the (calendar) year when the general shape of the following (fiscal) year's budget is being settled, and again at the time when detailed proposals are being invited from ministries and provinces.

The committee then holds extensive discussions with MoF and MPI on expenditure allocations and investment priorities before MoF determines the detailed proposals to be presented to the NA at its June/July session. If the NA is not satisfied that MoF has taken sufficient account of its views, the earlier discussions provide the basis for additional recommendations to GOL, which MoF must take into consideration before the NA gives its approval. Dimension score: B.

(ii) Extent to which the legislature's procedures are well established and respected

3.3.55 The consultation arrangements described in (i) above are well established. The NA has clearly indicated its wish that the budget calendar and procedures laid down in the Budget Law should be more fully respected by MoF. Dimension score: B.

(iii) Adequacy of time for the legislature to respond to the budget proposals

3.3.56 Through its Economic Planning and Finance Committee, the NA has both the time and opportunity to make an effective input into the preparation of the budget for the central government ministries. However, the committee does not yet have the opportunity and resources to make a similar contribution to the allocation of expenditure at province/district levels. Moreover, the time available to the NA as a whole to review the detailed proposals before the Session begins remains insufficient. Dimension score: C.

(iv) Rules for in-year amendment of the budget without prior approval by the legislature

3.3.57 Article 54 of the Budget Law allows only one significant amendment of the overall budget each year, and it must be approved by the NA. Within the overall total, Article 65 permits line ministers to reallocate expenditure in their budgets from one line to another in the same chapter. Reallocation from one chapter to another requires the approval of the Minister of Finance. Only the Prime Minister can reallocate provision from one ministry or province to another. There is no limit to the amounts of reallocations within the overall total approved by the NA. Dimension score: B

PI-28: Legislative scrutiny of external audit reports

Indicator	Brief explanation	Score
PI-28 (Scoring method M1)	(i) The SAO report on Budget Execution is presented to the Economic and Standing Committees of the NA, which prepare recommendations for endorsement by the immediately following Plenary Session (at which SAO's report is presented by the Head of the Office in the presence of national television). (Other SAO reports are submitted only to the Prime Minister and the NA committees, and no information is available about any NA responses to them.) (A) (ii) Although there is a high-profile hearing on the Budget Execution report, there are no comparable arrangements for hearings on detailed reports involving the audited entities. (C) (iii) Actions were recommended to the GOL by the NA on the basis of the SAO report on 2007–08. No formal response was published, but there was evidence of action by MoF to improve financial statements. (B)	C+

(i) Timeliness of Parliamentary examination of audit reports

3.3.58 The SAO report on Budget Execution for the previous year (2007–08) was presented first to the Economic and Standing Committees of the NA, which prepare recommendations for endorsement by the immediately following June/July session of the NA. The Head of SAO presented the report at this session in the presence of national television and other media, although the full text of the report was not published. That year, points in the report were taken up by the NA in its Resolution transmitted to the GOL in the same Session covering actual budget execution in 2007–08, the interim Report on Budget Execution during the first 8 months of 2008–09, and the budget for 2009–10. Other SAO reports were submitted only to members of the NA Committees, and were not available to other members of the NA. There was no information about NA responses, if any, to these other reports. Dimension score, based on the Budget Execution report only: A.

(ii) Extent of hearings on key findings

3.3.59 Apart from its work on the Budget Execution report, the NA did not hold any hearings with auditees about the findings in SAO reports. Dimension score: C.

(iii) Recommendations by the legislature and GOL's response

3.3.60 In its July 2009 Resolution, NA called for information on revenues from charges for services and associated expenditures to be included in budget execution reports. It also criticized some failures to account for or return sums advanced by the Treasury. Although the GOL did not reply formally, there was evidence of action by MoF and others to give effect to the recommendations. Dimension score: B.

3.4 DONOR INDICATORS

D-1 PREDICTABILITY OF DIRECT BUDGET SUPPORT

Indicator	Brief explanation	Score
D-1: Predictability of direct budget support (Scoring method M1)	(i) Considering only the years 2005–06 to 2007–08, budget support fell short by more than 15 percent in only 1 year. (C) (ii) It does not appear that donors provided any information about the quarterly path of their disbursements. (D)	D+

3.4.1 Table 3.4, provided by External Finance Department, MoF, shows the budgeted and actual receipts of budget support and project/program loans received for each year from 2005–06 to 2007–08 (in US$). Donors providing budget support comprise World Bank, ADB, EC, Japan, and AusAID.

Table 3.4 Budgeted and Actual Receipts of ODA *(US$)*

	FY 2005–2006		FY2006–2007		FY 2007–2008	
	Planned	**Actual**	**Planned**	**Actual**	**Planned**	**Actual**
Budget support	**29,679,494**	**28,567,713**	**8,000,000**	**2,724,675**	**40,243,704**	**40,243,704**
Total loan	14,399,770	15,000,000	5,000,000	2,724,675	15,243,704	15,243,704
Total grant	15,279,724	13,567,713	3,000,000	-	25,000,000	25,000,000
Project /program	**211,887,856**	**198,751,905**	**220,736,475**	**240,646,794**	**205,020,554**	**186,038,634**
Total loan	181,692,121	142,644,411	173,236,475	190,701,082	165,401,735	146,361,795
Total grant	30,195,735	56,107,494	47,500,000	49,945,712	39,618,819	39,676,840
Total	**241,567,350**	**227,319,618**	**228,736,475**	**243,371,470**	**245,264,258**	**226,282,339**

Source: Ministry of Finance, External Finance Department.

(i) Annual deviation of actual budget support from donor forecast

3.4.2 As table 3.4 shows, the donors' forecasts for the first and third years were close to the actual. However, in 2006–07 the ODA paid was barely one-third of the forecasts. Dimension score: C.

(ii) Compliance with quarterly estimates

3.4.3 MoF states that donors provided no information about the expected quarterly path of their disbursements. Donors usually make payments in annual tranches. Major donors provide annual estimates, but their fiscal years do not coincide with that of the GOL. Dimension score: D.

D-2 Financial Information provided by donors for budgeting and reporting on project and program aid

Indicator	Brief explanation	Score
D-2: Financial information provided by donors for budgeting and reporting on project and program aid (Scoring method M1)	(i) Most donors provide estimates of aid project disbursements in a form that is compatible with the aggregate Lao PDR classifications and in time for inclusion in the budget estimates (B) (ii) Donors provide quarterly reports within one month of end-of-quarter on the actual disbursements made for 58 percent of the externally financed project estimates in the budget.(C)	C+

(i) Completeness and timeliness of budget estimates by donors for project support

3.4.4 According to MoF figures (table 3.4), the amounts included in successive budget estimates for total project aid were within 10 percent of the actual out-turn in each of the 3 years, although in the earliest year, a shortfall in loan disbursements was substantially offset by higher-than-projected grants. Overall, it appears that donors provide a reasonable indication of the amounts of expected disbursements and their allocation to projects. MPI and MOF state that the information is provided in time for them to include it in the budget estimates. MPI collects quarterly foreign aid reports from donors on actual and projected disbursements. MOF collects this information from Project Management Units (PMUs) to prepare the next year's budget. Dimension score: B.

(ii) Reporting by donors of actual disbursements

3.4.5 According to MOF information, the World Bank and ADB, which account for 40 percent of total budgeted estimates, provide online real-time access to the information on disbursements through their Client Connection Service. Other donors, which account for 18 percent of total estimates of ODA disbursement, provide quarterly reports one month after the quarter ends. So it can be concluded that donors provide quarterly reports within 1 month of end-of-quarter on the actual disbursements made for 58 percent of the externally financed project estimates in the budget. Dimension score: C.

D-3 PROPORTION OF AID MANAGED BY NATIONAL PROCEDURES

Indicator	Brief explanation	Score
D-3: Proportion of aid that is managed by national procedures (Scoring method M1)	Less than 50 percent of aid funds are managed through national procedures.	D

3.4.6 Only receipts of direct budget support clearly are managed according to national procedures in relation to all procurement, payment/accounting, auditing, and reporting. On the basis of MoF External Finance Department (EFD) figures, direct budget support constituted 10 percent, 1 percent, and 18 percent of total external receipts in the 3 successive years, respectively. The remainder of receipts was related to project aid, for which donors still largely insist on their own procurement, payment/accounting, and audit procedures. Nevertheless, all such projects are formally within the audit remit of SAO, and all, in principle, are included in fiscal reports.

Table 3.5 Aid Funds Managed through National Procedures for Selected Donors *(%)*

	WB	ADB	EC	AusAID	Japan
Donor funds to GOL that use the national procurement procedures	36	28	30	14	45
Donor funds to GOL that the national payment/accounting procedures	36	100	30	14	45
Donor funds to GOL that use the national audit procedures	36	100	32	14	45
Donor funds to GOL that use the national reporting	36	28	52	14	45

Source: Loan and Grant Utilization Summary, FY07–08, External Finance Department, MOF and donors' responses to questionnaires.

3.4.7 To the extent that new arrangements are effective in ensuring adherence to proper procurement procedures, donors may be more willing to accept national procurement and payment arrangements.

4. Government Reform Process

4.1 Background

4.1.1 Reform of PFM in the Lao PDR is coordinated through the Public Expenditure Management Strengthening Program (PEMSP). After having been approved by the Prime Minister's Office and the Minister of Finance, the program was adopted by the GOL of Lao PDR in November 2005. With the inclusion of revenue administration reforms within this program, as part of the new Budget Law promulgation in 2007, the PEMSP was renamed the Public Finance Management Strengthening Program (PFMSP).

4.1.2 The PFMSP remains a multiyear, medium-to-long term rolling program to improve policy consistency, efficient public financial management (PFM), and increased transparency and accountability in PFM by strengthening institutional arrangements and capacity, and making progress toward appropriate international financial management standards.

4.1.3 The PFMSP provides a framework for implementing GOL's policies and strategies laid out in the "Policy Paper on Governance," the National Growth and Poverty Eradication Strategy, and the National Socio-Economic Strategy 2006–2010. PFMSP has prioritized and sequenced the GOL's PFM reform initiatives, taking into account requirements and institutional capacity. As noted throughout the earlier sections of this report, the actions within the PFMSP offer the prospect of PFM improvements that should, over time, justify significantly higher PEFA ratings on many of the PIs considered here.

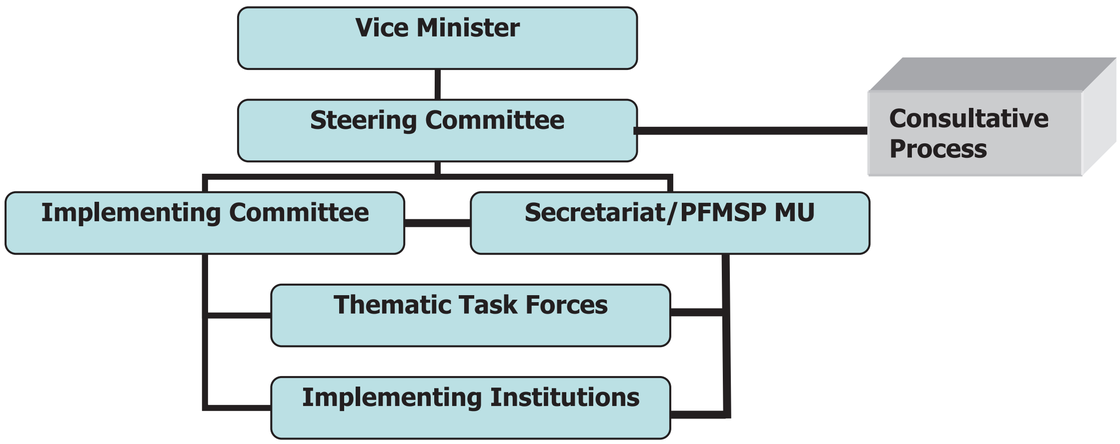
4.2 Management and Coordination

4.2.1 To facilitate program management and cross-departmental coordination, the Minister of Finance established an internal PFMSP Steering Committee (SC), which comprises representatives of the relevant MoF departments and is chaired by the Vice-Minister. The SC provides strategic guidance for PFMSP implementation; reviews and approves annual work plans, which lay out the steps to be taken to implement program components; and receives regular progress reports.

4.2.2 A PFMSP Implementation Committee (IC), chaired by the Director General for the Fiscal Policy Department, also was established to implement component elements of PFMSP as they relate to participating departments and agencies. The IC provides technical support to the PFMSP SC. In 2009 a PFMSP Management Unit (PFMSP MU) was created in the Fiscal Policy Department to provide support to the Director General in the coordination and supervision of component elements of the PFMSP. The PFMSP MU also assists in the administration of the recently created Multi-Donor Trust Fund (MDTF), which is a conduit for donor financial support of PFMSP. The PFMSP MU also serves as the secretariat for the PFMSP Implementation Committee's meetings. The PFMSP MU is staffed with three fulltime government officials, assisted by an international technical advisor and a local consultant. Depending on the focus of the program during specific periods, thematic task forces are formed to coordinate the program implementation in these areas. Four thematic task forces were created at the onset of the program. They cover revenue sharing, tax and custom centralization, national treasury centralization, and human resource and program management.

Figure 3.1 provides a schematic view of the management structure for PFMSP.

Figure 3.1 Schematic of PFMSP Management Structure



4.2.3 A progress report on the implementation of the annual PFMSP work plan is issued quarterly. Consultations with development partners are scheduled formally for at least twice a year and also take place as needed for specific development topics.

4.3 FINANCING AND DONOR SUPPORT

4.3.1 The PFMSP is supported by a variety of donors. The World Bank has provided funding of US$8.5 million under International Development Association (IDA) credit No. 3676-LA and additional financing of US$3 million under IDA Grant No. H316-LA toward the costs of the Financial Management Capacity Building Project (FMCBP), one of the funding sources for the PFMSP. Other donor support has come from the Asian Development Bank (ADB), Australian Agency for International Development (AusAID), European Commission (EC), French Development Agency (AFD), Japan International Cooperation Agency (JICA), Singapore Cooperation Enterprise (SCE), Swedish International Development Cooperation Agency (Sida) and Swiss Agency for Development and Cooperation (SDC).

4.3.2 In February 2009, a Multi-Donor Trust Fund (MDTF) was launched with $6 million in commitments from Australia, the EC, Sweden, and Switzerland. Administered by the World Bank, the MDTF provides a flexible source of funds on which the Lao Authorities can draw to pursue their priorities in strengthening PFM.

4.4 PFMSP COMPONENTS

4.4.1 The PFMSP is a comprehensive reform program with medium-term plans that are translated into an annual Work Plan. Apart from an element for program management, in 2009 the Annual work plan had 70 distinct activities grouped in 7 areas:

- Program Management
- Fiscal Planning and Budget Preparation
- Budget Execution, Accounting, and Financial Reporting
- Revenue Policy and Administration
- Local Government Financial Management
- Financial Legislation and Regulatory Framework
- Capacity Building.

4.4.2 Most of the individual activities are the responsibilities of individual MoF departments. Some activities also involve external bodies such as the State Audit Organization, line ministries, and provincial staff. MPI, which is responsible for planning and allocating capital spending, has participated to a limited extent in the PFSMP through the Medium-Term Fiscal Framework (MTFF) work supported by ADB. Current and prospective PFMSP activities relevant to each of the Performance Indicators have been summarized in the different sections of Part 3 of this report. Progress to date and additional action required in each of the six areas may be summarized as follows:

(i) Fiscal planning and budget preparation

4.4.3 The new Budget Law of December 2006 and its Implementing Decree (No. 25/PM of 14 February 2008) set out the framework and timetable within which the budget planning and execution processes should be carried out. The law also requires that the planning and presentation of each successive year's annual budget should take place within a medium-term fiscal framework (MTFF). Substantial progress has been made toward a more orderly budget preparation process. However, the budget calendar is not yet being fully observed, and a medium-term framework within which the development of each main public service can be planned is not yet in place.

(ii) Budget execution, accounting, and financial reporting

4.4.4 Central control has been established over the Treasury function at all levels of government, and work is in progress to consolidate all government bank balances in the Treasury Single Account (TSA). In future, all revenue is to be included in the budget presented to the NA. All revenue includes revenue from charges for services; and all expenditure, including that hitherto financed outside the budget from such user charges. A new electronic financial reporting system (GFIS) has been introduced, together with a new Chart of Accounts, which will facilitate expenditure reporting on a functional basis. However, these systems are not yet fully operational. In the medium term, this improved financial reporting system needs to be complemented by the development of the Treasury Information Management System (TIMS), which will integrate the execution and reporting processes. Work should begin soon to define national public sector accounting standards consistent with best international practice, with which all government financial reporting should eventually comply.

(iii) Revenue policy and administration

4.4.5 Central control has been established over the revenue collection process. This control should extend to receipts from charges that hitherto have remained mostly outside the budget. Value-Added Tax (VAT) (applicable so far to only the largest businesses) has been introduced. In addition, a start has been made toward the introduction of unique Taxpayer Identification Numbers (TINs), which eventually will apply to all taxpayers regarding all taxes. Nevertheless, much remains to be done to ensure that tax liabilities are defined more precisely, to close discretionary loopholes, and to enforce the full collection of owed amounts.

(iv) Local government financial management

4.4.6 Progress has been made in establishing a stable basis for the allocation of different revenue streams between central government and provincial/district administrations. A start also has been made in enforcing at least minimum per-capita expenditure levels on education and health services in all provinces/districts. Yet to be devised and implemented is a comprehensive system to allocate total spending power to each province that is derived from transparent and objective factors (population numbers and ages, population density).

(v) Financial legislation and regulatory framework

4.4.7 Further codification of the secondary legislation governing Treasury operations is likely to be needed. Similarly, secondary legislation will be needed to implement international accounting and financial reporting standards applicable to both general government and market sectors of the economy (including SOEs and the exploitation of state assets).

(vi) Capacity building

4.4.8 Much training already has been carried out in connection with different initiatives already undertaken within the framework of the PFMSP. Training will need to continue as additional PFMSP initiatives are rolled out. Training needs to be completed throughout the country in the implementation of standardized procurement procedures. Electronic processes will continue to replace manual operations in different areas of revenue assessment and collection, payment execution and reporting, and the presentation of accounts. For this reason, continuing major training efforts will be required to ensure that public authorities in all parts of the country acquire the capacity necessary to run the new systems.

4.4.9 This PFM Performance Report will be taken into account in the next review of the PFMSP over the coming few months. The PFM performance diagnosis will inform decisions on priorities for future action, including identification of areas that have not yet received sufficient consideration. The pursuit of improved ratings in subsequent PFM Performance reviews can never be an objective in its own right. However, such improvements can serve as measures of real PFM progress that can be expected to improve the quality and efficiency of public services, and therefore serve as targets that PFMSP should achieve within a specified timeframe.

4.4.10 Much of the PFM reform effort so far has been devoted to establishing an appropriate legal framework for budget preparation and execution, Treasury management, procurement, reporting and accounting, and external audit. The needs now are, first, to ensure that:

a. Budget Legislation is actually applied, that is, that revenue and expenditure are actually reported correctly and in full through GFIS, using the new Chart of Accounts;
b. Procurement legislation is brought fully into effect;
c. All government bank balances are actually consolidated in the Treasury Single Account
d. The range of external audit work is extended and the results published;

and, second, to:

Improve the budget planning process, so that available funds can be used to the best advantage in the development and improvement of public services for the whole population.

5. SUMMARY

5.1 Considerable progress has been made in establishing a good legal framework for Lao public financial management and in strengthening the central government's authority over budget planning and execution. The task ahead is to make a reality of these decisions and intentions, and so to improve the functioning of public services to benefit all citizens of the Lao PDR.

Appendix 1
Summary of PFM Performance Indicators and Source of Data/Information

Performance Indicators (PI)	Brief explanation	Score
PI-1 Aggregate expenditure out-turn compared to original approved budget (Scoring method M1)	Actual expenditure deviated from the initially approved amount by more than 10 percent in only 1 of the last 3 years. *Source:* GOL Official Gazettes for FY05–06, FY06–07, FY07–08.	**B**
PI-2 Composition of expenditure out-turn compared to original approved budget (Scoring method M1)	Aggregation of several major spending ministries into a single "other" heading, and the fact that provincial expenditure is broken down only by province and not by function make it impossible to assess whether there have been significant in–year changes in the expenditure mix. *Source:* GOL Official Gazettes for FY05–06, FY06–07, FY07–08.	**NR**
PI-3 Aggregate revenue out-turn compared to original approved budget (Scoring method M1)	Actual domestic revenue collection exceeded the budgeted amount in each of the last three years. *Source:* GOL Official Gazettes for FY05–06, FY06–07, FY07–08.	**A**
PI-4 Stock and monitoring of expenditure payment arrears (Scoring method M1)	(i) Apart from some outstanding payments for electricity, in which most of the accumulated arrears have already been paid, the Treasury Department is not aware of any arrears of current expenditure at the central level. Action is being taken to provide for paying off arrears owed to contractors and utility suppliers at province and district levels, and to prevent additional such arrears from being incurred. Dimension score: B. (ii) Specific initiatives have been undertaken to obtain information about arrears, which is not generated by routine expenditure returns. Dimension score: C. *Source:* MOF Budget Department Letter dated April 6, 2010 on Repayment of arrears for the electricity consumption by GOL agencies from 30/09/2005 to 30/09/2009 and allocations for 2009/10 electricity consumption payment.	**C+**
PI-5 Budget classifications (Scoring method M1)	The cash budget is set using administrative and economic classifications broadly consistent with GFS 1986. Exceptions are that some major repairs may be classified as investment, and some purchases of office and such equipment may be treated as current expenditure. However, hitherto there was no functional classification. *Source:* New COA, Treasury Accounting Codes, Bridging Tables for functional reporting of expenditure (MOF).	**C**

Performance Indicators (PI)	Brief explanation	Score
PI-6 Comprehensive-ness of information included in budget documentation (Scoring method M1)	The budget documentation is stated to include full information on five of the Benchmarks specified by the PEFA Frameworks. *Sources:* 1. FY2009-2010 Budget Plan document submitted by the GOL to the National Assembly. 2. Resolution by 7th Ordinary Session Meeting of the 6th National Assembly (Resolution No.137/NA, dated July 09, 2009 (National Assembly).	**B**
PI-7 Extent of unreported government operations (Scoring method M1)	(i) Except for the Road Maintenance and Forestry Development Funds, whose revenues and expenditures are included in the budget, revenue and expenditure of the extrabudgetary funds (other than payments to them included in the budget) are neither reported to the National Assembly nor published. Revenue from charges for the delivery of public services, and the associated expenditure, are neither reported nor published. Such expenditure could be on the order of 5 percent–10 percent of reported budgetary expenditure. In 2008–09 expenditure amounting to 2.7 percent of GDP (more than one-eighth of budgeted expenditure) was financed outside the budget through the bond issuance. Dimension score: D. (ii) In principle, complete information is included in fiscal reports about expenditure on loan-financed projects, although there may be some inconsistencies in the data. Expenditure on grant-funded projects is mostly covered as well. Dimension score: B. *Sources:* 1. Summary report on the national road maintenance fund activities FY 2008–2009 (from 10/2008 to 9/2009) published in *Vientiane Mai* newspaper on January 21, 2010 (Road Maintenance Fund, Ministry of Transport and Public Works) 2. 2006 Public Expenditure Tracking Survey Report (WB) 3. Budget Summary for FY08-09 (MOF)	**D+**
PI-8 Transparency of intergovernment-al fiscal relations (Scoring method M2)	(i) Allocation of spending power to provinces and districts (grants plus revenue share) is not based on transparent rules. Dimension score: D. (ii) Provinces' (and districts') budget proposals are submitted to MoF in the same timetable as ministries'. However, as in the case of the line ministries, the actual budgets eventually fixed by MoF may differ considerably from these proposals (see PI-11 below). Dimension score: D. (iii) No reports have been made showing the sectoral/functional breakdown of aggregate central and provincial government expenditure. Dimension score: D.	**D**

Performance Indicators (PI)	Brief explanation	Score
PI-9 Oversight of aggregate fiscal risk from other public sector entities (Scoring method M1)	(i) State-owned enterprises (SOEs) make quarterly reports to MoF SOE Financial Department on their financial performance, but no consolidated report is produced. External borrowing is effectively controlled by MoF. Dimension score: C. (ii) Provinces and districts are required to balance their budgets and have no power to borrow independently outside the government. However, there are indications that they have in effect been borrowing from contractors and suppliers. Dimension score: D. *Sources:* 1. Interviews with the SOE Financial Management Department, MOF. 2. Newspaper clip on domestic borrowing by Vientiane Municipality from private firm to develop That Luang esplanade (*Vientiane Times* February 24).	**D+**
PI-10 Public access to key fiscal information (Scoring method M1)	The general public has full access to information covering 1 of the 6 PEFA benchmarks. *Source:* Official Gazettes of 2009.	**C**
PI-11 Orderliness and participation in annual budget process (Scoring method M2)	(i) An annual budget calendar exists, at least by custom and practice, although the requirements of the Budget Law have not been followed. Although spending agencies generally have had time to prepare budget submissions, it is not clear that they all have been able to complete their submissions satisfactorily. Dimension score: C. (ii) Although there is probably a sufficient political understanding across the government about the sustainable level of aggregate expenditure, it has not been translated into realistic ceilings for each agency, within which they could plan how best to use the provision prospectively available. Dimension score: D. (iii)For each of the last three financial years, the NA has approved the following year's budget before the start of the year. Dimension score: A. *Sources:* 1. Budget Law, 2006 2. Budget plans of several agencies specified in the list of documentation provided by Budget Department, MOF (appendix 2).	**C+**

Performance Indicators (PI)	Brief explanation	Score
PI-12 Multiyear perspective in fiscal planning expenditure policy and budgeting (Scoring method M2)	(i) No forward estimates of fiscal aggregates have been prepared in the context of formulating each successive year's annual budget. Dimension score: D. (ii) Debt sustainability analysis has been undertaken annually, the lead being taken by the IMF/World Bank. Dimension score: A. (iii) No strategies yet have been prepared for the medium-term development of any of the main public services. Dimension score: D. (iv) Budgeting for investment and recurrent expenditure are separate processes. There are no arrangements for considering the future recurrent costs of maintaining and operating the assets/facilities created as a result of decisions on specific investments. Dimension score: D. *Source:* IMF Article IV Reports, interviews with FPD, MPI, ADB TA Consultant.	**D+**
PI-13 Transparency of taxpayer obligations and liabilities (Scoring method M2)	(i) Tax legislation lacks precision in some areas and is not in line with international accounting and reporting standards. Significant discretionary exemptions are given, which may distort competition among taxpayers. Dimension score: C. (ii) Some efforts are made to provide taxpayers with appropriate information, but they are not always user-friendly. The Tax and Customs Department websites are not yet operational. Dimension score: C. (iii) Although there are administrative procedures within the Tax Department for questioning tax assessments, the last word remains with the authorities. No dedicated independent appeals mechanism has been established, and the Courts' experience of appeals is very limited, comprising only customs duties cases. Dimension score: D. *Sources:* Interviews with Tax Department, written evidence from Customs Department (MOF), interviews with accountants/tax advisors.	**D+**

Performance Indicators (PI)	Brief explanation	Score
PI-14 Effectiveness of measures for taxpayer registration and tax assessment (Scoring method M2)	(i) Separate registration systems are maintained in each province with no links among them. A start has been made to introduce a unique Taxpayer Identification Number (TIN) in the context of the introduction of VAT in January 2010, which also will apply to customs duties. It is likely to take some years before TIN is applicable for all taxes throughout the country. Businesses cannot operate bank accounts until business, enterprise, and tax registration obligations have been met. Dimension score: C. (ii) Tax Department states that it is difficult to enforce registration and declaration obligations against small taxpayers, and that the department is obliged to devote much effort to their supervision. On the other hand, Tax Department is able to impose fines and penalties on delinquent taxpayers, and thus has a degree of coercive power. Recorded arrears are apparently relatively low. Customs Department has difficulty in enforcing revenue collection, given the length and porous nature of the country's land borders. However, once duties have been assessed, payment must be made before goods are released. Dimension score: B. (iii) Tax audits were stated by the Tax Department to be planned taking account of risk factors (including previous noncompliance). Nevertheless, some are based on random selection of taxpayers. In the case of the Customs Department, few staff are engaged in audit work. Focus is checking the consistency of documentation rather than examining the substance of transactions. Dimension score: D. *Source:* As for PI-13.	**C**
PI-15 Effectiveness in collection of tax payments (Scoring method M1)	(i) Over the last 3 years, arrears of tax at year-end have not exceeded 1.25 percent of tax collected during the year. Customs states that there are no arrears because tax must be paid before goods are released into circulation. Definition of arrears is very limited due to lack of clear assessments. (Not Rated-NR) (ii) All tax revenue is paid directly into Treasury accounts, although revenue collected in the provinces is remitted to the center only every two weeks. Dimension score: A. (iii) There is full monthly reconciliation between Tax Department records of receipts and Treasury bank records. Tax Department tracks actual payments against assessments on a running basis to chase late payers toward the end of the financial year. Dimension score: C. *Source:* As for PI-13.	**NR**

Performance Indicators (PI)	Brief explanation	Score
PI-16 Predictability in the availability of funds for commitment of expenditures (Scoring method M1)	(i) Once budgetary provision for the year has been determined, in consultation with the Treasury, the Budget Department sets cash ceilings for each budget line for the two subsequent quarters. These ceilings are updated quarterly. Dimension score: B. (ii) Since FY2009–10, ministries and provinces have not experienced problems in making payments, so long as the payments remained under the cash ceilings for the 6 months ahead. Dimension score: A. (iii) Major budget revision may be made only once a year and requires NA approval. Under the Budget Law, ministers can reallocate expenditure from one line to another within the same chapter of their budgets, but reallocation among chapters requires MoF approval. Reallocation among ministries or provinces requires the approval of the Prime Minister. Reallocations are not published. Dimension score: B. *Sources:* FY2009–10 budget plan and Q1&Q2 FY2008/09 budget plan of Vientiane province and Q1&Q2 FY2007–08 budget plan for MOE (October 10, 2007); Budget Law, 2006 and Official Gazettes.	**B+**
PI-17 Recording and management of cash balances, debt, and guarantees (Scoring method M2)	(i) Domestic and external public debt data are complete and reasonably reliable, but discrepancies can arise from exchange rate fluctuations. Internal reporting is ad hoc. (Information is published annually only by the IMF, following Article IV consultations.) Dimension score: C. (ii) MoF has prepared a plan to consolidate separate bank accounts into a Treasury Single Account (TSA). Nonetheless, numerous accounts with commercial banks remain open. An inventory of these bank accounts has been conducted, and action was expected to begin in the second half of 2010 to close them and consolidate the balances in the TSA. Dimension score: D. (iii) MoF External Finance Department ensures that external loans are contracted within preset annual ceilings and meet preset criteria for their terms. Domestic borrowing is managed by the Treasury to ensure cash availability. However, for domestic borrowing, provinces have engaged in uncontrolled issuing of guarantees. Dimension score: D. *Sources:* Interviews with FPD, Treasury, and External Finance Departments.	**D+**

<table>
<tr><th>Performance Indicators (PI)</th><th>Brief explanation</th><th>Score</th></tr>
<tr><td>PI-18
Effectiveness of payroll controls
(Scoring method M1)</td><td>(i) Public Administration and Civil Service Authority (PACSA) keeps a central database of all public servants (including those working in health and education but excluding police and armed forces). MoF has a database of the payroll in each ministry/province (police and armed forces excluded). Each quarter, PACSA gives a fresh authorization of approved staff numbers, grades, and incremental steps regarding each ministry/province payroll; and notifies recorded changes to these authorizations each month. Actual payroll payments by MoF must be consistent with these authorizations. Reflecting partial nature of this reconciliation, Dimension score: C.

(ii) PACSA notifies MoF twice a year of approved changes in staff numbers grading, increments, and allowances. MoF uses these consolidated instructions to update the payrolls of each ministry/province. Entitlement to increases in salary takes effect as soon as decisions are taken by the administrations concerned. Thus, the fact that the payroll is revised only twice a year necessitates numerous retrospective adjustments. Dimension score: C.

(iii) Responsibilities for changes to personnel and payroll records are clear, and there is both separation of functions and firm hierarchical supervision. The requirement for central notification of promotions and other increases in pay and/or allowances ensures an audit trail. Dimension score: A.

(iv) The State Audit Organization (SAO) has not yet carried out any directed payroll audits, but PACSA has in the past arranged for censuses involving physical verification of all civil employees, and in 2007 partial inspections covering education and health sectors. Dimension score: C.

Source: Interviews with MOF's Personnel Dept, National Treasury, and with PACSA. Lao PDR: Civil Service and Compensation Review. Draft May 2010 (World Bank).</td><td>C+</td></tr>
<tr><td>PI-19
Competition, value for money, and controls in procurement
(Scoring method M2)</td><td>(i) No data are yet available to assess the extent to which open competition is used to award public contracts. Dimension score: D.

(ii) Applicable legislation provides for the use of less competitive methods in defined circumstances, but evidence is incomplete that the rules for it are applied correctly. Dimension score: C.

(iii) No independent mechanism has been established to deal with complaints about how contracts are let. Dimension score: D.

Sources: Interviews with MoF's Procurement Monitoring Office (ProMO), new standard procurement documentation.</td><td>D+</td></tr>
</table>

Performance Indicators (PI)	Brief explanation	Score
PI-20 Effectiveness of internal controls for nonsalary expenditure (Scoring method M1)	(i) Lao PDR has not established any controls over expenditure commitments within the current budget year and, potentially, extending beyond the current budget year. MPI's list of approved investment projects submitted to the NA alongside the budget shows the total cost of each project as well as the estimated spending in the year immediately ahead. However, MoF does not track or control these future obligations. Dimension score: D. (ii) The Lao PDR system appears to rely more on the threat of compliance testing by inspection bodies (including the State Inspection Authority) than on controls to ensure that rules are obeyed. The only checks authorized before payments are of the availability of budgetary provision and the prima facie validity of the invoices. Dimension score: D. (iii)The rules for processing transactions by the Treasury are generally observed, and payment proposals that go above applicable cash ceilings (see PI-16) are automatically rejected. Budget rules may widely differ among provinces and districts. Transactions involving funds that have escaped the Treasury net are not protected in the same way. Dimension score: C. *Source:* Interviews with Treasury Department, MoF.	**D+**
PI-21 Effectiveness of internal audit (Scoring method M1)	(i) Internal audit does not exist as a separate function in Lao PDR. Dimension score: D. (ii) No internal audit reports have been produced as there is no separate internal audit. Dimension score: D. (iii)There being no internal audit reports, there is no management response to audit reports as such. Dimension score: D. *Source:* Interviews with Inspection Department, MoF.	**D**
PI-22 Timeliness and regularity of accounts reconciliation (Scoring method M2)	(i) All Treasury records of payment instructions and receipts are reconciled monthly with bank account records (by BOL at the center, and by commercial banks that hold the Treasury accounts in the provinces). There are no assurances of bank reconciliations for accounts outside Treasury control. Dimension score: B. (ii) Amounts held by ministries/provinces outside Treasury bank accounts should be subject to regular in-year reconciliation and clearance procedures, as should, for example, travel and subsistence advances. However, the National Assembly Resolution covering Budget Execution (PI-28 below) takes up SAO criticisms of money advanced from the Treasury not being accounted for or returned to the Treasury account. Moreover, some cash receipts at province/district level are used directly to finance expenditure without ever passing through any bank account. Dimension score: D. *Source:* Interviews with Treasury Department, MoF.	**C**

Performance Indicators (PI)	Brief explanation	Score
PI-23 Availability of information on resources received by service delivery units (Scoring method M1)	Recent inquiries at province and district levels indicate that local schools and health clinics have no information about the resources allocated to them other than staff salaries. *Source:* Lao PDR Public Expenditure Tracking Survey, March 2008, and "Public Expenditures for Pro-poor Agricultural Growth," DFID/WB (ARD) Partnership, Lao PDR Case Study, Feb 2008.	**D**
PI-24 Quality and timeliness of in-year budget reports (Scoring method M1)	(i) Throughout the year, GFIS provides good information about actual payments classified by administrative unit and economic category, enabling direct comparison with the original budget. There is no information about commitments. Dimension score: C. (ii) Reports are available monthly within four weeks of the end of each month. Dimension score: A. (iii)The reports are derived directly from Treasury operations and are reliable within the limits of their coverage. Expenditure financed from receipts not paid into Treasury accounts is not covered. Dimension score: C. *Source:* Interviews with Treasury Department, Sample of Quarterly Execution Report provided by TD.	**C+**
PI-25 Quality and timeliness of annual financial statements (Scoring method M1)	(i) A consolidated Budget Execution statement is prepared annually. It covers revenue and expenditure but not financial assets and liabilities. However, it has excluded revenue from charges for services and the associated expenditure. Dimension score: D. (ii) The Budget Execution statement is submitted for audit eight months after the end of the year to which it relates. Dimension score: B. (iii)Statements are presented in a consistent format over time in accordance with national accounting standards, which are not consistent with IPSAS. To reflect the fact that the standards have not been published. Dimension score: D. *Source:* Interviews with FPD, Accounting Department; Final Accounts published in Official Gazettes.	**D+**

Performance Indicators (PI)	Brief explanation	Score
PI-26 Scope, nature, and follow-up of external audit (Scoring method M1)	(i) Apart from its examination of the consolidated Budget Execution statements, SAO at present lacks the capacity and resources to audit in detail more than approximately one-third of ministries, provinces, and SOEs every year. Apart from the examination of the Budget Execution statement, audit work focuses on compliance. Performance audit has been initiated on procurement. National auditing standards are applied. Dimension score: D. (ii) SAO report on the previous year's budget execution is submitted to the NA within two months of its receipt of the budget execution statements from MoF. Dimension score: A. (iii) SAO findings are discussed with auditees, and there is evidence of follow-up action on significant points. However, SAO lacks the resources to undertake early and systematic follow-up of all its recommendations. Dimension score: B. *Source:* Interviews with SAO and a list of 18 audited agencies for FY08–09 (SAO) and NA Resolution as for PI-28 below.	**D+**
PI-27 Legislative scrutiny of the annual Budget Law (Scoring method M1)	(i) The following year's budget is presented by the GOL to the NA at its June/July session for approval. Prior to this, the NA's Economic Planning and Finance Committee has detailed consultations with MoF on the fiscal outlook and budget allocations, and with MPI on investment priorities. These consultations form the basis of NA's recommendations on the shape of the budget, to the extent that the final proposals do not already take into account the views of the committee. Dimension score: B. (ii) There are procedures for consultation with the Economic Planning and Finance Committee of the NA when the general shape of the budget is being set, and during the period immediately before it is submitted to the NA. The NA has been seeking to ensure that MoF actually complies with the calendar and procedural requirements for preparation of the budget laid down by the Budget Law. Dimension score: B. (iii) The NA (through the Economic Planning and Finance Committee) is involved in budget preparations over 3–4 months. However, the final proposals are received only a short time before the Session so the NA is not yet able to influence expenditure allocations at province/district level to the same extent as it can at central government ministry level. Dimension score: C. (iv) Only one major revision of the budget may be made each year, for which the NA's approval is required. There are clear rules governing the executive's wide powers to reallocate provision during the course of budget execution. Dimension score: B. *Source:* Interviews with NA Economic Planning and Finance Committee.	**C+**

Performance Indicators (PI)	Brief explanation	Score
PI-28 (Scoring method M1)	(i) SAO report on Budget Execution is presented to NA Economic and Standing Committees which prepare recommendations for endorsement by the immediately following Plenary Session (at which SAO report is presented by the Head of the Office in the presence of national television). (Other SAO reports are submitted only to the Prime Minister and the NA Committees, and no information is available about any NA responses to them). Dimension score: A. (ii) Although there is a high-profile hearing on the Budget Execution report, there are no comparable arrangements for hearings on detailed reports involving the audited entities. Dimension score: C. (iii) Actions have been recommended to the GOL by the NA on the basis of SAO report on 2007–08. No formal response has been published, but there is evidence of action to improve financial statements. Dimension score: B. *Source:* Interviews with SAO and NA Resolution on Endorsement of Summary Report on FY2008–09 budget Implementation and FY2009–10 budget Plan published in a Lao newspaper. The Resolution consists of 11 Articles, of which: • *Article 1* approves in principle the audit report by SAO on the final accounts of the FY2007–08 budget implementation. • *Article 2* advises GOL to implement audit opinion by SAO on misuse of public monies by some spending units. • *Article 3* approves the outturned figures for the first 8 months and estimated outturned figures of FY2008–09 budget. • *Article 4* approves the revised budget deficit for FY2008–09 budget. • *Article 5* approves budget revenue figures for FY2009–10 budget. • *Article 6* approves budget expenditure figures for FY2009–10 budget. • *Article 7* approves the budget deficit for FY2009–10 budget.	**C+**
D-1: Predictability of direct budget support (Scoring method M1)	(i) Considering only the years 2005–06 to 2007–08, budget support fell short by more than 15 percent in only 1 year. Dimension score: C. (ii) It does not appear that donors provide any information about the quarterly path of their disbursements. Dimension score: D. *Sources:* Budgeted and Actual Receipts of ODA for FYs05–08s (External Finance Department, MOF) and interviews with External Finance Department, MOF.	**D+**

Performance Indicators (PI)	Brief explanation	Score
D-2: Financial information provided by donors for budgeting and reporting on project and program aid (Scoring method M1)	(i) Most donors provide budget estimates of aid project disbursements, in a form compatible with the aggregate Lao PDR classifications and in time for inclusion in the budget estimate. Dimension score: B. (ii) Donors provide quarterly reports within one month of end-of-quarter on the actual disbursements made for 58 percent of the externally financed project estimates in the budget. Dimension score: C. *Source:* Interviews with External Finance Department, MOF and list of donors with timeliness of quarterly disbursement report and their project fund disbursement estimate in the budget (External Finance Department, MOF).	**C+**
D-3: Proportion of aid managed by use of national procedures (Scoring method M1)	Less than 50 percent of aid funds is managed through national procedures. *Source:* Responses on questionnaires by EC, AusAID, ADB, and JICA; and interviews with MoF's External Finance Department.	**D**

Appendix 2
List of Documentations

A. Government Self-Assessment Report

B. Budget Department, MOF

1. FY2008–09 budget plan of BOLikhamxay province (August 14, 2008)
2. Q1&Q2 FY2008–09 budget plan for BOLikhamxay province (November 12, 2008)
3. NA Resolution on endorsement of the FY2007–08 budget execution report and FY2008–09 budget plan (August 26, 2008)
4. FY2007–08 budget plan of Vientiane Capital (September 4, 2007)
5. Q1&Q2 FY2007–08 budget plan for MOE (October 10, 2007)
6. FY2006–07 budget plan for Luang Prabang province (July 26, 2006)
7. Q1 FY2008–09 budget execution report submitted for the GOL/Cabinet meeting
8. FY2009–10 budget plan for the Central Party Board on Training and Propaganda
9. FY2008–09 budget plan for Ministry of Energy and Mining
10. Detailed costing for Parts 10+11+12 of FY2008–09 submitted by the Party Committee for External Relations (May 2, 2009)
11. Estimated FY2008–09 budget execution and Q1&Q2 FY2009–10 budget plan of Vientiane Capital approved by the Prime Minister
12. FY2009–10 budget plan and Q1&Q2 FY2008–09 budget plan of Vientiane province
13. FY2009–10 budget plan for MOE (September 02, 2009)
14. Detailed FY2008–09 budget plan of Lao Women Union
15. State Budget Plan 2008–09—MOF 14–08–2008
16. State Budget Implementation 2005–06 and Budget Plan 2006–07—MOF 26/07/2006
17. State budget Implementation 2005–06, Six-Month State Budget Implementation 2006–07 and State Budget Plan 2007–08 MOF 4/9/2007
18. Budget Circulars–instructions:
    1) FY2005–06 budget:
        a) Prime Minister's Instruction on NSEDP and budget Planning

b) Finance Minister's Circular on Budget Planning

2) FY2006–07 Budget:

a) Prime Minister's Instruction on NSEDP and Budget Planning

b) Finance Minister's Circular on Budget Aggregates–Numbers and Guidance on Budget Implementation

3) FY2007–08 Budget:

a) Prime Minister's Instruction on NSEDP and Budget Planning

b) Finance Minister's Circular on Budget Aggregates–Numbers and Guidance on Budget Implementation

4) FY2008–09 Budget:

a) Prime Minister's Decree on NSEDP and Budget Planning

b) Finance Minister's Instruction on Budget Implementation

5) FY2009–10 Budget:

a) Finance Minister's Circular on Budget Planning

C. External Finance Department:

1. Loan and Grants Implementation 2005–06, 2006–07, 2007–08 (IMF format)
2. Loan Repayment Report FY2007–08
3. Summary of Budget and Actual Receipt of Budget Support from 2005–06 to 2008–09 (received on 28–01–2010).
4. List of donors and timeliness of quarterly reporting

D. Fiscal Policy Department:

1. National Socio-Economic Development Plan and Budget Plan from 2005–06 to 2008–09
2. Prime Minister 's Instruction on Implementation of State Budget from 2005–06 to 2008–09
3. Prime Minister's Instruction on Budget Formulation for 2009–10

E. State Audit Organization (SAO)

1. List of 18 audited agencies for FY08-09 (letter dated January 28, 2010)

F. **Comments on PEFA First Draft Report:**

1. State Audit Organization (dated 8/10/2009 and Sept 09)
2. Procurement Office, MOF (dated 14/10/2009)
3. External Finance Department, MOF (dated 4/9/2009 with Loans and Grants Utilization Forecast 2008–09 IMF Format and Current Status of Foreign Credits as 31/12/2008)
4. Financial Policy Department, Bank of Laos (dated 15/10/2009)
5. Tax Department, MOF (dated 16/10/2009)
6. Custom Department, MOF (dated 15/10/2009 and 8/9/2009)
7. Accounting Department, MOF (dated 7/10/2009)
8. Budget Department, MOF (dated 3/9/09 and 7/10/09)

Appendix 3
List of Participants to the PEFA

No.	Name	Position
1.	Mr. Amphol Southiphon	Technical Staff, Expenditure/Revenue Accounting Division, Fiscal Policy Department, MOF
2.	Mr. Bounleau Sinsayvoravong	Deputy Director General of External Finance Department, MOF
3.	Mr. Bounleuth Thepvongsa	DG, State Audit Department, SAO, Deputy Head of PEFA Working Group
4.	Mr. Chittakon Savasdy	Technical Staff, Expenditure/Revenue Division, Fiscal Policy Department, MOF
5.	Ms. Chounmaly Khammunty	Deputy Division Director, Macro Fiscal Policy Division, Fiscal Policy Department, MOF
6.	Ms. Daophet Sihavong	Deputy Division Director, Budget Department, MOF
7.	Ms. Khammai Bounthavy	Deputy Division Director of Expenditure, Department of Treasury, MOF
8.	Mr. Kenlangsy Sengkhamyong	Deputy Director General, SOEs Finance Management Department, MOF
9.	Mr. Kenlangsy Sengkhamyong	Department of State Enterprise Financial Management, MOF
10.	Ms. Phirany Phitsamay	Division Director, Accounting Department, MOF
11.	Mr. Phousavanh Chanthasombath	Statistics Department Ministry of Planning and Investment.
12.	Mr. Phouthanouphet Saysombath	Deputy Director General of National Treasury, MOF
13.	Mr. Lithideth Sanavongsay	Deputy Division Director, Foreign Relations Division, Cabinet, SAO
14.	Mr. Nakonkham Khamvongsa	Inspection Department, MOF
15.	Mr. Nisith Keopanya	Director General of Civil Service Management Department and Project Manager of GPAR PACSA
16.	Mr. Saysamone Xaysouliane	Director General of Budget Department, MOF
17.	Mr. Saythong Ouiphilavong	Deputy Division Director, ICT Division, Tax Department, MOF
18.	Mr. Sichantha Thammavong	Deputy Director, Macroeconomic Division, Department of General Planning, MPI
19.	Mr. Souvanhny Khammanyvong	Division Director, Department of State Enterprise Financial Management, MOF
20.	Mr. Syvai Vilayhan	Technical Staff, Macro Fiscal Policy Division, Fiscal Policy Department, MOF
21.	Mr. Somsanouk Sinamunty	Division Director, Macro Fiscal Policy Division, Fiscal Policy Department, MOF
22.	Mr. Souliya Souphithack	Deputy Division Director, Statistics Division, Fiscal Policy Department, MOF

No.	Name	Position
23.	Ms. Souvanpheng Boupphanouvong	Vice Chair, Committee for Economy, Planning and Finance, NA
24.	Mr. Sinxay Phetsavong	Technical Staff, Tax Department , MOF
25.	Mr. Souvanhny Khammanyvong	Department of State Enterprise Financial Management, MOF
26.	Mr. Thanta Khongphayly	DG, Department of Economy, Planning and Finance, Committee for Economy, Planning and Finance, NA
27.	Mr. Thedthoun Soukaloun	Technical Staff, Department of External Finance, MOF
28.	Ms. Thongdy Soulichack	Director General, Fiscal Policy Department, MOF, Head of Government PEFA Working Group
29.	Mr. Thone Phonpachamh	Director, Procurement Monitoring Office, MOF
30.	Mr. Vanpheng Khan	Deputy Director, Accounting Division, National Treasury, MOF
31.	Mr. Vixay Santivong	Director, Economic Statistics Division, Statistics Department, MPI
32.	Mr. Vongdeaun Kaobuaban	Technical Staff Accounting Department, MOF
33.	Mr. Christopher Hnanguie	Country Economist, Asia Development Bank
34.	Ms. Juana Aristizabal Pinto	Development Cooperation Attaché, European Commission
35.	Mr. Romain Louvet	Attaché (Governance, Health), Embassy of France
36.	Ms. Masako Kimura	Project Formulation Advisor, JICA
37.	Ms. Akemi Ishikawa	Advisor and Research, Embassy of Japan
38.	Mr. Remy Duiven	Deputy Country Director, Swiss Agency for Development and Cooperation
39.	Ms. Phanthakone Champasith	Program Officer, Development Cooperation, AusAID
40.	Mr. Jorgen Persson	Counselor, Embassy of Sweden in Bangkok, Section for Development Cooperation in Vientiane, LAO PDR
41	Ms. Daodeuane Duangdara	Manager Tax and Legal Services, PricewaterhouseCoopers
42	Mr. K. Ganesan Kolandevelu	Country Head, KPMG Lao PDR