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FIDUCIARY SYSTEMS ASSESSMENT

HUNAN SUBNATIONAL GOVERNANCE AND RURAL PUBLIC SERVICE DELIVERY

PROGRAM FOR RESULTS

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ABBREVIATIONS AND ACRONYMS

BEC	Bid Evaluation Committee
CIIA	China Institute of Internal Audit
CNAO	China National Audit Office
DLI	Disbursement-linked indicator
DPO	Development Policy Operation
DRC	Development and Reform Commission
FM	Financial Management
FSA	Fiduciary Systems Assessment
FY	Fiscal Year
GPL	Government Procurement Law
HLG	Higher-Level Government(s)
IFI	International Financial Institution
IIA	Institute of Internal Auditors
INT	Vice Presidency Integrity Department
IPSAS	International Public Sector Accounting Standards
MOF	Ministry of Finance
N/A	Not applicable
NDRC	National Development and Reform Commission
OPRC	Operational Procurement Review Committee
PAO	Provincial Audit Office
PforR	Program for Results
PAP	Program Action Plan
PFM	Public Financial Management
PIA	Program Implementing Agency
PRC	People's Republic of China
TBL	Tendering and Bidding Law
TOR	Terms of Reference
TSA	Treasury Single Account

SECTION 1: CONCLUSIONS

1.1 Reasonable assurance

Hunan Province, together with the World Bank, is in the process of preparing the Hunan Subnational Governance and Public Service Delivery Program-for-Results (PforR) Project. As part of preparing this operation, and pursuant to the World Bank's Policy and its associated Directive on PforR Financing of November 10, 2017 and June 20, 2019, respectively, as well as the World Bank's PforR Fiduciary Systems Assessment Guidance Note issued on June 30, 2017, the World Bank's Fiduciary Team has carried out a fiduciary systems assessment (FSA). According to the FSA - and given the agreed actions to strengthen the fiduciary systems, as reflected in the Program Action Plan (PAP), and other proposed mitigation measures will be implemented - the Program's fiduciary systems, including the financial management (FM), procurement, and governance systems, are considered to adequately meet the requirements laid out in the Bank's PforR Policy and Directive: They provide reasonable assurance that the Program's financing proceeds will be used for the intended purposes, with due attention to the principles of economy, efficiency, effectiveness, transparency, and accountability.

1.2 Risk assessment

Major FM risks identified in the FSA are: 1) The county budget credibility is weak, mainly hindered by their high reliance on HLG transfers and the lack of capacity to project the HLG transfers. 2) County governments haven't adopted medium-term budget, and the annual budget didn't provide a clear link with the local development strategy or explanation about fiscal implications of any policy change. 3) There were unfunded mandates – that county governments couldn't afford to finance some projects mandated by the HLG. 4) 'Program' is not a budget classification element in China and the required Program financial reporting can't be generated from government treasury system. 5) Government auditors did not audit the proposed Program funds and prepared the Program audit report.

The proposed mitigation measures include: 1) A DLI associated with enhancing the predictability of transfers to the eight Program counties has been agreed on, and a guideline on improving transfer predictability will be issued by Hunan Province in FY 2020; 2) DLIs on performance-based funds transfer for rural transport and compulsory education have been agreed on, and the transfer funds from HLGs will be distributed to counties based on Program output rather than Program input as an incentive for counties to prioritize their investment and in order to ensure the required counterpart funds are delivered to Program activities as committed; 3) Drawing on the experiences of other PforR projects in China, a tailored format for Program financial reporting will be designed and agreed on by the Bank and the Hunan Provincial Finance Department; and 4) The Bank will work with the Hunan Provincial Audit Office (PAO) to develop terms of reference (TOR) to help coordinate Program audits.

Major procurement risks identified are:

1) Contracts may be awarded to firms or individuals which are debarred or under temporary suspension by the Bank or other multilateral development banks. The following mitigation measures have been proposed: (a) Upon Program loan effectiveness, the Hunan Province Department of Finance shall issue a high-level official letter or official instruction to require Program implementation agencies to ensure that no contract will be awarded to ineligible firms or individuals. (b) Procurement staff at the Hunan Provincial Department of Finance are to check on a daily basis the latest lists of the debarred and temporarily suspended firms and individuals and share this information with all implementing agencies. (c) The TOR for annual external audit

shall include the task of randomly selecting contracts and assessing whether they have been awarded to an ineligible firm or individual.

2) The Bank may not be informed of fraud allegations and corruption issues during the implementation of the Program. A Program manual shall therefore require the client to inform the Bank of any credible and material allegations of fraud and any corruption issues as part of the Program progress reports, as mandated in the loan agreement.

Taking into consideration the above-mentioned FM and procurement risks and the proposed mitigation measures, the overall fiduciary risk of the Program is rated as ‘moderate’.

1.3 Procurement exclusions

Under the Program, no high value contracts will be awarded exceeding the thresholds set by the Operational Procurement Review Committee (OPRC).

SECTION 2: SCOPE

The scope of the FSA for the FM systems is based on the defined boundaries of the PforR operation and the Program Expenditure Framework. The Fiduciary Team has assessed the fiduciary systems of all key Program implementing agencies in Hunan Province, including the provincial Finance Department, Transport Department, Education Department, and Audit Office. Program activities will be implemented in eight selected counties in Hunan Province. A PEFA assessment has been conducted in each of these counties, and the FSA relies on these PEFA assessment results in most aspects.

The FSA of the procurement system covers the implementation agencies responsible for carrying out procurement and contract implementation, as listed in Table 1.

Table 1 - Procurement implementation agencies

County	Implementation agency
Liuyang	Public Works Construction Center
	Education Bureau
	Highway Construction & Maintenance Center
Pingjiang	Public Works Construction Center
	Education Bureau
	Transport Bureau
Rucheng	Public Works Construction Center
	Education Bureau
	Highway Construction & Maintenance Center
Guidong	Development & Reform Bureau
	Education Bureau
	Highway Construction & Maintenance Center
Yizhang	Public Works Construction Center
	Education Bureau
	Highway Construction & Maintenance Center

Youxian	Public Works Construction Center
	Education Bureau
	Highway Construction & Maintenance Center
Liling	Housing & Urban-Rural Development Bureau
	Education Bureau
	Transport Bureau
Chaling	Public Works Construction Center
	Education Bureau
	Highway Construction & Maintenance Center

SECTION 3: REVIEW OF THE PFM CYCLE

3.1 Planning and budgeting

3.1.1 Adequacy of budgets

The Budget Law of the People's Republic of China (PRC), issued in 2015 and revised in 2018, has set the budget management framework for the central government and local governments at all levels in China. The financial budget includes four budgets, and there are detailed provisions for the preparation, review, approval, supervision, implementation, and adjustment of the budget and final accounts. The Hunan Finance Department and county finance bureaus are responsible for preparing the annual budget and final accounts at the corresponding level, for organizing the implementation of the general budget, deciding on the use of the budget reserve, working out budget adjustment plans, supervising budget execution of the budget implementing entities, and for reporting to the People's Congress and its Standing Committee on the implementation of the annual budget.

The bottom-up preparation method and the process of 'two ups and two downs' are adopted when preparing the budget. The 'first up' refers to the budget proposals prepared by the budgetary units and submitted to the respective finance department/bureau. The 'first down' refers to the finance department/bureau's release of the budget ceilings for each budgetary unit upon review of the submitted proposals. For the 'second up', each budgetary unit revises its budget proposal in line with the received budget ceiling and re-submits it to the finance department/bureau. The 'second down' means the approved sectoral budget is distributed to each budgetary unit once the annual budget prepared by the finance department/bureau has been approved by the People's Congress.

The eight PEFA assessments have shown that all revenue and expenditure information is included in the budget reports. Most budget information is publicly accessible. Since the implementation of the new Budget Law, the budget management framework has been significantly improved. According to the new Law, all government revenues and expenditures are to be included in the budget to be approved by the People's Congress. In addition, the new Budget Law puts strong emphasis on budget transparency. The reform has addressed the need for more participation of both the legislature and the public in the budget process.

However, while county governments have a strong capacity for budget estimation and allocation of fiscal funds from own financing sources, they have little predictability of the amount and composition of HLG transfers. At the end of the preceding fiscal year (FY), HLGs normally pay a small portion of the transfers in advance, most of which are general transfers. Consequently, only this part of transfers is included in the

budget estimates. For FYs 2016 to 2018, the deviation of actual grants from original budgeted grants was consequently as follows:

Table 2 - Transfer fund outturn, as percentage of transfer fund budget

FY	Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling
2016	177.50%	225.80%	232.70%	204.80%	229.50%	116.98%	196.88%	151.27%
2017	162.70%	199.90%	170.40%	253.10%	275.90%	108.32%	178.24%	86.66%
2018	131.70%	361.40%	139.90%	109.40%	230.90%	99.37%	174.42%	95.16%

Significant budget adjustments take place as local governments do not receive full information on their grant and debt quotas from the HLG prior to the start of the FY. Moreover, budget adjustments are only partially reflected in the mid-year budget adjustment proposal submitted to the Standing Committee of the People's Congress for approval.

Upon approval of the HLG budget, the county government receives the remaining general transfer as well as information of the earmarked transfers. The disbursement of transfer funds is monitored by the Ministry of Finance (MOF) and therefore usually on time.

Great variation between budgeted and actual expenditures and revenues indicates that budget reliability in the selected eight Program counties is weak. Since most of these counties rely heavily on HLG transfers (see Table 3), yet HLGs fail to provide timely information on these transfers, county governments face difficulties in preparing sound budget estimates.

Table 3 - Ratio of HLG transfers to general public budget expenditures

FY	Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling
2016	35.15%	79.55%	74.69%	85.00%	61.96%	39.17%	49.69%	62.40%
2017	28.97%	76.29%	74.99%	86.00%	72.72%	38.31%	50.64%	67.36%
2018	27.28%	71.05%	68.41%	73.00%	74.30%	38.86%	51.01%	58.22%

In addition, county governments neither prepare medium-term budgets, nor do they link budgets to the prevailing development strategies or provide any explanation about the fiscal implications of policy changes. Similarly, county governments do not prepare multiple-year program budgets. In addition, in some counties, the costing information of major investment projects is not included in the budget documents.

The funds to be invested in the proposed Program would stem from various funding sources, including transfer funds from the central and provincial governments, as well as funds from the respective county government's budget. The Fiduciary Team observed gaps between the funds available and funds to be invested due to the weak capacity of some county governments in raising counterpart funds (some earmarked grants from the HLG are distributed to the counties in the form of subsidies, and the county government is required to contribute to the counterpart funds but their financial capacities are weak). In addition, there appears to be some mismatch between the demands of county governments and the projects initiated by the HLG.

The lack of predictability of HLG grants hampers the capacity of local governments to forecast cash or credibly allocate budgets to budgetary units. The weak control of in-year budget allocation and expenditure arrears (as noted in the PEFA assessments) make it hard for budgetary units to effectively deliver public services.

In light of the above issues, the Bank is concerned about the predictability and reliability of funds for the proposed Program. It recommends that the Hunan Provincial Finance Department develops a program-based expenditure classification or prepares the budget by program. This would moreover support the Government in moving towards program-based PFM, including program-based financial reporting.

3.1.2 Procurement planning

The responsible implementation agency prepares the procurement plan based on the available allocated budget and/or according to the available self-raised funds. The procurement plan is submitted to the respective supervision authority and the finance department/bureau for review and clearance. Since the procurement plan is prepared by the implementation agency, which is the end-owner of the works, goods, and services to be procured, the plan is closely linked to its needs. The procurement of some goods and services, such as for the education sector and schools, might be consolidated and procured centrally at provincial, prefectural, or county level for economy of scale. During the FSA, the eight selected Program counties were asked to provide information on actual contract volumes awarded compared to the original cost estimates. The provided data are as follows:

Table 4 - Actual award price against cost estimate

County	Implementation agency	Actual award price against cost estimate (%)		
		Works	Goods	Services
Liuyang	Public Works Construction Center	82	95	97
	Education Bureau	100	93	No data
	Highway Construction & Maintenance Center	95	100	No data
Pingjiang	Public Works Construction Center	No data	No data	No data
	Education Bureau	80-85%	N/A	80-85%
	Transport Bureau	97		99
Rucheng	Public Works Construction Center	98.13	95.05	97.01
	Education Bureau	93.07	94.05	95.07
	Highway Construction & Maintenance Center	99.30	95.43	
Guidong	Development & Reform Bureau	90	N/A	95
	Education Bureau	86.5	96.5	99
	Highway Construction & Maintenance Center	97		
Yizhang	Public Works Construction Center	95	N/A	95
	Education Bureau	97	99	97.6
	Highway Construction & Maintenance Center	95		95
Youxian	Public Works Construction Center	93-100	86	82
	Education Bureau	98	99	99
	Highway Construction & Maintenance Center	95		
Liling	Housing & Urban-rural Development Bureau	95.13	87	99.65
	Education Bureau	99.1	33-99	90-99
	Transport Bureau	90	96	N/A
Chaling	Public Works Construction Center	95	90	

	Education Bureau	95	99	
	Highway Construction & Maintenance Center	97		

3.1.3 Procurement profile of the Program

Procurement activities under the Program will include the procurement of (i) works related to compulsory education, that is, primary schools and junior high schools and rural road rehabilitation/maintenance; (ii) goods and non-consulting services related to compulsory education, rural road rehabilitation/maintenance, digital platforms, and institutional strengthening and capacity building; and (iii) consulting services related to compulsory education, rural road rehabilitation/maintenance, digital platforms, and institutional strengthening and capacity building.

3.2 Budget execution

3.2.1 Treasury management and funds flow

Hunan Province started the Treasury Centralized Payment System Reform in 2003. Governments at all levels have since integrated all financial funds into the treasury single account (TSA) system. All revenues are directly collected into the treasury account or the special financial account, and all expenditures are paid to the contractors/suppliers/beneficiaries through the TSA.

Cash forecasting includes revenue and expenditure forecasts. While the county tax bureaus are responsible for forecasting cash revenues, the county finance bureaus are responsible for expenditure forecasting. The county tax bureaus forecast cash revenue monthly, whereas cash expenditure forecasting is divided into daily expenditure and non-basic expenditure forecasting. Daily expenditure forecasts are made based on the payment schedule, according to the Budget Law.

Payments can be made to the budgetary units within the approved budget. No restrictions, such as commitment ceilings apply to the budgetary units. The centralized payment center at each county finance bureau is responsible for initiating all payments, following the request of the budgetary units.

However, aggregate expenditure outturn deviated significantly from the budgeted amounts in the last three FYs, 2016-2018 (see Table 5). The deviation was largely caused by the unpredictability of HLG transfers. In addition, significant budget adjustments were made, which undermined the predictability of budget execution.

As no internal controls existed over payment arrears until 2019, incurred expenditure arrears are likely to not have been recorded in the budget units' bookkeeping. Until 2019, the Government used cash-basis accounting. Since no monitoring system for payment arrears was in place, data on the stock of expenditure arrears were not available to the county finance bureaus.

Table 5 - Aggregate expenditure outturn, as percentage of budget

FY	Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling
2016	146.30%	190.40%	130.90%	165.00%	248.20%	106.12%	150.50%	232.67%
2017	156.60%	187.20%	121.10%	206.80%	193.90%	107.25%	152.10%	220.63%
2018	153.20%	284.40%	121.80%	109.60%	157.10%	103.18%	155.19%	211.28%

Predictability of in-year resource allocation is low. In FY 2018, the originally approved budget expenditure amounted to a comparably small share of the executed expenditure (see Table 6). As the budget is not reliable, in-year budget adjustment is frequent, but not well regulated. As a result, commitment ceilings, going up to the approved budgets, cannot be meaningfully administered.

Table 6 - Ratio of original approved budget to final account expenditure

FY	Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling
2018	33.00%	33.00%	54.00%	48.00%	58.00%	136.73%	74.50%	69.47%

Some county governments have issued documents that require all budgetary units to submit and publish their overall expenditures and their expenditure performance plans, including public service outputs and results, with the sectoral budget. The documents also provide a framework for self-assessment reports, and budgetary units were required to carry out self-assessments of the budgeted expenditures in FY 2018.

However, the PEFA assessors have noted that for some sectors, only output indicators are included in the performance plans, no outcome indicators. In some instances, outcome and output indicators are described quite vaguely, and indicators are often not sufficiently specified to capture whether planned outputs and outcomes have been achieved. Overall impact of the used resources is therefore not clear.

Since the Central Government has been paying more attention to budget performance evaluation, the Hunan Provincial Finance Department has been cooperating with the provincial Education Department to prepare a set of detailed budget performance evaluation indicators.

3.2.2 Accounting and financial reporting

Counties in Hunan Province used to use a FM information system to improve the efficiency of PFM. It comprised, among other things, a sectoral budget management system, a budget index system, a debt management system, a centralized treasury payment system, a budget implementation monitoring system, and an agricultural subsidies distribution system. To further improve FM ability and efficiency, Hunan Province began to develop an electronic financial system in 2019. The system, comprising 25 financial business management subsystems and four financial comprehensive management subsystems, was officially launched in January 2020. It covers income, expenditure, debt and assets and spans all processes related to budget preparation, budget execution, and the preparation of final accounts. It links budget supervision and performance evaluation and it integrates the PFM of the province, the municipalities, counties, and townships. By adopting the advanced integrated FM information system, Hunan Province expects to establish a unified standard for business and financial data and to achieve an all-in-one processing of financial operations in the province.

Before 2019, three accounting regulations were used in the public sector in China, that is, the general budget accounting regulation, the accounting regulation for administrative units, and the accounting regulation for public service units. Except for general budget accounting, which has remained on cash-basis, the government has moved to modified accrual-based accounting.

Before 2019, the budget execution report was prepared by the provincial Finance Department/county finance bureaus and submitted to the People’s Congress at the corresponding level for review and approval. The report was prepared annually comparing budget execution with the approved budget and contained

information about revenue, expenditure and liabilities, however no information about financial and tangible assets. Moreover, regular monthly and quarterly reports were prepared for the analysis of budget execution. Budget execution data were compared to the original budget in terms of coverage and classification, and they were largely consistent and useful for the analysis. The annual budget execution report was prepared according to national standards, and submitted timely to the external auditor after the end of the FY.

In 2013, the MOF initiated a piloting reform for accrual-basis government financial reporting. Also Hunan Province introduced accrual-basis financial reporting on a trial basis, but the reports were neither submitted to the People's Congress for review and approval nor subject to the government auditors' annual audit. In 2018, an accrual-basis accounting regulation was issued by the MOF for the public sector in China to provide a concrete basis for budget executing entities to record their transactions and prepare their financial reports on accrual basis. The new regulation, which adopts international good practice and principles of the International Public Sector Accounting Standards (IPSAS), became effective on January 1, 2019. The first accrual-basis government financial report should be prepared for FY 2019, however not be submitted to the People's Congress and auditors, since the related procedures and requirements are still under consultation and discussion.

For fixed assets owned and used by budgetary units, both physical and financial data are maintained in the selected counties. However, for infrastructure managed by the budgetary units, only physical, no financial information is held. According to the MOF's newly issued government accounting regulation, from January 1, 2019 onwards, all fixed assets, including infrastructure, should be presented in the accrual-based reports. But it was noted during the identification mission that no assets valuation had been conducted in the eight selected counties of rural roads, and as a result, the assets value could not be reflected in the financial reports.

Since 'program' is not a budget classification element, program-based financial reports cannot be generated from the government treasury system. Unlike for the education sector, for which two budget line items can be used to collect and present expenditures associated with the PforR operation, no budget items are available for rural road expenditures to be included in the Program. Also, the budget items for administrative services are still under discussion. As an alternative, it has been agreed that a set of satellite accounts shall be established to track expenditures on rural transport, and a tailored Program financial reporting template will be discussed and agreed on by the Bank and all government entities involved.

3.2.3 Procurement processes and procedures

3.2.3.1 Procurement regulatory framework

Generally, the procurement of works, goods, and material is incorporated into permanent works, and consultancy services related to works, including geological exploring and survey, engineering design, cost estimating and pricing, and construction supervision follow the procedures specified in the Tendering and Bidding Law (TBL) and the related implementation regulations enacted by the governments at central, provincial, prefectural, and county level in accordance with the TBL. The TBL became effective as of January 1, 2000. At the central level, the implementing regulation came into force on February 1, 2012 and was amended on March 1, 2017, March 19, 2018, and March 2, 2019.

Other procurement follows the procedures stipulated by the Government Procurement Law (GPL) and the related implementing regulations promulgated by the governments at central, provincial, prefectural, and

county level. The GPL became effective as of January 1, 2003. At central level, the implementing regulation for the GPL issued by the State Council became effective as of March 1, 2015.

3.2.3.2 Procurement processes and procedures

Procurement following the TBL

The Development and Reform Commission (DRC) at central, provincial, prefectural, and county level provides overall guidance for, and coordination of, all procurement activities which follow the TBL and its related implementing regulations. The relevant sectoral government authorities at the given level assume the day-to-day supervision responsibilities for the procurement activities.

The procurement methods allowed for by the TBL include open competitive bidding and direct invitation (limited competitive bidding or shopping), with open competitive bidding being the preferred method.

Public resources transaction centers exist at the provincial, prefectural, and some county levels. They provide an electronic platform for their clients, the implementing agencies, to publish their procurement notices and to issue their bidding documents and any subsequent clarification and addenda. All bidders are required to register with the transaction centers' information system. They then submit their bid securities and bids either electronically or in person. The transaction centers also provide physical space for bid opening and evaluation. Together with staff from the relevant sectoral government authorities, the staff of the transaction centers assume the supervision and monitoring functions during the bid opening and evaluation. However, they do not participate in the bid evaluation. The transaction centers also provide a website for the publication of the contract award recommendation and, after the standstill period, of the final contract award.

In all provinces, it is common practice for qualified procurement agent companies to carry out procurement services on behalf of clients. These companies receive a special certification from the relevant government authorities.

If the value of the contract to be procured exceeds a specified threshold – that is, ≥ 4 million for works, ≥ 2 million for goods, and ≥ 1 million for services - procurement needs to take place through open competitive bidding at the local public resources transaction center. If the value of the contract to be procured is less than the specified threshold, procurement can be carried out through limited competitive bidding or shopping, and the procurement is not required to be conducted at the public resources transaction center. The invitation for limited competitive bidding or shopping is sent to at least three qualified bidders.

The procurement notice is published on the website of the Hunan Provincial Tendering and Bidding Supervision (<http://www.bidding.hunan.gov.cn>) and the relevant prefectural website of the public resources transaction center (for example for Chenzhou, <http://czggzy.czs.gov.cn/>). It contains information of civil works, goods or services to be procured, including the information on the quantity of the works activities/goods/service assignments, the location, the requested completion/delivery time, the name, address, and contact of the client, the qualification and experience requirements, etc.

The client is responsible for the preparation of the bidding documents, with assistance from the hired procurement agent company (which normally helps with the commercial part of the bidding document), the design institute (which normally helps with the technical part of the bidding document) and sometimes a

professional firm (which usually helps with the bill of quantities). There are standard bidding documents issued by various line ministries and sectoral departments. In accordance with the TBL and relevant implementation regulations, the bidding documents must not contain biased qualification, experience or technical requirements. Reference to specified manufacturers is also not allowed.

After publication of the procurement notice, potential bidders are given at least five calendar days to acquire the bidding documents.

Any request for clarification regarding the bidding documents is required to be sent not later than ten calendar days prior to the deadline for bid submission and opening. The client is required to provide response to such requests for clarification within three calendar days. Any clarification or addendum shall be issued in writing to all the bidders not later than 15 days prior to the deadline for bid submission and opening.

The time between the date of availability of the bidding documents and the deadline for bid submission and opening is normally at least 20 calendar days.

According to the TBL and its implementing regulations, if the number of bids received is less than three, the client must conduct re-bidding.

All bids received by the deadline for bid submission and opening, and which are properly sealed, are opened and read out. Any bid which is not properly sealed will be rejected, unopened, and not read out.

The amount of the bid security does not exceed two percent of the cost estimate. Validity of the bid security and validity of the bid are the same.

According to Clauses 27 and 50 of the Implementing Regulation, the client is allowed to specify the acceptable maximum bid price in the bidding document. However, the client is not allowed to specify the acceptable lowest bid price. A bid shall not be rejected because the bid price falls outside the margin or bracket of the cost estimate. Further, whether the bid price is close to the cost estimate or not shall not be a condition for contract award recommendation. However, according to Clause 51 of the Implementing Regulation, if the bid price is lower than the cost or higher than the specified acceptable maximum bid price, the bid shall be rejected.

The bid evaluation committee (BEC) comprises five or seven members, one from the client and others selected randomly from official sectoral expert databases maintained by the relevant government authorities at the central or provincial level. The experts are normally required to have a working experience of not less than eight years in the relevant sector.

The contract is normally awarded to the lowest responsive bidder that meets the qualification and experience requirements specified in the issued bidding documents.

The contract award recommendation is disclosed to the public including all the bidders, and the standstill period is at least three calendar days.

The contract award information is published on a specified website of the Hunan Provincial Tendering and Bidding Supervision (<http://www.bidding.hunan.gov.cn>). In addition, it is also published on the prefectural website of the public resources transaction center (for example for Chenzhou, <http://czggzy.czs.gov.cn/>).

Within 30 calendar days after contract award, the client and the successful bidder sign the contract. The successful bidder will furnish to the client the performance security, if so required in the bidding document. The amount of performance security normally does not exceed ten percent of the contract price.

Within five calendar days of contract signing, the client will return the bid securities to the bidders including the saving interest amount accrued in the corresponding period.

Procurement following the GPL

The MOF and the finance authorities at central, provincial, prefectural, and county levels provide overall guidance for, and coordination and supervision of, all procurement activities which follow the procedures of the GPL and its implementing regulations. The relevant sectoral government authorities assume the day-to-day supervision responsibilities for procurement activities.

If the value of the contract to be procured exceeds the specified threshold (normally RMB 1 million), procurement shall be conducted through open competitive bidding at the local public resources transaction center. If the value of the contract to be procured is less than the specified threshold, the procurement can be carried out through limited competitive bidding or shopping. The procurement is not required to be conducted at the public resources transaction center.

The following procurement methods may be adopted under the GPL:

- Open competitive bidding (the preferred procurement method).
- Direct invitation.
- Competitive dialogue.
- Single source selection.
- Shopping.
- Other methods which may be approved by the relevant government authorities.

The procurement notice is published on the specified website of Hunan Provincial Government Procurement (<http://www.ccgp-hunan.gov.cn/>). In addition, the procurement notice is also published on the relevant prefectural website of the public resources transaction center (for example for Chenzhou, <http://czggzy.czs.gov.cn/>). The procurement notice contains information of civil works, goods or services to be procured, including information on the quantity of the works activities/goods/service assignments, the location, the required completion/delivery time, the name, address and contact of the client, the qualification and experience requirements, etc..

At least five calendar days are made available to the potential bidders to acquire the bidding documents.

Any clarification or addendum is issued in writing to all bidders not later than 15 days prior to the deadline for bid submission and opening.

The client is responsible for the preparation of the bidding document, but there are standard bidding documents issued by the MOF. The bidding documents may not contain biased qualification, experience or technical requirements. Reference to specified manufacturers is also not allowed.

The amount of bid security does not exceed two percent of the cost estimate.

With respect to the evaluation criteria, the GPL provides two options for bid evaluation: (a) contract award to the lowest responsive bidder; (b) contract award to the highest rated responsive bidder.

The BEC members are selected randomly from official expert databases for government procurement maintained by the relevant government authorities at the central or provincial level.

The contract award recommendation is disclosed on the website of Hunan Provincial Government Procurement (<http://www.ccgp-hunan.gov.cn/>) within two working days after the contract award recommendation is made. In addition, the information is published on the relevant prefectural website of the public resources transaction center (for example for Chenzhou, <http://czggzy.czs.gov.cn/>).

If the number of qualified bidders or the number of responsive bids is less than three, re-bidding is required.

The bid security is returned to the unsuccessful bidders within five working days after contract award notification and to the successful bidder within five working days after contract signing.

Procurement performance

Procurement is generally efficient. The time from publication of the procurement notice to the deadline for bid submission and opening is normally 20 calendar days. The bid evaluation is usually completed in one day. Once the evaluation is completed, the contract award recommendation is disclosed to all bidders for three days on the official website of the government and the website of the public resources transaction center. If no complaint is received within the standstill period, the contract is awarded promptly and signed within 30 calendar days after contract award. In general, the bidding process is highly competitive. The data provided by the eight selected Program counties show that there is adequate competition with a substantial number of participating bidders:

Table 7 - Number of participating bidders

County	Implementation agency	Number of participating bidders		
		Works	Goods	Services
Liuyang	Public Works Construction Center	15-35	3-5	3-8
	Education Bureau	40-48	3-8	No data
	Highway Construction & Maintenance Center	3-27	3-6	2-6
Pingjiang	Public Works Construction Center	8-15	N/A	N/A
	Education Bureau	3-6	N/A	3-6
	Transport Bureau	3-5		
Rucheng	Public Works Construction Center	3-5	3-10	3-7

	Education Bureau	3-5	3-10	3-8
	Highway Construction & Maintenance Center	75-100	3-10	N/A
Guidong	Development & Reform Bureau	10	0	6
	Education Bureau	6-15	3-5	3-5
	Highway Construction & Maintenance Center	12		
Yizhang	Public Works Construction Center	3-45	N/A	3-10
	Education Bureau	3	3	3
	Highway Construction & Maintenance Center	3-45	N/A	3-10
Youxian	Public Works Construction Center	15-25	8	6
	Education Bureau	10	5	5
	Highway Construction & Maintenance Center	> 3		
Liling	Housing & Urban-rural Development Bureau	5	5	5
	Education Bureau	3-18	3-7	3-5
	Transport Bureau	3-5	3-5	N/A
Chaling	Public Works Construction Center	3-31	3-8	3-5
	Education Bureau	5-20	3-5	
	Highway Construction & Maintenance Center	5-9		

Competitive bidding is the most common procurement method under both the TBL and the GPL. Table 8 shows the share of contracts procured through competitive method for each of the eight selected counties in FY 2018:

Table 8 - Procurement in FY 2018

County	Total value of procurement (RMB)	Total value of contracts procured through non-competitive method (RMB)	Total value of contracts procured through competitive method (RMB)	Percentage of competitive method by value (%)
Liuyang	1,286,713,000.00	17,490,000.00	1,269,223,000.00	98.64
Pingjiang	2,572,161,562.00	34,086,454.00	2,538,075,108.00	98.70
Rucheng	1,033,964,061.59	32,433,500.00	1,001,530,561.59	96.90
Guidong	462,558,424.70	21,156,077.00	441,402,347.70	95.40
Yizhang	756,222,722.65	0.00	756,222,722.65	100.00
Youxian	523,550,311.44	0.00	523,550,311.44	100.00
Liling	1,922,287,259.00	5,127,600.00	1,917,159,659.00	99.73
Chaling	No data.	N/A	N/A	N/A

Note: The data do not include very small contracts. The thresholds for very small vary from county to county with RMB 0.2-0.5 million for works, RMB 0.1-0.2 million for goods, and RMB 0.1-0.2 million for services.

During the FSA, data were also collected on cancellation and re-bidding of procurements (see Table 9). The reasons for cancellation and re-bidding include that none of the bidders meet the qualification requirements, that some major work or good items are left out in the issued bidding documents, or that the lowest evaluated responsive bid price significantly exceeds the cost estimate.

Table 9 - Number of cancellations and re-bids

County	Implementation agency	Total number of contracts			Number of cancellations and re-bids		
		2016	2017	2018	2016	2017	2018
Liuyang	Public Works Construction Center	48	54	50	1	2	1
	Education Bureau	151	229	153	0	0	0
	Highway Construction & Maintenance Center	20	9	19	1	2	1
Pingjiang	Public Works Construction Center	17	33	4	0	0	0
	Education Bureau	70	100	104	0	0	0
	Transport Bureau	43	67	30	0	0	0
Rucheng	Public Works Construction Center	135	290	383	0	0	0
	Education Bureau	24	37	25	0	0	0
	Highway Construction & Maintenance Center	0	3	5	0	0	0
Guidong	Development & Reform Bureau	39	23	10	0	0	0
	Education Bureau	44	43	44	0	2	2
	Highway Construction & Maintenance Center	8	8	4	0	0	0
Yizhang	Public Works Construction Center	86	108	44	0	0	0
	Education Bureau	45	82	88	0	0	0
	Highway Construction & Maintenance Center	110	150	165	0	0	0
Youxian	Public Works Construction Center	275	321	242	0	0	0
	Education Bureau	155	192	195	0	0	0
	Highway Construction & Maintenance Center	7	10	6	0	0	0
Liling	Housing & Urban-rural Development Bureau	21	104	40	3	3	0
	Education Bureau	79	82	117	0	0	0
	Transport Bureau	5	15	17	0	0	0
Chaling	Public Works Construction Center	224	526	195	10	18	27
	Education Bureau	1	9	8	0	0	0
	Highway Construction & Maintenance Center	0	3	7	0	0	0

3.2.3.3 Institutional procurement arrangements

Four parties are usually involved in the procurement process:

1. The implementation agency (the client). The implementation agency assumes the responsibility for procurement as well as contract implementation, which includes: procurement planning and preparation of the budget, preparation of the bidding documents, organizing the procurement, participation in the bid evaluation, signing and execution of the contract, supervising the quality of the works, and ensuring compliance with the contract terms.

2. A procurement agent: Each client will hire an independent external procurement agent. The agent’s responsibilities include assisting with the preparation of the commercial part of the bidding documents, publishing the invitation for bids, issuing the bidding documents, opening the bids publicly, organizing the bid evaluation (but not being a member of the BEC), and preparing the bid evaluation report.

3. A design institute: Each client will also hire an external design institute. The responsibility of the design institute is to assist the client in preparing the technical part of the bidding document.

4. The public resources transaction center: If the cost estimate of the contract exceeds the specified threshold, the procurement activities are carried out via the platform provided by the public resources transaction center.

3.2.4 Contract administration and performance

Once the contract is awarded, the client signs the contract with the contractor, supplier or consultant selected. The client is responsible for contract administration throughout the contract implementation period. The contractor, supplier or consultant may not assign the contract to another party. However, subject to prior concurrence of the client, the contractor or consultant may sub-contract some works and assignments as long as they are not critical components or activities.

Regarding the timeliness of contract completion, most contracts are completed within the contractual period. Table 10 provides information for a number of contracts executed by implementation agencies in each county. Causes for time slippage include, among other things, unforeseen geological events, the need for additional works or delay caused by lengthy land acquisition procedures.

Table 10 - Timeliness of contract completion

County	Implementation agency	Number of contracts surveyed	Number of contracts completed within initial contract period	Number of contracts with time slippage	Percentage of time slippages against initial contract period
Liuyang	Public Works Construction Center	10	6	4	Contract 1: 6%. Contract 2: 14%. Contract 3: 16%. Contract 4: No data.
	Education Bureau	10	8	2	Contract 1: 66%(50/30 days). Contract 2: 50% (90/60 days).
	Highway Construction & Maintenance Center	10	10	0	N/A.
Pingjiang	Public Works Construction Center	8	5	3	Contract 1: 33% (40/30 days). Contract 2: 20% (360/300 days). Contract 3: 5% (420/400 days).

	Education Bureau	10	8	2	Contract 1: 9% (82/75 days). Contract 2: 1% (85/75 days).
	Transport Bureau	10	7	3	Contract 1: 242% (24/7 months). Contract 2: 100% (12/6 months). Contract 3: 88% (17/9 months)
Rucheng	Public Works Construction Center	10	1	9	Contracts 1-4: 11%. Contracts 5-8: 22%. Contract 9: 33%.
	Education Bureau	10	10	0	N/A.
	Highway Construction & Maintenance Center	4	4	0	N/A.
Guidong	Development & Reform Bureau	10	0	10	Contracts 1-2: 13%. Contracts 3-4: 17%. Contracts 5-6: 25%. Contracts 7-10: 33%.
	Education Bureau	10	10	0	N/A.
	Highway Construction & Maintenance Center	10	10	0	N/A.
Yizhang	Public Works Construction Center	10	10	0	N/A.
	Education Bureau	No data.	No data.	No data.	No data.
	Highway Construction & Maintenance Center	10	1	9	Contract 1: 6%. Contract 2: 75%. Contracts 3-9: 100% above.
Youxian	Public Works Construction Center	10	10	0	N/A.
	Education Bureau	10	10	0	N/A.

	Highway Construction & Maintenance Center	8	No data.	No data.	No data.
Liling	Housing & Urban-rural Development Bureau	10	10	0	N/A.
	Education Bureau	10	4	6	Contracts 1-4: 33%. Contract 5: 50% . Contract 6: 166%.
	Transport Bureau	10	3	7	Contracts 1-4: 66%. Contracts 5-7: 100% above.
Chaling	Public Works Construction Center	No data.	No data.	No data.	No data.
	Education Bureau	4	2	2	No data.
	Highway Construction & Maintenance Center	No data.	No data.	No data.	No data.

In terms of cost control, cost variation may occur during contract implementation, leading to additional costs and cost overrun. Variations are handled in accordance with the terms and conditions of the contract. Their final value is subject to strict clearance depending on the value of the variation and local regulations. For example, for contracts in the transportation sector, variations are first certified by the project supervision engineer and then endorsed by the relevant client staff at the site. They are subsequently submitted to the relevant transport bureau for clearance and to the local financial bureau for final approval.

Table 11 presents information on cost overruns for a number of historical contracts for each county. Causes for cost overrun include, among other things, unforeseen geological events, the need for additional works or delay caused by lengthy land acquisition procedures.

Table 11 - Cost overrun

County	Implementation agency	Number of contracts surveyed	Number of contracts with cost overrun	Range of cost overrun (in %)	Number of contracts with cost overrun > 15%
Liuyang	Public Works Construction Center	10	3	C1: 2.26%. C2: 2.77%. C3: 3.43%.	0

	Education Bureau	10	0	N/A.	0
	Highway Construction & Maintenance Center	9	2	C1: 1.08%. C2: 1%.	0
Pingjiang	Public Works Construction Center	0 (audit pending)	N/A.	N/A.	N/A.
	Education Bureau	10	8	C1-5: <10%. C6-8: 10-13%.)	0
	Transport Bureau	8	2	C1: 0.4%. C2: 1.5%.	0
Rucheng	Public Works Construction Center	10	0	N/A	0
	Education Bureau	10	0	N/A	0
	Highway Construction & Maintenance Center	4	0	N/A.	0
Guidong	Development & Reform Bureau	4	4	C1: 1%. C2: 10%. C3-4: 12%.	0
	Education Bureau	10	0	N/A.	0
	Highway Construction & Maintenance Center	9	6	2-9%	0
Yizhang	Public Works Construction Center	6	4	C1: 21%. C2: 15%. C3: 11%.	C4: 21%.
	Education Bureau	2	1	8%	0
	Highway Construction & Maintenance Center	2	1	9%	0
Youxian	Public Works Construction Center	10	9	C1-C8: 4-8%.	C9: 63%.
	Education Bureau	10	0	N/A.	0

	Highway Construction & Maintenance Center	6	6	C1-2: 5-6%.	C3: 32%. C4-6: above 100%.
Liling	Housing & Urban-rural Development Bureau	1	1	16%.	1
	Education Bureau	9	8	C1-8: 14-15%.	0
	Transport Bureau	4	2	C1-2: 17-19%.	2
Chaling	Public Works Construction Center	No data.	No data.	No data.	No data.
	Education Bureau	3	2	C1: 5%. C2: 12%.	0
	Highway Construction & Maintenance Center	No data.	No data.	No data.	No data.

As for quality control, the supervision engineer and the client are responsible for daily oversight and quality supervision. The client is responsible for organizing final acceptance. Final acceptance is jointly conducted by representatives from the relevant government agencies, such as the local finance bureau, the environment protection bureau, the land resources bureau, the water bureau, the house and urban-rural development bureau, and the quality and technology supervision bureau, as well as representatives of the client, in accordance with the applying national specifications or national code and regulations.

As shown in Table 12, no major quality or performance issues have occurred for the surveyed contracts in the eight selected counties.

Table 12 -Contracts with quality and performance issues

County	Implementation agency	Number of contracts surveyed	Number of contracts with quality issues	Number of contracts with performance issues
Liuyang	Public Works Construction Center	10	0	0
	Education Bureau	10	0	2 (Delivery delay)
	Highway Construction & Maintenance Center	10	0	0
Pingjiang	Public Works Construction Center	10	10	0
	Education Bureau	10	0	0
	Transport Bureau	10	0	0

Rucheng	Public Works Construction Center	10	0	9 (Completion delay)
	Education Bureau	10	0	0
	Highway Construction & Maintenance Center	4	0	0
Guidong	Development & Reform Bureau	10	0	0
	Education Bureau	10	0	0
	Highway Construction & Maintenance Center	10	0	0
Yizhang	Public Works Construction Center	10	0	0
	Education Bureau	10	0	0
	Highway Construction & Maintenance Center	10	0	0
Youxian	Public Works Construction Center	10	0	0
	Education Bureau	10	0	0
	Highway Construction & Maintenance Center	8	0	0
Liling	Housing & Urban-rural Development Bureau	10	0	0
	Education Bureau	10	0	0
	Transport Bureau	10	0	0
Chaling	Public Works Construction Center	No data.	No data.	No data.
	Education Bureau	10	0	0
	Highway Construction & Maintenance Center	No data.	No data.	No data.

Payment is made by the client to the contractor, supplier or consultant in accordance with the terms and conditions of the contract and without major delay. Normally, payment is made one to four weeks after the payment application is issued by the client. However, for most contracts, payment to the contractor, supplier or consultant will halt once the total payment made reaches a certain percentage (normally 80 percent) of the total contract price. The remaining 20 percent are paid once the government audit of the project is concluded. It normally takes six months to two years for the government audit to be concluded after the project is completed and taken over by the client.

An efficient dispute resolution procedure is included in each contract. In case of a dispute, the first option is an amicable settlement between the two contract parties. If no agreement is reached, the dispute is referred to the relevant government supervision authorities for adjudication. If either party is dissatisfied with the recommendation of the adjudicator, the party can refer the dispute further to either the local arbitration commission or the court. Usually, contracts provide for both parties to invoke the arbitration or lodge the legal suit.

Contractual remedies are specified in the signed contract. The client is entitled to terminate the contract in case of default of the contractor, supplier or consultant. This requires a written notification served in due course by the client to the other party.

3.3 Internal controls

3.3.1 Internal controls

The Chinese Government takes internal control in the public sector very seriously. The Regulation on Internal Control of Administrative and Public Service Units was issued by the MOF in 2012. It provides detailed instructions and guidance to all budgetary units on strengthening their internal control function. Moreover, a set of basic internal control standards and practical guidance were issued by the MOF in recent years, as reference for all public sector entities. At the MOF itself, the Inspection and Evaluation Bureau has been established and is responsible for the internal control and internal audit of the MOF. In 2014, the MOF issued the Basic Internal Control Rules (Decree No. 40), which provide a good model for other ministries and subnational government entities. All public sector entities are required to prepare an annual internal control report.

There is adequate control over, and stewardship, of program funds, with well-defined delegation of authority. Following the national policy and regulations issued by the MOF and NDRC, the Hunan Provincial Government has issued a series of regulations regarding fund management, implementation measures, and result verification procedures, etc.

Activities under the Program will concentrate on the transport, education and the administrative service sectors, and related internal control regulations have been issued by the provincial sectoral departments. For instance, Decree No. 22, which was issued by the Ministry of Communication in 2015, and Regulation No. 24, issued by the Hunan Provincial Transport Department in 2011, have regulated and managed rural road maintenance throughout the province. The Ministry of Communication has also established detailed technical criteria to implement and supervise rural road maintenance. While the county transport bureaus are responsible for rural road maintenance, both the provincial and prefecture transport bureaus conduct regular supervision of the performance of the counties. The provincial Transport Department has developed detailed performance evaluation regulations and it requires that all county level rural roads should be supervised once every two years (50 percent/ year), while the township level rural roads should be supervised once every five years (20 percent/ year).

The provincial Transport Department assessed the maintenance performance of the eight Program counties in 2019. Its report shows that the portion of rural roads in average or below average condition is very high in some counties (see Table 13). This evidences the existing gap between required and available funds for road maintenance.

Table 13 - Road condition at average or below-average level according to county, FY 2019

Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling
41.28%	80.87%	46.34%	91.88%	75.88%	66.40%	83.97%	84.23%

In 2019, the MOF and Ministry of Education jointly issued Decree No. 100 regarding Measures for the Management of Subsidy Funds for the Improvement and Capacity Enhancement of Weak Areas in Compulsory Education. It defines the areas in need of support and stipulates how to calculate and allocate subsidies, the application procedures for the beneficiaries, and how to supervise the usage of subsidies. The Hunan Provincial Education Department also issued a document in 2016 to regulate the supervision of the Program for Strengthening the Capacity of Weak Compulsory Education Schools. Every year, the provincial Education Department takes the lead in supervising the implementation of the program. Various methods are adopted including routine and dynamic monitoring, using third party evaluation, self-evaluation and field supervision. Though sampling is used for supervision and evaluation, in principle, supervision by the county education bureaus should cover every school under their administration. In turn, every county should be reviewed by the prefecture education bureau, and every prefecture should be supervised by the provincial Education Department. A summery supervision report is prepared by the provincial Education Department and released to the public. Local governments are required to take remedial action and report to the provincial Government within three months upon receiving feedback from the provincial Education Department. The summary supervision report carried out in 2017 was fairly positive and the achievement rate of the required activities was about 95 percent. However, some weaknesses were identified. Available funds were insufficient in meeting the demands of schools, a number of schools were not included in the program due to poor financial capacity of the county government, and delays occurred while waiting for approval of construction land.

Segregation of duties is prescribed throughout the expenditure process with responsibilities clearly defined for each level. Commitment control applies to all payments made from the TSA. Actual expenditures are in line with the approved budget and do not exceed commitment amounts or projected available cash resources. The disbursement system provides a safe mechanism for authentication and signature confirmation, which prevents unauthorized access to the database. Compliance with payment rules and procedures is high, and all exceptional expenditures are paid from a budget reserve fund.

Controls over budget execution are robust but heavily rely on a manual system. An internal control system is in place to control changes to the personnel payroll. The approval process maintains a task trail as each approver accesses the electronic treasury system using a unique password and identification number. Overall, good performance was observed in terms of integration of payroll and personnel records, management of payroll changes, internal control of payroll and payroll audit.

The internal controls over other aspects of budget execution also comprise a mix of traditional paper-based controls and the use of technology. Requests for non-salary expenditures are initiated by the spending units through paper-based forms, and then a set of complex internal review procedures are followed to verify the intention to procure, the purchase order, and the request for payment. Since the roles and responsibilities of various reviewers are not well defined in the government documents, some duplications were noted that jeopardize the efficiency of the internal control process. The Treasury performs ex-ante control of all payments using a checklist, to verify the required controls and compliance with various requirements (including procurement) are in place before releasing the funds.

Rules for investment project management have been issued in some counties. Infrastructure projects should be selected in accordance with the following procedures:

- The related sectors submit their application to the county investment project office (the office).
- The office reviews the applications after consulting with the sectors and reports the preliminary project list to the executive meeting of the county leaders.
- Once a final decision is made, the office formulates and publishes the annual plan for investment projects.

Detailed rules are provided also for the implementation of investment projects. The county investment project office is responsible for project monitoring and management. Weekly reports on both cost and physical progress are submitted to the office by each construction entity. Information on the implementation of investment projects is prepared annually but not published.

Verification of the achievement of DLIs will rely on an independent third-party verification agent (VA) through on-site review. A detailed verification protocol has been designed and is reflected in the PAD.

Internal control for procurement

For procurement following the TBL, daily procurement is under the supervision and oversight of the DRC and relevant sectoral government agencies at high level. For procurement following the GPL, daily procurement is under the supervision and oversight of the finance authority and relevant sectoral government agencies at high level.

In terms of procurement decisions, a procurement plan is prepared by the client. It is subject to clearance and approval by its supervision authority and the finance bureau. The qualification and evaluation criteria are set by the client in the issued bidding document. The contract award recommendation is made by the BEC on basis of these criteria. The decision for contract award cannot be overruled by the client. In case the decision for contract award needs to be revised, the BEC needs to re-convene.

With respect to the transparency and confidentiality of the procurement process, procurement is conducted via the platform of the public resources transaction center, if the contract value exceeds the specified threshold. This process is witnessed by staff of the transaction center and supervised by inspection staff from the relevant government agencies. The bid opening and evaluation are carried out at the center. If the procurement is processed outside the transaction center, the client's inspection staff and the staff from the DRC or local finance authority witness and supervise the bid opening and evaluation.

The agencies involved in the procurement process include the client, the procurement agent company, and the public resources transaction center. All agencies have clear mandates, a clear segregation of function, and clearly defined responsibilities for different units and staff. Ethical standards apply to all their staff when carrying out their daily work.

All procurement documents are kept for a specified time period. According to the TBL, procurement documents must be retained for at least ten years after completion of the procurement. According to the GPL, procurement documents must be kept for at least 15 years after completion of the procurement.

3.3.2 Internal audit

Internal audit practice complies with the Audit Law and the related regulations as issued by the China National Audit Office (CNAO). Article 3 of the CNAO Decree No. 11 of 2018 defines five types of internal audit: financial

revenue and expenditure audit, accountability audit, performance audit, audit of the implementation of key policies, and internal control and risk audit.

With Provincial Government Decree No. 255 of 2011, the Hunan Provincial Government issued the Hunan Provincial Internal Audit Measures, which require local governments and their administrative institutions to conduct internal audit in line with the prevailing regulations. The internal audit function has been established in the involved provincial departments. The institutional arrangements and responsibilities are listed in Table 14.

Table 14 - Institutional arrangements and responsibilities of provincial departments

Entity	Is a separate internal audit unit established?	Main responsibilities of internal audit unit	Do internal auditors audit project expenditures?
Provincial Finance Department	Yes	<ul style="list-style-type: none"> ▪ Responsible for establishing the internal control mechanism at the agency and responsible for the daily work of the internal control committee of the agency. ▪ Takes the lead in formulating and reviewing the internal control system and measures of the agency's organs. ▪ Organizes the implementation of special inspections, assessments and evaluations of internal control, and puts forward suggestions for handling existing problems. ▪ Guides the internal control of various offices and units at the agency. ▪ Responsible for system construction. ▪ Responsible for the internal supervision and inspection of the department. ▪ Implements internal supervision and inspection on the implementation of fiscal regulations, policies, systems, and budgets in various offices and units of the department. ▪ Occasionally reviews the funds of loan projects. 	Yes
Provincial Transport Department	Used to have a separate IA unit, but now merged with finance division	<ul style="list-style-type: none"> ▪ Conducts financial audit and accountability audit on its internal units and subordinates. ▪ Audits procurements and usage of government-owned assets. 	Yes

Provincial Education Department	Yes	<ul style="list-style-type: none"> ▪ Guides the internal audit of the province's education system. ▪ Carries out internal audit on the implementation of major party and state policies and measures, as well as financial revenue and expenditure, of the units directly under the department. ▪ Organizes internal audit investigations on regular economic activities and major fund management matters of the education system. 	Yes
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The county audit offices are responsible for the supervision of, and technical guidance on, the internal audit work conducted by the budgetary units. In the selected counties, most budgetary entities with subordinates have established an internal audit function. The main internal audit activities include financial audit, accountability audit, and performance audit. At times, a budgetary unit may hire an accounting firm to assist with the internal audit of its subordinates. As shown in Table 15, the coverage of internal audit in some counties is impressive.

Table 15 - Internal audit coverage in FY 2018

Item	Liuyang	Pingjiang	Rucheng	Guidong	Yizhang	Liling	Youxian	Chaling*
Expenditures	92.69%	96.20%	77.30%	81.70%	42.20%	35.30%	30.96%	N/A
Revenue		86.80%	100.00%	100.00%	100.00%			N/A

*In Chaling County, an internal audit function has been established in most budgetary units, however, the internal audit was not conducted in the time period assessed.

The internal audit work framework including internal audit procedures, audit methods, and audit quality control are guided by the Internal Audit Standards, the Code of Professional Ethics for Internal Auditors, and the Internal Audit Quality Evaluation Guidance, which are issued by the China Institute of Internal Audit (CIIA). The CIIA was founded in 1987 and has been a member of the Institute of Internal Auditors (IIA) since it was established.

Most budgetary units carry out internal audit on their internal entities and subordinates in accordance with the Internal Audit Standards issued by the CIIA, prepared internal audit reports, provided rectification suggestions, and received follow-up responses from the auditees. During FYs 2016-2018, most audited units took remedial action according to the internal auditors' recommendations within twelve months.

However, it was noted that not all budgetary units prepared an annual internal audit work plan for FY 2018. In addition, though related government entities issued some guidance and intended to improve the internal audit quality, an internal audit quality assurance process is not established in the selected counties.

3.3.3 Program governance and anticorruption arrangements

3.3.3.1 Complaints and reviews

Complaint Mechanism for Procurement following the TBL

Two tiers of complaint handling exist for procurement following the TBL. Under the first tier, the bidder can lodge any complaint to the client with a view to the bidding documents, the bid opening, or the contract award recommendation. The contract award recommendation is required to be disclosed for at least three calendar days. Any complaint regarding the contract award recommendation must be submitted within this standstill period. The client is required to respond to the complaint within three calendar days.

Under the second tier, the bidder can lodge any complaint to the relevant supervision authority regarding the bidding documents, the bid opening, the contract award recommendation, or other non-compliance of the procurement process with the relevant laws, rules, and regulations within ten calendar days from his/her awareness of the issue. Within three working days, the supervision authority shall determine whether the complaint is valid. If the complaint is determined valid, within 30 working days, the supervision authority shall issue its written judgement and determination. If the complainant is not satisfied with the resolution, the complainant is entitled to request an administrative review by an HLG office or administrative litigation.

Complaint Mechanism for Procurement following the GPL

Similarly, for procurement under the GPL, there exist two tiers of complaint handling. Under the first tier, the bidder can lodge any complaint to the client regarding the bidding documents, the procurement processing, the contract award recommendation, or other non-compliance of the procurement processing with relevant laws, rules, and regulations within seven working days from his/her awareness of the issue. The client is required to respond to the complaint within seven working days.

Under the second tier, if the bidder is not satisfied with the response from the client or if the client does not respond within the required time, the bidder can lodge any complaint to the relevant supervision authority regarding the bidding documents, the bid opening, the contract award recommendation, or other non-compliance of the procurement processing with relevant laws, rules, and regulations within 15 working days after receiving the response from the client or after expiry of the required responding time, as the case is applicable. Within 30 working days, the supervision authority must issue its written judgment and determination. If the bidder is not satisfied with the determination made by the supervision authority or if the supervision government authority does not make its determination within the required time, the bidder can refer the matter to a high-level administrative review or invoke administrative litigation.

During the fiduciary assessment, information was collected about the complaints received in the past three years. The data are summarized in Table 16. All complaints are normally responded to within time, as specified by the TBL or GPL and the applying implementing regulations.

Table 16 - Complaints received

County	Implementation agency	Total number of contracts			Number of 1 st tier complaints			Number of 2 nd tier complaints		
		2016	2017	2018	2016	2017	2018	2016	2017	2018
Liuyang	Public Works Construction Center	48	54	50	1	1	1	1	0	0
	Education Bureau	151	229	153	1	0	0	0	0	0

	Highway Construction & Maintenance Center	20	9	19	0	0	0	0	0	0
Pingjiang	Public Works Construction Center	17	33	4	0	0	0	0	0	0
	Education Bureau	70	100	104	0	0	0	0	0	0
	Transport Bureau	43	67	30	0	0	0	0	0	0
Rucheng	Public Works Construction Center	135	290	383	2	3	3	0	0	0
	Education Bureau	24	37	25	0	0	0	0	0	0
	Highway Construction & Maintenance Center	0	3	5	0	0	0	0	0	0
Guidong	Development & Reform Bureau	39	23	10	0	0	0	0	0	0
	Education Bureau	44	43	44	0	0	0	0	0	0
	Highway Construction & Maintenance Center	8	8	4	0	0	0	0	0	0
Yizhang	Public Works Construction Center	86	108	44	0	0	0	0	0	0
	Education Bureau	45	82	88	0	0	0	0	0	0
	Highway Construction & Maintenance Center	110	150	165	0	0	0	0	0	0
Youxian	Public Works Construction Center	275	321	242	0	0	0	0	0	0
	Education Bureau	155	192	195	0	0	0	0	0	0
	Highway Construction & Maintenance Center	7	10	6	0	0	0	0	0	0
Liling	Housing & Urban-rural Development Bureau	21	104	40	0	1	6	0	0	1
	Education Bureau	79	82	117	0	0	0	0	0	0
	Transport Bureau	5	15	17	0	0	0	0	0	0
Chaling	Public Works Construction Center	224	526	195	1	2	2	1	2	2
	Education Bureau	1	9	8	0	0	1	0	0	0
	Highway Construction & Maintenance Center	0	3	7	0	0	0	0	0	0

3.3.3.2 Compliance with the Anti-Corruption Guidelines

The Chinese Government has put multiple institutions in place to combat fraud and corruption. They are designed to prevent, report, detect, investigate, prosecute, and sanction fraud and corruption. First, within all implementation agencies involved in procurement, so-called discipline inspection commissions are in place that directly report to the discipline inspection commissions attached to higher-level supervision agencies. Second, there is the Ministry of Supervision at the central level with supervision bureaus at the provincial, prefectural, and county levels. Third, under the Chinese People's Procuratorate, anti-corruption bureaus have been set up at central, provincial, prefectural, and county level. Fourth, audit offices exist at central, provincial, prefectural, and county level, and all agencies involved in procurement are subject to an annual external

independent audit. All these agencies have comprehensive mandates to combat fraud and corruption while carrying out procurement. Any bidder or any party can report fraud and corruption issues to any of these government agencies.

Still, the Bank may not be informed of fraud and corruption allegations during implementation of the Program. The Program manual will therefore require the client to regularly inform the Bank of any credible and material allegations of fraud and corruption in the Program progress report, as required in the loan agreement.

The Bank's right to conduct an inquiry into such allegations or other indications, independently of or in collaboration with the Borrower, regarding activities and expenditures supported by the Program, as well as its right to access to the required persons, information, and documents will be observed in accordance with the standard arrangements between the Government of the PRC and the Vice Presidency Integrity Department ('INT') of the Bank.

Procurement will be implemented by the implementation agency as established by each county, with assistance from the procurement agent company. These parties may not have knowledge of the firms and individuals debarred and temporarily suspended by the World Bank and other multilateral development banks. Therefore, there is a potential risk that contracts may be awarded to ineligible firms or individuals. The proposed mitigation actions are: (a) The Hunan Province Department of Finance shall, upon project loan effectiveness, issue a high-level official letter or official instruction to the implementation agencies to ensure that no contract will be awarded to ineligible firms or individuals. (b) Procurement staff at the Hunan Provincial Department of Finance will check the latest lists of debarred and temporarily suspended firms and individuals on a daily basis and share them with all implementation agencies. (c) the TOR for annual external audit includes the task of randomly selecting awarded contracts to check whether they have been awarded to ineligible firms or individuals.

3.4 Auditing

Hunan Province and its counties receive various external audits and inspections throughout the year, primarily focusing on the proper usage of public funds. The annual external audit findings on budget execution by the PAO are included in its annual report to the Provincial People's Congress, and the full audit report is published on the PAO official website. However, due to manpower shortage at the audit offices, not every budgetary unit is audited yearly. The audit strategy for government auditors is to conduct audit on a rolling basis, and for audit to cover multiple years.

The audit bureaus in the selected counties carry out audit and have access to the necessary data without any restriction. A number of material issues and systemic and control risks are usually detected and disclosed in the audit reports, and remedial action is taken by the audited units effectively and timely. The audit bureaus submit their audit reports to the legislature in a timely manner, after receiving the financial reports. The standing committees of the county people's congresses provide timely approval of the audit reports and call for in-depth hearings on the main findings of the audit reports once a year. Most of the audited entities with issues disclosed in the audit reports participate in the hearing. The standing committees follow up and conduct hearings on the rectification taken by the auditees.

For FYs 2016-2018, most budget expenditures were audited in some of the selected eight counties, but external audit coverage was low in others (see Table 17). The audit quality of the county audit bureaus is subject to the supervision and control of the Hunan PAO, in accordance with the Audit Law of the PRC.

Table 17 - External audit coverage, FYs 2016-2018

County	Liuyang	Pingjiang	Rucheng	Guidong*	Yizhang	Liling	Youxian	Chaling
Expenditures	95.27%	40.00%	19.70%	0.00%	9.30%	56.07%	64.97%	71.54%

*In Guidong County, the budget expenditures of 14 public service units selected were not audited for FYs 2016-2018. Instead, the county audit office paid its attention to special purpose vehicles and accountability audit.

The audit reports on budget execution for FY 2018 prepared by the PAO and eight county audit bureaus show that the Government's financial capacity continues to be strengthened and budget expenditures associated with people's livelihoods, such as poverty alleviation, ecological protection, and education, has increased steadily. Fiscal and taxation reforms continue to deepen. The provincial department has issued a series of measures to prevent and resolve government debt risks, strengthen government debt management, and implement the requirements of the People's Congress budget review and supervision to focus on expenditure budgets and policy expansion. In addition, the effectiveness of rectification has continuously improved. However, the following weaknesses and issues have been disclosed in the audit reports:

Table 18 – Main findings disclosed by external auditors, FY 2018

Entity	Findings
Hunan Province	<ol style="list-style-type: none"> 1. Some units' budgets are not standardized. Observed problems include under-editing and less budget adjustments, detailed budget adjustments, unscientific budget additions, high additional rates, and unreasonable arrangements. 2. Budget implementation is not taking place properly. Budget execution rates are low, release of funds is not timely, and the proportion of advance transfer payments to cities and counties is low. 3. FM is not strict. The official card settlement system is insufficiently implemented. Accounts are not cleaned in a timely manner. Expenditure arrangements face irregularity issues. The management of special funds is inadequate. System construction is lagging behind. incomplete integration, and irregular distribution; 4. Final accounts drafting is inaccurate. Problems include the underestimation of income, multiple expenditures, and the improper presentation of subjects or levels. <p>In the process of auditing the budgets of provincial departments, it was found that some provincial-level units show signs of inaccurate budget preparation, inadequate budget revenue collection and management, non-compliance of budget expenditures, poor performance of fund use, and insufficient cleaning of bank accounts and existing funds. Other issues include irregular purchases, non-compliant asset management, rigorous FM, and inadequate implementation of policies and systems, relying on departmental fees or profit.</p>
Liuyang City	<ol style="list-style-type: none"> 1. Some budget management is not comprehensive and standardized. 2. Some revenues are not collected timely.

	<ol style="list-style-type: none"> 3. Approved budgets are not executed properly by some budgetary units. 4. The final accounts are not standardized. 5. Comprehensive FM is not in place. 6. Ear-marked funds are mis-appropriated in some budgetary units. 7. Budget funds are not used efficiently. 8. Government procurement is not conducted in line with the required procedures. 9. Control of settlement of receivables and payables is weak.
Pingjiang County	<ol style="list-style-type: none"> 1. The project expenditure budget is not prepared scientifically. 2. Budget revenue is not released timely. 3. The ear-marked transfer funds are not delivered to the budgetary units timely. 4. Social security payment to farmers whose land is expropriated is not accounted in their individual accounts timely. 5. Some budget funds carried forward from previous years are not settled timely.
Rucheng County	<ol style="list-style-type: none"> 1. Some non-tax revenues are not turned in to the treasury. 2. Some funds are not recorded in the general budget. 3. Budget funds are lent to non-budgetary units. 4. Account receivables and payables are not settled timely. 5. Some revenues are not stable and under the pressure of balancing budget revenue and expenditures.
Guidong County	<ol style="list-style-type: none"> 1. Budget preparation needs to be further standardized. 2. Actual reserved funds far exceed the approved budget. 3. Some savings are not returned to the treasury. 4. Some ear-marked transfer funds are not distributed timely. 5. Budget execution is not balanced. 6. Expenditures are recorded as receivables. 7. Land use funds are not paid timely. 8. Account receivables and payables are not settled timely.
Yizhang County	<ol style="list-style-type: none"> 1. Budget preparation is incomplete. 2. Gaps exist between the budget and final accounts for some revenues. 3. Some budget funds are retained at the county finance bureau and not specified for budgetary units and projects. 4. The approval rate of government funds is low. 5. Some revenues are not turned in to the treasury timely. 6. The usage of reserve funds is not in line with the requirements. 7. Some borrowing funds are not collected timely. 8. Some expenditures are not documented for several years.
Liling County	<ol style="list-style-type: none"> 1. Some tax and non-tax revenues are not turned in to the treasury timely. 2. Some receivables are not collected timely. 3. Cash is used to pay for large expenditure amounts. 4. Expenditures of three budgetary units are not included in single treasure payment system. 5. Some training expenses are not recorded under the proper budget items. 6. Transferred funds from HLGs are not delivered timely.
Youxian County	<ol style="list-style-type: none"> 1. Some budget quota for transfer funds are not recorded in the management system. 2. Budget quota are not distributed to budgetary units timely.

	<ol style="list-style-type: none"> 3. Some savings are not returned timely. 4. Some non-tax revenues are not turned in timely. 5. Regulations on lending budget funds are violated. 6. Some budget funds are not used for the intended purpose. 7. Some problems occur with procurement, such as that contract packages are split and bid securities to bidders are not returned.
Chaling County	<ol style="list-style-type: none"> 1. Government funds are not used in line with requirements. 2. Some expenditures are not properly recorded as budget items. 3. Some budget funds are not delivered in line with requirements. 4. Budget management is weak. For instance, the budget for government capital is not prepared correctly, and lots of savings of transferred funds to township and villages. 5. Revenue from the sale of state-owned land is not collected timely. 6. Budget funds are lent to non-budgetary entities. 7. Some non-tax revenues are not turned in to the treasury timely. 8. Subsidies to farmers are retained. 9. In two units, expenditures were made without the approved budget.

The Hunan Provincial Government has issued some documents to strengthen the follow-up on issues disclosed by government auditors and required the audited units to take corresponding remedial action. In FYs 2016-2018, the majority of audited budgetary units in the selected counties took follow-up actions effectively and timely, and submitted the rectification report to the county audit offices. The standing committees of the respective county people's congress systematically followed up on the rectification of the issues disclosed in the audit reports. Both the annual audit reports on budget execution and the summarized reports on follow-up actions were published on the county government websites in most project counties.

Audit of the proposed Program will be conducted by the Hunan PAO. Besides conducting the audit on budget execution and other provincial level entities, the PAO has been the auditor of Bank financed projects in Hunan province for about two decades. It is one of the auditors the Bank accepted in China. The first year's audit report issued by the PAO will be subject to a quality review by the CNAO.

To gain reasonable assurance on the proper usage of Program funds, the CNAO and the PAO will agree with the Bank on audit TOR and conduct annual Program financial statement audits that will be publicly disclosed. The CNAO and the PAO will adopt the audit approach and coordination mechanisms used in other Bank-financed PforR operations. The PAO will coordinate internally to minimize the chances of duplicate audits conducted by different auditors, and to maximize reliance on each other's findings. The auditors will conduct the financial audit on the PforR financial statements in accordance with the audit TOR to meet the Bank's audit requirements. The audit report will be submitted to the Bank within nine months of the end of the calendar year. It has been agreed that the Program audit would focus on the following aspects:

- Whether the transfers from central and provincial governments have been delivered to the counties timely and completely.
- Whether the stipulated verification procedures and requirements are fully complied with by the related entities.
- Whether the Program funds are used properly and in line with the applying regulations and procedures, by sampling of Program counties.

External audit for procurement

As mentioned, the agencies involved in procurement include the client, the procurement agent company, and the public resources transaction center. All these agencies are subject to annual external audit. In addition, there are external project-specific audits for each project. During the project implementation period, the projects are selected randomly for project-specific annual external audit. Upon completion, each project is subject to an external project-specific audit. The audit not only covers the bidding process, but also contract implementation, including an assessment of whether proper procedures have been followed for the issuance of variations, whether these variations are reasonable, whether unauthorized sub-contracting or assignment of the whole contract to third parties has taken place, whether the payment paid to the contractor/supplier/consultant corresponds with the actual progress of works/goods delivery/service delivery, whether there are payment delays, etc..

3.5 Procurement and FM capacity

A steering committee has been established in Hunan Province comprising representatives from the provincial Finance Department, DRC, Transport Department, Education Department and Administrative Services Bureau. A project management office has been set up at the provincial Finance Department.

The Hunan Provincial Finance Department is responsible for coordinating and supervising the preparation and implementation of the proposed PforR operation. Besides managing the disbursement of many Bank-financed projects in Hunan Province, the provincial Finance Department also implemented a development policy operation (DPO) financed by the Bank with a total loan amount of USD 200 million. The Department is not only capable of managing projects by international financial institutions (IFIs), but also shows strong support for the proposed Program. During the PEFA assessment in eight counties, it was observed that most county staff is familiar with the operation, including the required internal control procedures, the reporting process, annual budget preparation and implementation, etc. All necessary documents including a copy of each appropriation circular, and all regulatory documents issued by the provincial, municipal, and county governments are systematically filed.

The parties involved in procurement normally include the implementation agency, the procurement agent company and the design institute. Both the procurement agent company and the design institute are professional firms which possess sufficient human resources with the needed expertise, skills and experience. The implementation agencies have adequate experience in conducting the procurement and contract implementation. The procurement portfolios managed by the implementation agencies in the past three years are shown in Table 19.

Table 19 - Contracts procured in FYs 2016-2018

Country	Implementation agency	Category	Total number of contracts			Total contract value (RMB 10,000)		
			2016	2017	2018	2016	2017	2018
Liuyang	Public Works Construction Center	Works	42	42	38	24,446	109,421	24,004
		Goods	1	4	8	58	389	1,653
		Services	5	8	4	287	947	764
	Education Bureau	Works	57	86	37	7,926	13,524	4,882
		Goods	37	57	79	4,623.15	4,083.25	5,235.13

		Services	57	86	37	634	1,080	390
	Highway Construction & Maintenance Center	Works	14	8	14	28,478.08	8,242.17	11,928.28
		Goods	2	0	1	514.977	0	149.39
		Services	4	1	4	285.92	43.61	188.34
Pingjiang	Public Works Construction Center	Works	17	33	4	317,479	201,412	36,047
		Goods	0	0	0	0	0	0
		Services	0	0	0	0	0	0
	Education Bureau	Works	35	50	52	8,926	17,066	21,499
		Goods	0	0	0	0	0	0
		Services	35	50	52	1,264	3,755	4,288
	Transport Bureau	Works	6	27	8	4,460	35,699.09	6,932.46
		Goods	0	0	0	0	0	0
		Services	37	40	22	1,060.80	1,143.6	333.73
Rucheng	Public Works Construction Center	Works	3	140	285	172.7	13,788.77	34,971.38
		Goods	106	106	66	24,269.23	10,440.36	8,031.86
		Services	26	44	32	1,285.57	1,448.22	1,653.05
	Education Bureau	Works	1	18	10	59.16	1,787.05	1,112.43
		Goods	12	18	15	2,682.18	2,272.11	2,330.63
		Services	1	1	0	42.5	27.93	0
	Highway Construction & Maintenance Center	Works	0	3	4	0	384.43	4,358.92
		Goods	0	0	1	0	0	1,240.56
		Services	0	0	0	0	0	0
Guidong	Development & Reform Bureau	Works	27	20	6	154,291	40,598	15,560
		Goods	0	0	0	0	0	0
		Services	12	3	4	1,825	176	349
	Education Bureau	Works	7	7	6	1,861.97	2,568.61	1,336.58
		Goods	14	12	16	2,516.54	655.79	3,574.69
		Services	23	24	22	56.33	82.36	44
	Highway Construction & Maintenance Center	Works	4	4	2	1,179.28	839.92	294.1
		Goods	0	0	0	0	0	0
		Services	4	4	2	47.16	33.21	11.85
Yizhang	Public Works Construction Center	Works	84	98	34	93,856.49	137,696	43,795.46
		Goods	0	0	0	0	0	0
		Services	2	10	10	195	1,513.09	642.17
	Education Bureau	Works	32	66	23	1,677	10,679	1,674
		Goods	11	12	52	204	339	5,757
		Services	2	4	13	34	149	691
	Highway Construction & Maintenance Center	Works	31	55	45	1,700	2,992	42,688
		Goods	0	0	0	0	0	0
		Services	79	95	120	260	350	1,800

Youxian	Public Works Construction Center	Works	99	166	80	78,874	189,600	62,000
		Goods	86	90	85	6,121	11,402	9,994
		Services	90	65	77	9,348	15,633	11,739
	Education Bureau	Works	63	82	91	11,000	13,000	18,000
		Goods	28	36	40	4,000	5,500	7,000
		Services	64	74	64	400	50	550
	Highway Construction & Maintenance Center	Works	3	3	2	496.1	1,556.54	2,194.75
		Goods	0	0	0	0	0	0
		Services	4	7	4	138.6	57.38	66.08
Liling	Housing & Urban-rural Development Bureau	Works	13	84	28	55,390.28	228,673.46	107,666.4
		Goods	1	4	1	230	878.81	519.18
		Services	7	16	11	1,080	2,460.26	6,037.51
	Education Bureau	Works	52	46	72	7,672.2	8631.3	1,1681.2
		Goods	25	34	42	1,405.68	1,796.54	1,812.3
		Services	2	2	3	15.6	15.6	50.85
	Transport Bureau	Works	5	7	15	3,484.80	9,038.23	10,946
		Goods	0	8	2	0	2,990.33	675.90
		Services	0	0	0	0	0	0
Chaling	Public Works Construction Center	Works	70	360	28	9,774	48,657	6,333
		Goods	129	142	141	17,729	40,956	48,885
		Services	25	24	26	304,834	182,038	2,469
	Education Bureau	Works	1	6	7	137.84	3,184.60	5,860.72
		Goods	0	1	0	0	94.86	0
		Services	0	2	1	0	55.98	30
	Highway Construction & Maintenance Center	Works	0	1	5	0	1,163.75	4,637.38
		Goods	0	0	0	0	0	0
		Services	5	0	2	0	16.8	88.35

Based on an assessment of the performance information and institutional arrangements, the fiduciary systems adopted have enough capabilities to ensure the successful implementation of the Program and the achievement of its development objectives.

SECTION 4: PROGRAM SYSTEMS AND CAPACITY IMPROVEMENTS

The overall fiduciary risk of the envisaged PforR operation is rated as 'moderate' given the proper implementation of the proposed mitigation measures:

Table 20 – Program system risks and mitigation measures

Risk	Mitigation action	Timing	Type of action (PAP, DLI, etc.)
The contracts may be awarded to firms or	<ul style="list-style-type: none"> ▪ The Hunan Province Department of Finance shall, upon project loan 	Implementation	PAP

<p>individuals which are debarred or under temporary suspension by the Bank or other multilateral development banks.</p>	<p>effectiveness, issue a high-level official letter or official instruction to implementation agencies to ensure that no contract will be awarded to ineligible firms or individuals.</p> <ul style="list-style-type: none"> ▪ One of the duties of the procurement staff at the Hunan Provincial Department of Finance will be to check the latest lists of the debarred and temporarily suspended firms and individuals on a daily basis and share them with all implementation agencies. ▪ The TOR for annual external audit include the task of randomly selecting awarded contracts on to check whether they have been awarded to ineligible firms or individuals. 		
<p>The Bank may not be informed of any credible and material allegations of fraud and corruption during the implementation of the Program.</p>	<ul style="list-style-type: none"> ▪ The Program manual will require the client to regularly inform the Bank of any credible and material allegations of fraud and corruption in the Program progress report, as required in the loan agreement. 	Implementation	PAP
<p>Great variation between budgeted and actual expenditures and revenues exist due to the unpredictability of HLG transfers. This indicates that budget reliability in selected counties is weak. In addition, multiple-year program budgets are not prepared by county governments.</p>	<ul style="list-style-type: none"> ▪ A DLI associated with enhancing the predictability of HLG transfers to the eight Program counties is agreed and a guideline for improving transfer predictability will be issued by Hunan Province in FY 2020. ▪ DLIs on performance-based funds transfer for rural transport and compulsory education have been established and the transfer funds from HLGs will be distributed to the Program counties based on output rather than input so the county is incentivized to prioritize its investment and the counterpart funds will be delivered to Program activities as committed. 	Implementation	DLI-2, DLI-5 and DLI-7
<p>‘Program’ is no budget classification element in China and the required Program financial reporting cannot be generated from the government treasury system.</p>	<ul style="list-style-type: none"> ▪ By referring to the experiences of other PforR operations in China, a tailored format for Program financial reporting shall be designed and agreed on by the Bank and the provincial Finance Department. 	Implementation	PAP

<p>Government auditors do not audit proposed program funds or prepare program audit reports. Though Program boundaries have been narrowed down to three sectors, many activities are included in the proposed Program and this poses a challenge to auditors when planning Program audit.</p>	<ul style="list-style-type: none"> ▪ To gain reasonable assurance on the proper usage of Program funds, the Bank will work with the Hunan PAO and agree on audit TOR to help coordinate Program audit. 	<p>Implementation</p>	<p>PAP</p>
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SECTION 5: PROGRAM IMPLEMENTATION SUPPORT

During Program implementation, the proposed fiduciary implementation support includes:

- Work with the team to review Program implementation progress, including the achievement of Program results and implementation of the PAP.
- Work with the team to assess timeliness and adequacy of Program fund appropriation as approved in the budget.
- Continuously assess and monitor the performance of the FM and procurement systems under the Program and provide suggestions for enhanced efficiency and effectiveness.
- Monitor application of the PforR anti-corruption guidelines.
- Monitor the performance of the fiduciary systems and the audit report, including the implementation of the PAP.
- Monitor the PforR financial statement reporting process and assist the client as necessary.
- Help the client resolve implementation issues and carry out institutional capacity building;
- Assist CNAO and the audit offices at provincial and county level in strengthening audit arrangements.
- Hold regular trainings for provincial and county audit offices, particularly with respect to procurement post audit to build capacity.
- Monitor changes in fiduciary risks of the Program and, as relevant, compliance with the fiduciary provisions of legal covenants.