

# REPORT ON THE OBSERVANCE OF STANDARDS AND CODES (ROSC) Lao PDR

**ACCOUNTING AND AUDITING**  
**January 7, 2009**

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## EXECUTIVE SUMMARY

This report provides an assessment of accounting and auditing practices within the corporate sector in Lao PDR with reference to the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), and the International Standards on Auditing (ISA) issued by the International Federation of Accountants (IFAC). This assessment is positioned within the broader context of the Lao PDR's institutional framework and capacity needed to ensure the quality of corporate financial reporting

Since 1992, Lao PDR has utilized the Lao Accounting System that requires the submission of a completed chart of accounts to the Taxation Department of the Ministry of Finance. In practice, most of these financial statements are not audited. There is no effective system of auditor certification or licensing in Lao PDR. New accounting and audit laws have recently been approved in order to enable the future introduction of updated Lao accounting and audit standards; however, these laws are currently descriptive in nature and require clarification. The Ministry of Finance sets accounting and audit standards in Lao PDR but lacks any real technical capacity to manage this responsibility.

The Lao Institute of Certified Public Accountants (LICPA) lacks any capacity to operate effectively, and there is no system of oversight of auditors or accountants practicing in Lao PDR. The LICPA does operate a CPA certification scheme, but this program falls short of compliance with IFAC International Education Standards. No university in Lao PDR provides a specific accountancy degree program. In effect, there is a lack of provision of required accountancy training and skilled local professionals.

The audits of public interest entities are primarily carried out by representatives of the major international networks. The lack of senior local staff and lack of understanding of the local environment within those organizations is of concern particularly as regulators lack any capacity to monitor the quality of financial reporting.

A significant strengthening exercise is required if Lao PDR is to create a strong corporate financial reporting infrastructure. The policy recommendations are aimed at Lao PDR authorities for consideration. These principle-based policy recommendations include strengthening the statutory framework, strengthening monitoring and enforcement mechanism, upgrading academic and professional education and training, instituting an arrangement for independent oversight of auditing profession, capacity building of regulators and the professional body, adopting full IFRS and ISA, upgrading the licensing procedures for accountants and auditors in practice, introducing a Lao PDR professional qualification examination with focus on adequate level of practical training, issuing and disseminating implementation guidance on applicable standards, enhancing the delivery of continuing professional education, and ensuring adherence to code of ethics. Considering the limited capacity of Lao PDR institutions, the recommendations are premised to require the support of international partners, to help promote a gradual and continuing process of improvement.

## PREFACE

There is a broad agreement among members of the international financial community that the observance of international standards and codes is pivotal in strengthening national and international financial architecture. In a world of integrated capital markets, financial crises in individual countries can imperil international financial stability. At the global level, international standards enhance transparency. They help to better identify weaknesses that could contribute to economic and financial vulnerability, foster market efficiency and discipline, and ultimately contribute to a global economy that is more robust and less prone to crisis. At the national level, international standards provide a benchmark that can help identify vulnerabilities as well as guide policy reform. To best serve these objectives, however, the scope and application of such standards need to be assessed in the context of a country's overall development strategy and tailored to individual country circumstances.

Following the international financial crises of the 1990s, the international financial community recognized the real need to assess the degree to which a country observes internationally recognized standards and codes. The World Bank and the International Monetary Fund (IMF) instituted *Reports on the Observance of Standards and Codes (ROSC)* that assess key areas in a country's economic well-being—accounting and auditing, anti-money laundering and combating the financing of terrorism, banking supervision, corporate governance, data dissemination, fiscal transparency, insolvency and creditor rights, insurance supervision, monetary and fiscal policy transparency, payments system, and securities regulation.

The ROSC Accounting & Auditing review focuses on the institutional framework regulating the accounting and auditing practices, comparability of national accounting and auditing practices with international standards and good practices using International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA) as benchmarks, and evaluates the effectiveness of enforcement mechanisms for ensuring compliance with applicable standards and codes.

This ROSC Accounting and Auditing review was carried out in active collaboration with the Government of Lao PDR through the Department of Accounting of the Ministry of Finance, and with assistance of stakeholders including the Accounting Council, Lao Institute of Certified Public Accountants (LICPA), and the Bank of Lao PDR. It included discussions with representatives of the profession, banks, insurance companies, corporate entities, state-owned enterprises, audit firms, academia, and various other knowledgeable individuals. The Ministry of Finance guided and facilitated the ROSC review exercise.

The review benefited from inputs and suggestions from peer reviewers: Richard L. Symonds, Sr. Counsel, LEGPS; Thomas A. Rose, Adviser, EASFP; Manoj Jain, Sr. Financial Management Specialist, SARFM; Jennifer K Thomson, Sr. Financial Management Specialist, EAPCO; and Russell Guthrie, Director, Quality Assurance and Member Body Relations, IFAC. The report was prepared by a team comprising M. Zubaidur Rahman, Program Manager, OPCFM; Donald Mphande, Sr. Financial Management Specialist, EAPCO; and Neil Wallace, Consultant.

## ABBREVIATIONS AND ACRONYMS

AFA	Asean Federation of Accountants
BOL	Bank of Lao PDR PDR
CPA	Certified Public Accountant
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
IASCF	International Accounting Standards Committee Foundation
IES	International Education Standard
IFAC	International Federation of Accountants
IFRIC	International Financial Reporting Interpretation Committee
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
ISA	International Standard on Auditing
LAS	Lao Accounting System
LICPA	Lao Institute of Certified Public Accountants
MOF	Ministry of Finance of Lao PDR
NGO	Nongovernmental organization
ROSC	Reports on the Observance of Standards and Codes
SOE	State-owned enterprise

## I. INTRODUCTION

1. **This assessment of accounting and auditing practices in Lao PDR is part of a joint initiative of the World Bank and the International Monetary Fund (IMF) to prepare *Reports on the Observance of Standards and Codes (ROSC)*.** The assessment focuses on the strengths and weaknesses of the accounting and auditing environment that influence the quality of corporate financial reporting and involves a review of both mandatory requirements and actual practice. It uses International Financial Reporting Standards (IFRS)<sup>1</sup> and International Standards on Auditing (ISA)<sup>2</sup> as benchmarks and draws on international experience and good practices in the field of accounting and audit regulation. The assessment uses a diagnostic template developed by the World Bank to facilitate collection of data. The data is complemented by the findings of a due diligence exercise based on a series of meetings with key stakeholders conducted by World Bank staff. The intended audience of the ROSC includes national and international market participants with an interest in the corporate financial reporting regime of Lao PDR. An overview of the ROSC Accounting and Auditing and the detailed presentation of methodologies are available in the World Bank Group website.<sup>3</sup>

2. **Development.** Lao PDR is a small, predominantly rural country of 5.9 million people. It has a gross national income per capita of US\$630.<sup>4</sup> Lao PDR has maintained relatively stable macroeconomic conditions; its economy continues to grow, but at a relatively slower pace as the impacts of the global financial turmoil are starting to be felt—real GDP growth slowed in 2008 to about 7 percent, and projection for 2009 is between 5 and 7 percent. The country is making progress on its Millennium Development Goals and on reforms.<sup>5</sup> The macroeconomic conditions of Lao PDR remain relatively stable, reflecting improved monetary and fiscal discipline, with inflation in single digits for the last several years, public expenditures under control, and the fiscal situation steadily improving. The poverty headcount fell further from 33 percent in 2002/2003 to 31 percent in 2005/2006. The Government has accelerated reforms across several areas, including public financial management, trade and private sector development, governance and anti-corruption, and natural resources management. The overall competitiveness of the agriculture and manufacturing sectors is relatively weak, hampering the capacity of the economy to generate employment and ensure broad-based improvement in living standards. Due to the current global financial crisis, the economy is facing a number of challenges that feed through a projected decline in foreign direct investment, commodity prices, potential private sector credit constraints, and declining exports. The economic downturn in industrialized world gives Lao PDR more urgency to

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<sup>1</sup> IFRS correspond to the pronouncements issued by the International Accounting Standards Board (IASB) and to International Accounting Standards (IAS) issued by its predecessor, the International Accounting Standards Committee (IASC), as well as related official interpretations. References in the ROSC to IFRS also include IAS.

<sup>2</sup> ISA are issued by the International Auditing and Assurance Standards Board (IAASB) within the International Federation of Accountants (IFAC).

<sup>3</sup> Access ROSC Accounting and Auditing at [www.worldbank.org/ifa/rosc\\_aa.html](http://www.worldbank.org/ifa/rosc_aa.html).

<sup>4</sup> Data from [Lao PDR Economic Monitor](#), The World Bank Office, Vientiane—November 2008.

<sup>5</sup> *Country Assistance Strategy Progress Report for Lao PDR*, World Bank, 2007.

several areas of ongoing structural reforms, aimed at increasing revenues and at improving the investment climate.

3. **Capital markets.** There are no capital markets in Lao PDR. Proper development of a capital market requires appropriate legal and accounting infrastructure, necessary regulatory and institutional structures, and human resource capacity. A draft decree on the creation of a Stock Exchange has been prepared with the intention of it opening in 2010. An ad hoc Working Group which includes the Ministry of Finance and Bank of Lao PDR has been established to steer this process.

## II. INSTITUTIONAL FRAMEWORK

### A. Statutory Framework

4. This section outlines the legal principles applicable with regard to accounting, auditing, and financial reporting and an introduction to issues concerning the institutional framework.

5. **There are inconsistencies between the Enterprise Law, the Audit Law, and the Accountancy Law.** Basic requirements for accounting, financial reporting, and auditing in Lao PDR are set out in the Enterprise Law 2005. The Accounting Law was passed by the National Assembly in 2007 and will come into effect in 2009. The Audit Law came into effect in 2007. The inconsistencies arise in the Enterprise Law Article 154 that states an auditor may be a shareholder of a limited company whereas under the Audit Law this is now prohibited. The Enterprise law has a requirement for the audit of financial statements of public companies and limited companies according to the amount of registered capital; whereas the Tax law does not have a comparable audit requirement. The Accounting and Audit Laws both do however state that "all regulations and rules which go against this present Law are repealed."

6. **The Enterprise Law regulates business activities in Lao PDR.** The Law recognizes four types of business entities:

- *Ordinary partnership* where business is conducted jointly by partners and where all partners have unlimited responsibility for the enterprise's liability.
- *Limited partnership* is formed under an agreement between 2 or more parties for the purpose of conducting business under a joint name. Designated partners have unlimited responsibility for the enterprise's liability, called "general partners" while other designated partners with limited liability are called "limited partners."
- *Limited companies* have at least 2 shareholders but not exceeding 30 persons.
- *Public companies* are required to have at least 9 founding shareholders. There is free transferability of shares and entitlement to openly sell shares.

7. **The Government of Lao PDR deserves credit for introducing new accounting and auditing laws in 2007, which attempted to adopt a number of international**

**“like” standards.** However, these laws and related regulations do not provide a robust statutory framework in the area of accounting and auditing. In many cases the laws appear to be indistinct and do not cover pertinent crucial issues, thus leaving room for misinterpretation. The Audit Law lacks clarity on audit certification and licensing requirements and also lacks clarity on auditor appointment and removal as well as auditors’ rights and duties. The Accounting Law includes much descriptive type narrative and attempts to outline much of the qualitative characteristics of IFRS. Likely update and revision of IFRS will necessitate revision of the Accounting Law. For example, the IASB is consulting on the development of a revised Conceptual Framework. Any revision would require amendment to Article 5 of the Accounting Law.

**8. Lao PDR is seeking to establish a strong corporate financial reporting regime with intention of introducing IFRS-based accounting standards as national standards in the near future.** In order for this to be possible, there must be significant strengthening of capacity at all relevant institutions including the Ministry of Finance (MOF) Accounting Department, the Accounting Council, and the Lao Institute of Certified Public Accountants (LICPA). There must also be considerable strengthening of accountancy training at both academic and professional levels.

**9. The Accounting Law, Article 14, requires that annual financial statements should be submitted to the registry office of companies.** In practice, except for banks and insurance companies, annual financial statements are submitted by companies solely to the Taxation Department of the Ministry of Finance. Financial statements submitted to the Taxation Department are not available to the public and, in practice, are not subject to external audit. Due to unavailability of financial statements, it is difficult for public users and potential investors to compare the quality of financial statements and assess the financial standing of a given enterprise thereby limiting informed decision-making. Furthermore, it is an impediment to transparency in the corporate sector and can have detrimental effects on the country’s investment climate.

**10. Lao PDR should consider applying simplified accounting standards for small and medium-sized enterprises (SMEs).** The Accounting Law, Article 20, mandates the use of the Lao Accounting System for preparation of legal entity financial statements. Accounting standards are decided by the Prime Minister upon proposal from the Minister of Finance. For statutory financial reporting purposes, all enterprises in Lao PDR utilize the Lao Accounting System developed and introduced in 1992. This system requires all enterprises to complete a standard chart of accounts for submission to the MOF Taxation Department. As translated by the Ministry of Finance, *IFRS 2003* is intended to be adopted as national accounting standards, with limited updates based on IFRS 2005, for all enterprises in the near future. The law provides that specific accounting standards should be issued for SMEs. However, these specific standards are yet to be developed. The accounting standard setters in Lao PDR are encouraged to develop and issue simplified standards different from the ones developed for public interest entities.<sup>6</sup>

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<sup>6</sup> Within this report, public interest entities are those in which the general public has an interest by virtue of the nature of their business size, their number of employees, or their range of stakeholders. Examples

Experience shows that this can ensure greater success and an improved compliance culture.

11. **Under the supervision of the Ministry of Finance, the Accounting Council is mandated by the Accounting Law to act as technical advisor, carrying out specific research on accounting standards and other related regulations.** However, the Accounting Council meets irregularly and does not have a full-time staff. The Accounting Council lacks any capacity to act in an effective oversight role. The 12 person Accounting Council is led by its current president who is an ex officio Vice Minister of the MOF. The LICPA, Chamber of Commerce, and a commercial bank are represented on the Council along with other members from various government departments and the public sector.

12. **The Accounting Law, Article 73, provides the Ministry of Finance with the right to propagate and disseminate laws and legislation concerning accounting; Article 74 details the rights and duties of the MOF Accounting Department.** Because of their significant responsibility, the 23 full-time staff of the MOF Accounting department need to further improve their technical capacity. Two separate units within the Accounting Department are responsible for developing accounting and auditing standards.

13. **The LICPA was founded by decree in 1998.** The Accounting Law, Articles 66 to 68, and the Audit Law, Articles 54 to 57, detail the intended role and responsibilities of LICPA. The LICPA is a member of the Association of Southeast Asian Nations (ASEAN) Federation of Accountants but is not a member of the International Federation of Accountants (IFAC). The Accounting and Audit Laws require clarification of LICPA's exact responsibilities regarding training, examination, and certification and licensing of accountants and auditors. With only 3 administrative staff, the LICPA lacks sufficient capacity to carry out the functions expected of any modern professional accountancy body.

14. **There is no legal requirement for a group of companies to prepare consolidated financial statements.** For the companies with subsidiaries in Lao PDR, there is no legislative requirement for consolidation. This represents a serious shortcoming in the regulatory framework as nonconsolidated financial statements provide an incomplete view of company's financial performance and position.

15. **The Law on Commercial Banks 2007 sets the requirements for financial reporting by banks.** The Bank of Lao PDR (BOL) has responsibility for the supervision of banks. Under the Law on Commercial Banks, Article 57, banks must issue audited financial statements by April 30 of each calendar year. Financial statements, an annual report on operations and an auditor's opinion, must be published in a national newspaper. As yet, this has not happened in practice. Despite the requirement that copies of the annual report be provided to the public on request without charge, this facility does

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include banks and similar financial institutions, insurance companies, investment funds, pension funds, publicly traded companies, and large enterprises, including large state-owned enterprises.

not exist in practice. Banks are also subject to monthly financial reporting, including statement of assets and liabilities, detailed information on loans and deposits, and various financial ratios. The Bank of Lao PDR PDR prescribes the chart of accounts and formats for banks in order to prepare their financial statements. This chart of accounts was introduced in 1997. There is no statutory requirement for banks to use IFRS. The Chart of Accounts for Banks is being revised at the present time in line with a recent version of the IFRS. However, there is no mechanism in place for updating the Bank Chart of Accounts to reflect up-to-date changes in the IFRS. The IFRS include standards that have been developed to help banks prepare financial statements showing a true and fair representation of income and expenditure and assets and liabilities. For example, IAS 32, *Financial Instruments: Disclosure and Presentation*, and IAS 39, *Financial Instruments: Recognition and Measurement*, were set to enable banks to account for financial instruments. However, the 1997 Lao Accounting System for Banks does not enable banks to properly account for such complex activity. Also, the current Lao Accounting System is not comprehensive enough to handle all types of accounting issues encountered in bank financial reporting.

**16. The Insurance Law sets out the various compositions of technical provisions relating to an insurance contract but not the measurement principles and disclosure requirements with respect to financial reporting.** The Insurance Law, Article 35, requires insurance companies to submit annual financial statements to the Department of State Owned Enterprises (SOE) Financial Management, no later than June 30 of each calendar year. Article 33 requires all insurance companies to be audited. There is however no system in place to enforce this requirement and no capacity within the Department of SOE Financial Management to review the quality of financial statements submitted by any of the 4 insurance companies in Lao PDR. Given that insurance companies are required to prepare financial statements in accordance with the Lao Accounting System and that IFRS is not legally required, the quality of financial reporting is questionable. Standards such as IFRS 4, *Insurance Contracts*, are of critical importance when measuring insurance company liabilities.

**17. The Audit Law covers provisions relating to both the audit of public and private sector entities.** Article 6 requires that the detailed contents of state audit standards are decided by the National Assembly upon proposal of the President of the National Audit Agency.

## **B. The Profession**

**18. Due to lack of resources, the LICPA is unable to operate effectively.** If held to comparison with IFAC Statements of Membership Obligations, the LICPA falls short of public expectations for a modern professional accountancy body. The LICPA has a 6 person Council, of which 3 are from academia. There are 3 administrative staff members. With only 150 subscribed members and limited income, the LICPA must make strengthening its capacity the highest priority.



19. **Lao PDR has a shortage of qualified professional accountants.** Around 2,000 companies are registered with the Ministry of Commerce, but the LICPA has only 150 individual members. There is a lack of well-trained and qualified local auditors. Many audit firms, including the members of large international firm networks, do not have an adequate number of qualified local Lao PDR staff to conduct work. There are 40 accounting firms operating in Lao PDR, including 3 local offices of the large international accounting firm networks. Much of the audit work carried out by the international firms is for group reporting purposes or for lenders and falls outside of the statutory reporting arena. All 16 banks and 4 insurance companies, as well as most large corporate entities, are audited by local members of international firm networks. The small local audit firms mostly concentrate on tax and bookkeeping services with only occasional audit work for medium-size and small companies.

20. **The LICPA members are required to have completed a 6-month training and examination program that includes 10 subjects.** More than 400 certificates of completion have been issued since 1996 when the program was first introduced by the Ministry of Finance. However, only 150 persons have LICPA membership. The training program is in the Lao language hence no foreign persons have yet completed the program and obtained LICPA membership. No foreign-based professional accountancy training program is active within Lao PDR, hence few local persons hold any IFAC-affiliated professional accountancy qualifications.

21. **The LICPA has an operational certification scheme for accountants, but there is no recognized system of auditor certification and licensing in Lao PDR.** There is little or no awareness of the requirements of International Education Standard (IES) 8, *Competence Requirements for Audit Professionals*, the IFAC-issued training and experience requirements. Competence in this area requires a higher level of education and training in audit and related areas than is required of other professional accountants. Without a managed and controlled scheme of training, examination, certification, and licensing, Lao PDR cannot develop a genuine audit profession capable of carrying out audits in compliance with ISA. A grandfathering-type scheme will be required in Lao PDR with a provision that all existing accountants and auditors subject to ‘grandfathering’ should be required to undergo intensive training. Looking toward the future, a system of education and examination, compliant with all International Education Standards should be introduced for future accountants and auditors.

22. **Outside the large accounting firms, there is a lack of local persons with the capacity to produce IFRS-compliant financial statements, which may be required for group reporting purposes or for lenders.** Companies are required only to submit annual financial statements to the MOF Taxation Department. These financial statements are prepared in accordance with the Lao Accounting System. Local accountants are familiar with this System. These annual financial statements are not necessarily subject to audit. Members of the international network dominate the market for the provision of IFRS- and ISA-compliant accounting and auditing services, which is driven by group reporting and lender requirements.

23. **Although the LICPA has translated the IFAC 2005 Code of Ethics for Professional Accountants, there is no system in place to ensure that practicing accountants and auditors actually comply with it.**<sup>7</sup> As an aspiring IFAC member, the LICPA must now examine methods that can be utilized to achieve compliance by the local profession. Among accountants and auditors with whom the ROSC team met, there is a varying degree of awareness of the actual content of the ethical standards. Without any means of ensuring auditors are working in compliance with ethical standards, the public cannot be assured of genuine commitment and adherence to the 5 internationally agreed fundamental principles of professional ethics: integrity and objectivity, professional competence and due care, confidentiality, professional behavior, and technical standards.

24. **Corporate management tends not to take full responsibility for preparing financial statements.** Some stakeholders have cited instances when company management has either partly or fully relied on auditors to prepare financial statements. The Law on Commercial Banks, Article 56 even requires that auditors should assist banks in maintaining proper accounting records. This may be due to lack of qualified professionals available for preparing financial statements and to corporate management's misperception about the role of auditors. The latter point arises from company directors' lack of knowledge on auditing procedures thus impairing significantly their fiduciary responsibility. In such cases, the auditors' involvement in the preparation of bank financial statements, and audit of the same financial statements may threaten auditors' independence. This results in non-compliance with international good practices on auditor's professional ethics. In practice, the bank management as well as their supervisors have very limited understanding of the value of an audit and the information it contains. In the past they have not used the auditor's reports as a guide to improvement, but have often seen them as just another required report.

25. **Relevant Lao laws do not provide for significant penalties against negligent auditors.** There is no legal requirement to have professional liability insurance. This tends to impair an auditor's accountability and in many cases has created an environment of unconcern toward risks of malpractice suits by auditors. Lao PDR has not yet experienced any litigation against auditors.

26. **There is no actuarial profession in Lao PDR.** This represents a serious problem for the financial reporting by insurance companies, in particular where actuarial valuations should be required for purposes of income recognition and the recognition and measurement of assets and liabilities.

### C. Professional Education and Training

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<sup>7</sup> The *Code of Ethics for Professional Accountants*, developed by IFAC International Ethics Standards Board for Accountants (formerly the Ethics Committee), establishes ethical requirements for professional accountants and provides a conceptual framework for all professional accountants to ensure compliance with the fundamental principles of professional ethics. Under the framework, all professional accountants are required to identify threats to these fundamental principles and, if there are threats, apply safeguards to ensure that the principles are not compromised.

27. **The LICPA professional education program lacks the necessary depth of coverage to enable compliance with IFAC International Education Standards.** The 6-month, 10-subject program covers a wide range of topical subject matter but lacks the depth and rigor to enable IES compliance. Lack of both professionally qualified trainers and up-to-date, translated IFRS- and ISA-compliant material presents a serious constraint to the program's value to the Lao business environment.

28. **IFAC recommends teaching professional ethics separately in the pre-qualifying education of professional accountants.**<sup>8</sup> Ethics training is included within the audit module of the LICPA student education syllabus. However, given the brevity of the overall LICPA training program, actual training is unlikely to provide adequate coverage on professional ethical dimensions. The LICPA must look toward developing training material on ethics that covers both international as well as local ethical issues.

29. **There is no specific accountancy degree course available at any university in Lao PDR.** The overall quality of accounting education and training in Lao PDR is not sufficient to produce the required number and skill level of qualified professional accountants and auditors. Poor communication skills, insufficient practical exposure, and lack of broad-based business knowledge and critical-thinking ability have all been identified as problems that must be addressed. In essence, neither the professional nor academic accounting education in Lao PDR adequately provides exposure to the conditions and challenges facing modern accountants. This fact has been a major contributing factor to the absence of any Lao person holding a senior accounting position within practice and industry anywhere in Lao PDR.

30. **The LICPA has no system to enforce practical experience requirements for accountant trainees.** Practical experience should be regarded as an integral part of any professional accountant's education and training.<sup>9</sup> A mentoring system for accountant trainees, utilizing experienced members should be developed. All students should be required to maintain a standardized training logbook.

31. **There is no required continuing professional development for members of the LICPA.** Without such a requirement and corresponding means of enforcement, it is unlikely that members will develop or maintain necessary professional skills.<sup>10</sup> However, continuing professional education must never be regarded as a substitute for the essential foundation provided by pre-qualification student education.

32. **Professionals working in small local accountancy firms lack capacity to undertake audits in line with international good practices.** Many practitioners, who

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<sup>8</sup> IFAC has issued IES 4, *Professional Values, Ethics, and Attitudes*; and Educational Guideline No. 10, *Professional Ethics for Accountants: The Educational Challenge and Practical Application*.

<sup>9</sup> IFAC IES 5, *Practical Experience Requirements*, requires that the professional body ensure all candidates receive adequate practical experience.

<sup>10</sup> IFAC has issued IES 7, *Continuing Professional Development, A Program of Lifelong Learning and Continuing Development of Professional Competence*.

focus more on bookkeeping, accounts preparation, and taxation services are handicapped by their lack of access to current literature on IFRS and ISA. The LICPA does not provide any technical advisory support and does not make available practical tools such as implementation guidance or audit manuals. Such valuable member services should be regarded as a key function of any modern professional accountancy body.

#### **D. Setting Accounting and Auditing Standards**

33. **The Accounting Law, Article 18, requires that accounting standards are decided by the Prime Minister upon proposal of the Minister of Finance.** For statutory reporting purposes, companies continue to submit to the Taxation Department unaudited annual financial statements in accordance with the Lao Accounting System. When audits are carried out, LICPA members have been required to use the last translated version of *ISA 1995*. Two units exist within the MOF Accounting Department to develop accounting and auditing standards. *IFRS 2003* has recently been translated into the Lao language as have 28 standards from *ISA 2005*. It is the intention of the Ministry of Finance to introduce these standards as Lao Accounting Standards and Lao Standards on Auditing in the near future. This presents two critical issues: First, the versions of ISA translated for use are out of date; and second, IFRS is not applicable to medium-size and small entities. Non-availability of the current versions of IFRS and ISA causes problems for practicing accountants and auditors in Lao PDR in the same way as in many other developing countries.<sup>11</sup>

34. **Although the Ministry of Finance is mandated to set the accounting standards, it lacks resources.** With insufficient budget and limited professionally qualified staff, the MOF Accounting Department operations are constrained. This hinders timely adoption and updating of IFRS and issuing guidance with respect to practical application of these standards. The MOF Accounting Department, the Accounting Council, and the LICPA lack capacity to review and interpret critical topical issues and provide required advice to the professional community. Preparers of financial statements therefore generally seek the advice of auditors on technical matters.

35. **Banks are required to submit financial statements to the Bank of Lao PDR in accordance with a prescribed chart of accounts. The existing chart of accounts was introduced in 1997. A revised chart of accounts is being implemented at the present time. However, the revised chart of accounts does not reflect recent changes (2008 onwards) in the IFRS.** Given the complexity of the modern financial environment, the 1997 chart of accounts does not enable banks to present financial statements that show a true and fair view. Reliance is placed on the services of the two international audit firms to help submit true and fair financial statements. There is confusion as to whether financial statements are submitted in accordance with the 1997 accounting system, or current IFRS. The Bank of Lao PDR also issues prudential regulations that have an impact on preparation of general purpose financial statements.

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<sup>11</sup> English version of the current ISA may be accessed at the following website: <http://www.ifac.org/IAASB/index.php>. The summaries of the current English version of IFRS, may be accessed at the following website: <http://www.iasplus.com/index.htm>

Annual returns submitted by the 16 banks registered with the Bank of Lao PDR are reviewed by both the BOL Supervisory and Accounting Departments. Only the BOL Accounting Department reviews returns for compliance with accounting requirements, but does not have any professionally qualified accountants on staff. Given the challenges of bank accounting, the BOL Accounting Department lacks the capacity to carry out this role effectively.

#### **E. Enforcing Accounting and Auditing Standards**

**36. Although the Accounting Law Articles 84 to 87 detail potential sanctions for infringement, there is no clear and effective mechanism for enforcing the corporate accounting, financial reporting, and auditing requirements.** This situation is compounded by lack of any system to report noncompliance. The Accounting Law does not define which entities are to ensure enterprises' compliance with applicable accounting, financial reporting, and auditing requirements; and what type of control the authorities should exercise in that matter. This has resulted in complete absence of monitoring and enforcement activities with regard to applicable standards.

**37. The LICPA does not have the capacity to carry out necessary quality control review of monitoring and enforcement activities.** Auditors are not subject to practice review, and there is no effective mechanism for disciplinary action in cases of violation of applicable standards. A review mechanism would help ensure that audit firms have adequate quality control arrangements and that they are carrying out audits in accordance with ISA.

**38. The Taxation Department does not receive IFRS training.** Financial reporting in Lao PDR is heavily influenced by taxation considerations. It is therefore essential that the Taxation Department understand the reasons for adopting IFRS and also its technical requirements.

**39. Lack of implementation guidance prevents local audit firms from properly understanding or being able to comply with ISA.** Lack of guidance has also prevents local accountants from being able to understand or apply IFRS when required. This has contributed in some cases to a knowledge gap among preparers and auditors of financial statements. Consequently, it raises a possibility of applying the standards inconsistently and resulting in compliance gaps between standard requirements and actual practices. Lacking access to modern audit practice manuals, many audit practitioners are unable to deal with important concepts like audit risk, audit planning, internal control, materiality, documentation, going concern, and quality control.

**40. The Law on Commercial Banks establishes BOL authority to enforce accounting regulations and conduct supervision.** However, the BOL Supervision Department focuses more on prudential reporting than on general purpose financial reporting. The BOL Accounting Department, which does not include any professionally qualified accountants, carries out limited reviews of financial statements to ensure compliance with the required accounting system. Banks are required to submit financial

statements in accordance with the system and chart of accounts developed in 1997. There is a clear need for enhancing BOL staff technical capabilities, particularly in terms of practical application of accounting standards with regard to monitoring and enforcement of financial reporting requirements. Banking supervisors have expertise in the legal and compliance issues outlined in different official pronouncements of the Bank of Lao PDR and can challenge banks where differences arise. However, they need to have sufficient technical accounting knowledge in order to effectively monitor and enforce compliance with regard to applicable accounting and auditing standards. The Law on Commercial Banks, Part VI outlines sanctions against violators. Such a system of sanctions can only be expected to operate effectively if the relevant supervisors have the necessary technical skills to identify issues of concern.

41. **The Department of State Owned Enterprise Financial Management does not monitor compliance by insurance companies with accounting standards mainly due to its lack of technical capacity.** There is no qualified actuary or professionally qualified accountant on the staff of the Department of State-Owned Enterprise Financial Management. This lack of expertise seriously limits capacity to verify whether the provisions relating to insurance contracts are correctly calculated, which is one of the most sensitive aspects of accounting by insurance companies.

### III. ACCOUNTING STANDARDS AS DESIGNED AND AS PRACTICED

42. **The Lao Accounting System (LAS) is not compatible with the current requirements of IFRS.** However, it has the benefit of being generally understood by preparers of financial statements. This system is mandatory for all companies submitting annual financial statements to the Taxation Department. For statutory financial reporting purposes, all enterprises in Lao PDR follow the LAS. This system requires all enterprises to complete a standard chart of accounts for submission to the MOF Taxation Department. There is general acknowledgement that the gap between LAS and IFRS is considerable. The standards gap analysis reveals that there are significant differences between the accounting policies generally used and disclosures made under LAS for statutory reporting purposes and those which would be required under IFRS.

43. **The 2003 version of IFRS, with certain updates from IFRS 2005, has been used by the Ministry of Finance to develop a set of proposed Lao Accounting Standards.** As yet, the proposed new standards have no legal backing. Since 2005, the IASB has issued several new standards, and updated or repealed others. None of these changes are reflected in the proposed Lao national standards. As a consequence, many of the newly IASB-issued standards will not be applied in Lao PDR, and some national proposed standards will be out of date. In addition, the interpretations issued by the Standing Interpretations Committee and its successor International Financial Reporting Interpretation Committee (IFRIC), which are integral components of IFRS, have not been adopted in Lao PDR.

44. **The absence of accounting standards in sensitive areas poses a serious threat to the quality of the financial information in the corporate sector.** This is a major shortcoming since proper reporting of many sensitive and frequent transactions cannot be made.

45. **Some banks and larger companies in Lao PDR prepare separate sets of financial statements under IFRS and the Lao Accounting System to satisfy the needs of shareholders or lenders.** This is the case for enterprises that have foreign shareholders or have borrowed from international creditors, including multilateral or bilateral donors. While this contributes to the quality of the financial information, it has the drawback of obliging those companies to prepare two different sets of financial statements, one for statutory purposes, the other for investors and lenders. It creates a disincentive for regulators and stakeholders to strengthen the statutory financial reporting regime and represents an additional administrative burden for those companies.

46. **While not required for statutory financial reporting purposes, implementing IFRS when required for group or lender purposes causes practical difficulties for companies and their auditors.** Discussions by the ROSC team with representatives of companies and auditors revealed serious implementation issues. Most of these problems arise from lack of adequate expertise among corporate accountants who find it difficult to prepare financial statements in accordance with the IFRS. Moreover, Lao accountants in some cases lack industry-specific knowledge with regard to application of relevant IFRS. The ROSC team observed this problem is pervasive in the banking and insurance industries.

47. **Evidence suggests the lack of adequate capacities to prepare IFRS-based financial statements.** The ROSC team's discussions with company management during its due diligence mission led it to believe that the companies may not have adequate resources or ability to prepare IFRS-based financial statements. It is possible therefore that the auditors either prepared or provided assistance with preparation of financial statements, raising a significant independence issue.

48. **Corporate financial statements are not easily available.** In practice, except for banks and insurance companies, annual financial statements, in a chart of accounts format, are submitted by companies solely to the Taxation Department of the Ministry of Finance. Financial Statements submitted to the Taxation Department are not available to the public.

49. **Banks are required to submit financial statements to the Bank of Lao PDR in accordance with a chart of accounts introduced in 1997.** There is no statutory requirement for banks to use IFRS. This is an issue of serious concern given the complexity and sophistication of modern commercial bank operational activity. The IFRS include standards that have been developed to help banks prepare financial statements showing a true and fair representation of income and expenditure and assets and liabilities. For example, IAS 32, *Financial Instruments: Disclosure and Presentation*, and IAS 39, *Financial Instruments: Recognition and Measurement*, were set to enable

banks to account for financial instruments. However, the 1997 Lao Accounting System for Banks does not enable banks to properly account for such complex activity.

50. **The World Bank ROSC team reviewed 28 sets of financial statements.** The sample included 4 commercial banks, 24 companies of which 4 were joint-ventures, 3 were foreign-owned firms, 12 SOEs, and 5 private companies. The compliance gap analysis focused on both the compliance of statutory financial statements required to be prepared in accordance with LAS and voluntary or contractual (e.g., required by a holding company or lender) financial statements which purported to be prepared in accordance with IFRS. The financial statements purporting to be prepared in accordance with LAS were generally found to have been prepared in compliance with national requirements. However, statutory financial statements submitted to the MOF Taxation Department are not audited and hence there was no highlighting of any non compliance within any audit report.

51. **The financial statements reviewed which had been prepared in accordance with LAS do not comply with some of the most basic requirements of modern accounting and financial reporting.** It appears that the information contained in LAS-compliant financial statements are hardly useful for decision making by the market participants. Some of the gaps with basic accounting requirements are highlighted below:

- ***Presentation of financial statements.*** The presentation of annual accounts in accordance with the format of the chart of accounts is a significant departure from the requirements of the IAS 1, *Presentation of Financial Statements*. This could seriously impair the use of financial statements. Some companies did not provide prior period information, either in financial statements or in the accompanying notes. This impedes the reader's ability to understand the performance of the reporting entity and evolution of its financial position.
- ***Inventory.*** Failing to follow all requirements related to measuring and disclosing inventories at the lower of either cost or market value appears to be a serious deficiency.
- ***Impairment losses.*** Potential failures to recognize impairment losses on property, plant, and equipment could result in overstated assets. The reviewed financial statements did not indicate whether the long-term assets were impaired. Absence of any disclosure regarding impairment may prompt the users of information to doubt the validity of stated asset values. It could create a misconception that the carrying amounts of property, plant, and equipment in the financial statements are overstated. However, in reality it may or may not be overstated.
- ***Related party.*** Many entities that appear to have related parties, including some financial institutions, did not provide important disclosures such as relationship and transactions, pricing policies, volumes of related party transactions, and



corresponding amounts. Inadequate disclosure in this regard leads to noncompliance with IAS 24, *Related Party Disclosures*.

- ***Contingent liabilities.*** Some companies did not adequately disclose contingent liabilities, making their financial statements noncompliant with internationally comparable disclosure requirements in this regard.

#### IV . AUDITING STANDARDS AS DESIGNED AND AS PRACTICED

52. **Lao PDR cannot implement ISA without first developing a proper system for training, examining, certifying, and licensing of auditors.** Significant strengthening of both existing education and monitoring systems are required.

53. **Lao Auditing Standards, which are based on ISA, are not up to date.** LICPA requires members to use the translation of *ISA 1995*. Since 1995, the International Auditing and Assurance Standards Board (IAASB) has promulgated several ISA statements while no equivalent updates have been made in Lao PDR. Many critical matters are left uncovered by the national standards. Without the updates to reflect internationally agreed standards, audit practice in Lao PDR faces reduced quality. Lao Standards on Auditing cannot be regarded as conforming to the ISA.<sup>12</sup>

54. **Audits of all Lao PDR's 16 banks and 3 insurance companies are carried out by local offices of international networks.** Internally within those firms reliance is placed on the skills and experience of senior foreign personnel who may not speak the Lao language or have a clear understanding of the Lao PDR legal environment or taxation requirements. Reliance is also placed on internal training to develop and maintain necessary technical and practical skills of senior and junior staff. Lack of local skill and experience may be a critical problem, particularly in relation to audit procedures required by ISA 315, *Understanding the Entity and its Environment and Assessing the Risk of Material Misstatement*, and ISA 330, *The Auditor's Procedures in Response to Assessed Risk*. Proper audit planning and risk assessment requires a thorough understanding of local conditions. Additionally, internal training for junior and middle ranking staff can never be considered to be a substitute for completion of a fully IES-compliant professional training program managed by an IFAC member body.

55. **The environment for developing the auditing process in Lao PDR does not appear to be conducive to compliance with auditing standards.** ROSC-conducted interviews revealed several factors that seem to explain the difficulties or disincentives in complying with ISA:

- ***Corporate entities are not required to submit audited financial statements to the Taxation Department.*** There is no audit requirement within the taxation system for corporate financial reporting.

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<sup>12</sup> *A Guide for National Standard Setters That Adopt IAASB's International Standard But Find It Necessary to Make Limited Modifications*, Policy Position, IFAC, July 2006.

- ***Lack of understanding of the value of the audit process by corporate entities.*** Representatives of audit firms recognized a difficulty with companies that are not familiar with the potential control or commercial value of external audit. There is general misunderstanding as to the role and importance of statutory audit. Much audit work is carried out for group purposes or on behalf of lenders
- ***Lack of practical experience and technical expertise for applying auditing standards and enforcing accounting standards.*** There is no effective accounting and auditing education program in Lao PDR.
- ***Absence of monitoring and effective sanctions.*** There is no monitoring for compliance with auditing standards and ensuring that practicing auditors in Lao PDR observe quality assurance procedures. Not publishing the financial statements of most companies reduces risk of uncovering poor quality auditing. The lack of oversight weakens auditors' incentive for quality.

56. **Local audit firms do not have the capacity or support to carry out ISA-compliant audit work.** While the 3 large agencies of international networks have full access to training, technical support, and advisory services, local firms have no such benefit. Lack of LICPA support for local practitioners provides clear competitive advantage to the large firms. A basic function of a modern professional accountancy body should be the provision of training, technical support, and advisory services to all members. Except for those connected to international networks, most audit firms do not have access to quality audit practice manuals. In the absence of proper guidance, auditors generally find it difficult to deal with important concepts such as audit risks, audit planning, internal control, materiality, documentation, and going concern. This difficulty is further aggravated when the auditors do not have adequate industry-specific knowledge. Improvements in the audit quality can largely be achieved by the development and dissemination of practical guidance on the implementation of auditing standards.

## V. PERCEPTION OF THE QUALITY OF FINANCIAL REPORTING

57. **The financial statements of corporate entities are not readily available due to there being no system of accommodating financial statements or equivalent.** There is in effect, no system of open and available financial reporting in Lao PDR.

58. **Financial statements in Lao PDR are prepared in accordance with the Lao Accounting System introduced in 1992.** Banks are required to submit financial statements to the Bank of Lao PDR in accordance with a chart of accounts introduced in 1997. There is a dominance of tax reporting in an absence of other demands with limited or no enforcement by the appropriate authorities, and limited capacity of auditors and accountants.

59. **Banks do not rely on the financial statements presented by potential borrowers in determining whether to extend credit.** Although entities may be required to submit their financial statements as part of the loan application process, banks generally base their lending decisions on other factors, including amount of collateral, business forecasts, and site visits. The majority of corporate lending is generally based on the borrower's capacity to post collateral rather than its ability to service the debt. Financial analyses supporting lending decisions are limited; as such, audited corporate financial statement figures often matter little in the lending process.

60. **The users believe that financial statements audited by large firms meet higher standards of financial reporting.** Interviews and discussions with various stakeholders, including donor agencies and bankers, reveal that a higher degree of reliance is placed on the financial statements that are audited by the members of international accounting firm networks.

61. **Representatives of the audit profession expressed the view that auditing was not highly valued.** They perceived there was no pressure from the market to improve the quality of audit. Most of the enterprises in Lao PDR tend to raise capital by borrowing, secured by assets rather than on the strength of financial statements.

## VI. POLICY RECOMMENDATIONS

62. The following recommendations are interrelated and mutually supportive and are designed to improve collectively the financial reporting environment in Lao PDR. The policy recommendations emerge from this ROSC review, as well as the valuable inputs received from the various stakeholders. These primarily principle-based recommendations take a holistic approach and are expected to provide input in preparing a country action plan geared toward the sustainable high-quality corporate financial regime in Lao PDR. In implementing the recommendations, a country action plan should identify specific activities to be undertaken under the supervision of a national stakeholder group and possibly with the assistance from the World Bank and other development partners. It would be helpful to the Government's own plans as reflected in the draft Financial Sector Strategy to recognize the link between the two activities and to work in parallel and in coordination. The national stakeholder group should be comprised of representatives from the regulators, the LICPA, academia, banks, insurance companies, and the chamber of commerce. Based on the successful experience of other countries, this stakeholder group should assume ownership of the country action plan and develop strategies for implementation. The group will work under the auspices of the Ministry of Finance.

63. The following points have been taken into account in considering the policy recommendations:

- Clarifying the statutory framework in order to improve corporate accounting, auditing, and financial reporting practices;

- Building capacities for professional accountants and auditors and regulators;
- Emphasizing the case for strengthening capacity of national institutions involved with corporate accounting and auditing practices;
- Achieving greater financial transparency in the corporate sector and limiting tax evasion through ensuring proper calculation of corporate profits;
- Promoting a gradual process of improvement in the monitoring and enforcement activities in the context of accounting and auditing of the public interest entities.

64. **The policy recommendations should be supported by assistance from the development partners.** Some recommendations may require costly interventions relative to the Lao economy. With the support of development partners the cost of implementing many of the policy recommendations would be substantially reduced and would reap increased benefits. Considering relatively limited institutional capacities, it will be in the interest of Lao PDR to promote the case for international collaboration to strengthen corporate accounting and auditing practices with the support and guidance of international expertise from within the region and beyond.

#### *A. Strengthening Statutory Framework*

65. **There is a need to modernize the statutory framework governing accounting, auditing, and financial reporting.** Immediate steps need to be taken by the Ministry of Finance to carry out a comprehensive review of all legislation related to accounting, auditing, and financial reporting in order to identify vague or conflicting requirements. Arrangements should be made to prepare with international advisory support, an internationally comparable accounting and auditing legislation, and thus develop a modern and internationally comparable statutory framework of accounting and auditing.

#### *B. Building Capacity for Professional Accountants, Auditors, and Regulators*

66. **Auditor appointment and removal regulations should be defined, as should auditor rights and duties.** For example, auditors should have the right to attend and be heard at company Annual General Meetings.

67. **A national certification scheme for accounting technicians should be developed.** Accounting technicians play a key role supporting professional accountants. Lao PDR should aim to develop a critical mass of such skilled persons within the local business community. There should be a clear pathway between the first level of the professional training program and the technicians program. Persons holding the technicians certificate should be granted entry to higher levels of the professional training program enabling a pathway to the professional qualification for non University graduates.

68. **Accountants from the public sector should be encouraged to study for the LICPA CPA qualification.** Professional accounting skills are critical within both private and public sectors. The LICPA should be regarded as the national centre of excellence for the entire Lao PDR professional accountancy training. A final year test of professional skills case study examination with public sector orientation should be developed for public sector specialists. The LICPA's professional examination curriculum, teaching and testing should be improved with the help of a strong professional accountancy body.

69. **The LICPA should provide non-certificate accountancy training for the general business community.** An extensive nationwide retraining program is required. In conjunction with the National University of Lao, the LICPA should establish itself as the leading provider of professional financial management training in Lao PDR.

70. **Strict procedures for the issue of audit practice licenses should be introduced by LICPA and overseen by the Accounting Council.** A person should only receive the right to practice audit in Lao PDR following completion of an IES-compliant education and examination program. In particular, the LICPA should ensure compliance with IES 8, *Competence Requirements for Audit Professionals*. A 'grandfathering-type' scheme should be required for existing auditors. However, all auditors granted license under this scheme should be required to attend intensive training delivered by national and international experts.

### *C. Implementing International Accounting and Auditing Standards*

71. **Legal backing should be provided for the use of ISA in statutory audits of corporate entities.** Enterprises that fall below certain threshold should be exempt from annual statutory audits. The latest version of ISA should be required for all corporate external audit work. There should be thresholds for simplified financial reporting by the small-size and micro-enterprises. Enterprises that fall under those thresholds should be exempt from annual statutory audits.

72. **IFRS should be required for all public interest entities and detailed transition plan should be developed for their implementation.** This will require that public interest entities are defined. Such definition should result from an analysis of the business structure in Lao PDR. Where the regulators need additional information for prudential supervision purposes, this should be an addition to the IFRS. Simplified financial reporting requirements for small and medium enterprises should be developed. This threshold for financial reporting purposes should be defined by law.

73. **The Ministry of Finance should decide which standards to adopt for small and medium enterprise.** The simplified financial reporting requirements for SMEs, developed by IASB (currently exposure draft, not yet finalized), or similar reporting requirements developed by accounting standard setters in other developed and developing countries (e.g. Sri Lanka, India, UK), could be used as the basis for developing accounting and reporting standards for the medium-sized enterprises. And an updated

version of the Lao Accounting System could continue to be used by those companies defined as small-size. For the micro-enterprises and other informal business entities, there should not be any requirement for mandatory preparation of financial statements; arrangements should be made for simplified and less burdensome tax filings by these enterprises.

**74. An awareness program for improving the degree of compliance with the applicable financial reporting requirements should be introduced.** The LICPA and other regulators should work jointly to design awareness programs highlighting the significance of compliance with accounting and auditing standards and to improve information dissemination channels. Shareholders, directors, and top officials from the corporate sector should be briefed adequately on their responsibilities to ensure compliance with standards and enforcement process, including legal implications. The benefits of compliance with standards and best practices should be highlighted in such programs. In addition, these programs should include cases focusing on emerging international developments and the role of transparent financial reporting in attracting both strategic and portfolio investors.

#### ***D. Achieving Financial Transparency in the Corporate and Public Sector***

**75. Public interest companies should be required to submit their financial statements to the newly structured Accounting Council.** In addition to filing annual financial statements with other regulator(s), the public interest entities should submit their legal entity and consolidated financial statements to the Accounting Council. The Accounting Council should make necessary arrangements for reviewing these financial statements for the purpose of monitoring compliance with the applicable accounting and auditing standards.

**76. Group companies fulfilling the criteria of public interest entities should be required to prepare consolidated financial statements.** In order for this requirement to be effective, extensive nationwide training will be required.

#### ***E. Strengthening Capacity of National Institutions***

**77. The LICPA capacity must be strengthened considerably.** While operating as a self-regulatory body, the LICPA should be overseen on behalf of the public by the Accounting Council. Within a sound system of governance LICPA should be provided with initial funding in order that it can establish operational directorates capable of providing genuine value to Lao PDR, its business community, and accountancy profession. Led by a president and a competent full-time chief executive officer, LICPA should establish directorates for the following:

- Education and training
- Examination
- Registration

- Members services and technical support
- Monitoring
- Legal, investigation and discipline
- Appeals
- Finance

78. **A twinning arrangement with a strong IFAC member body should be established.** It should be ensured that this mature professional body has genuine capacity and commitment to support and provide ongoing advice to the LICPA. It must be ensured that this twinning partner commits itself to ongoing long-term support and the provision of experienced internal staff with relevant domestic and international experience. The twinning partner will be expected to help prepare a full business and financial plan for the LICPA. This should include a full business risk analysis. Given available income from training, examination and subscription fees, the LICPA should be expected to become self financing within 5 years.

79. **IFAC membership should be a long-term aim for the LICPA.** In the meantime the twinning partner should help guide the LICPA through the IFAC Compliance Program and toward working in accordance with the IFAC Statements of Membership Obligations. The achievement of IFAC Associate status within 3 years ought to be a realistic target.

80. **An enhanced oversight role for the Accounting Council should be defined.** The Accounting Council should include a broader range of stakeholders in order to address systematically the needs of private and public sector stakeholders in all areas of corporate financial reporting. There should be legal backing for establishment of an arrangement for audit practice review under the auspices of the Accounting Council. The review arrangement should be provided with adequate power and resources. Regulators should be provided with adequate authority to sanction appropriately for violations of applicable accounting and auditing standards and rules for ensuring effective monitoring and enforcing actions.

81. **Create a sustainable accounting and auditing standardsetting structure.** The Accounting Law requires that accounting standards are set by the Ministry of Finance. The MOF Accounting Department lacks the technical expertise to manage this process. An improved standard setting structure should establish a framework of cooperation among the MOF Accounting Department, Accounting Council, and LICPA and should utilize the expertise of all local experts. Foreign experts can help initiate this process.

82. **The technical capacities of the MOF Accounting Department, the Accounting Council, BOL Supervision and Accounting Departments, and Department of State-Owned Enterprise Financial Management must all be improved.** These institutions should be able to determine with confidence the degree of compliance by companies with the applicable standards; to accomplish this, they should do the following:

- Recruit technically qualified personnel,
- Receive practical training on implementation of IFRS and ISA from international and local experts, and
- Be provided with improved financial and technical resources.

83. **With emphasis on public interest entities, an Audit Inspection Unit should be established within the Accounting Council.** In partnership with LICPA, specialists should be drawn from the local profession to carry out the following functions;

- ***Audit practice review.*** Inspectors will be responsible for conducting practice reviews of the auditors of public interest entities, ensuring each audit firm is reviewed at a reasonable, regular interval. After completion of the initial review, recommendations should be provided to the audit firms for overcoming detected shortcomings concerning quality assurance arrangements. The practice review should evaluate an audit firm's quality assurance arrangements, its audit approach, and the working papers with regard to selected audit engagements. The policies and procedures for carrying out audit practice review activities will be developed by the unit with support from an established IFAC member body.
- ***Investigation.*** Valid complaints against auditors and audit firms and any irregularities identified from the reviews of financial statements and audit practices should be investigated.
- ***Disciplinary power.*** Following reviews, steps should be taken for appropriate sanctions on relevant parties in order to ensure compliance with the auditing requirements.
- ***Reporting to the public.*** The findings and decisions of the unit, including sanctions taken against errant auditors, should be made public. This would increase confidence in audited financial information on the part of both domestic and international users.

84. **The capacity of the Bank of Lao PDR and the Department of State-Owned Enterprise Financial Management to make meaningful reviews of corporate financial statements should be strengthened.** It is essential that staff better understand the relationship between prudential and general purpose corporate financial statements. The following activities should be organized:

- Staff of the banking and insurance regulators should be provided with training on technical, theoretical, and practical aspects of IFRS and ISA by both foreign and domestic experts. More general training should also be provided on recent operational developments in the banking and insurance sectors.
- Senior staff should be encouraged to engage in international forums relating to application of IFRS in banks.



- A study tour should also be organized to allow staff to view regulatory and supervisory activity in a developed environment.
- Foreign experts, with experience in the region, should work internally within the Bank of Lao PDR and Department of State-Owned Enterprise Financial Management. The foreign experts can provide both hands on advice and training.

#### ***F. Improving Monitoring and Enforcement***

**85. Monitoring and enforcement mechanisms should be implemented to ensure compliance with accounting and auditing standards.** The Accounting Council should be granted power to effectively monitor and enforce applicable accounting, auditing, and financial reporting requirements primarily for public interest entities. Legislation should also give the Accounting Council adequate power to require submission of audited financial statements by all other public interest companies. In order for the Accounting Council to carry out its supervisory and enforcement functions, a proposed Financial Reporting Review Panel should be staffed with adequate technically qualified people who are charged with the following: (a) reviewing financial statements filed with the Accounting Council; (b) requesting any additional information from companies and their auditors; (c) conducting on-site inspections at companies, as needed; and (d) imposing legal and administrative sanctions for noncompliance. The Review Panel could include accounting experts drawn on part-time basis from various sectors. To ensure the transparency of the process, deter enterprises from noncompliance, and foster users' confidence in the effectiveness of the regulatory regime, the Accounting Council should publicly report each calendar year on enforcement actions conducted, issues addressed, and sanctions taken.

**86. Establish governance structures within public interest entities.** Like some banks, Lao PDR public interest entities should establish audit committees that can play a role in monitoring the effectiveness of audit process, especially with regard to auditors' compliance with independence requirements. In this regard, a ROSC Corporate Governance assessment should be conducted in Lao PDR.

#### ***G. Advancing Education and Training Requirements***

**87. Increased government funding is required to enable an ongoing process of update and translation of standards and implementation guidance.** Update and translation of standards is a highly technical process, as well as time consuming and costly. Within this process, the LICPA should liaise with the IASB and IFAC in order to ensure adherence to the required translation policies of those standard setting bodies.

**88. Academic and professional accountancy education and training must be improved.** A strategic plan should be developed for the introduction of quality accountancy education in Lao PDR. Efforts should be focused around the LICPA and National University of Lao PDR (NUL). A nationwide training needs analysis is required

in order to develop such a plan. The views of government, business, and the profession must be sought.

89. **An accountancy degree course should be created at the National University of Lao.** In conjunction with an established foreign university, with its own respected accountancy degree course, the National University of Lao should develop an undergraduate program leading to a bachelor's degree in accountancy. This course should include training in IFRS, ISA, and ethics as well a range of other business and finance-related topics. LICPA should be involved at all stages of this development process with the accountancy degree expected to provide graduates with exemptions from the LICPA professional examination program.

90. **The LICPA should develop a student education and examination process which both meets the needs of the business community and complies with IFAC International Education Standards.** The twinning partner will be expected to help develop this program and should be capable of assisting with the preparation of a suitable syllabus and learning outcomes. The twinning partner will also be required to work with the LICPA to help prepare required training material. In this respect it is essential that the twinning partner operates its own internal high-quality education as well as examination program and can provide specialist advice from practicing lecturers and trainers.

91. **A mentoring system for trainee accountants, utilizing experienced members should be developed.** All students should be required to complete standardized logbooks, in which they record practical experience during the training period.

92. **The LICPA should introduce compulsory continuing professional education for all members.** In accordance with IES 7 *Continuing Professional Development*, all LICPA members should be required to undergo post-qualification training each year. This is essential in order that practitioners keep abreast of latest technical developments. The LICPA itself should organize and provide training sessions.

93. **The twinning partner should provide intensive training of trainers for a selected group of National University of Lao and the LICPA members.** Experienced professional trainers should train this key group of persons in the latest technical issues, modern training methodology and also materials preparation and maintenance techniques. This group of trainers will have significant responsibility for dissemination of information throughout Lao PDR.

#### ***H. Strengthening Local Accounting and Auditing Capacity***

94. **Given that members of the international networks currently carry out all audit work for banks and insurance companies in Lao PDR, it is essential that their local offices are involved in this strengthening program.** Their emphasis to date has however been on work carried out for clients for group reporting and lenders purposes.

The critical importance of statutory reporting, public interest, and understanding the local environment must be emphasized to staff of those offices. The importance to the public of LICPA and its professional education programs, delivered in accordance with IES, must be emphasized. Internal training cannot be considered as a substitute.

**95. The LICPA should help strengthen audit work carried out by local audit firms.** Technical and other practical support services should be provided to all members. All standards should be made available to members; and in collaboration with the twinning partner, audit manuals and other practical tools should be developed. Implementation guidance for IFRS, ISA, any other adopted accounting standards and the IFAC Code of Ethics for Professional Accountants should be developed. Such guidance should cover all technical requirements and include practical examples and be tailored to the local environment.

**96. Understanding the audit process and the ISAs currently in effect.** The LICPA needs to make huge efforts to enhance understanding of the local auditors about the requirements of current ISAs. The IAASB has promulgated a significant number of pronouncements since the ISAs of 1993 (which is the version last translated in Laos). However, it would be important to get across the reality which is since 1993, the ISAs themselves have moved towards and “audit risk” basis and more of a “top down” approach. The auditors in Lao PDR not only have to catch up to what the 1993 standards required but the ISAs themselves which now reflect a newer way of thinking about the audit process. For this reason, greater emphasis has to be made to ensure:

- a. There is an understanding by all key stakeholders as to purpose and objective of an audit. Related to this may be the need to introduce the concept of corporate governance as it will help to ensure there is sufficient understanding of the role of management with regard to the audited financial statements.
- b. There is immediate emphasis on getting higher educational institutions up to speed on the concept of auditing.
- c. Ensuring that LICPA is clearly supported in its role as a recognized professional accountancy body with responsibilities for accreditation and training of practicing auditors.

**97. Taxation Department staff should be provided with training on practical implementation of IFRS and ISA.** It is essential that the Taxation Department staff have an understanding of the proposed new accounting standards. The LICPA should provide IFRS training to all Taxation Department inspectors and other key staff.

**98. National Audit Agency staff should be provided with training on practical implementation of IFRS and ISA.** The LICPA should arrange training for the National Audit Agency with the reciprocal agency of the twinning partner. Specific focus should be given to practical issues related to the implementation of IFRS by state-owned enterprises.