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*Republic of Belarus*  
*Corruption Vulnerability Scan*

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**ABBREVIATIONS & ACRONYMS**

BEEPS	Business Environment and Enterprise Survey
CPIA	Country Performance and Institutional Assessment
CAS	Country Assistance Strategy
CVS	Corruption Vulnerability Scan
EBRD	European Bank for Reconstruction and Development
ECA	Europe and Central Asia
EU	European Union
GDP	Gross Domestic Product
GEF	Global Environment Fund
ICB	International Competitive Bidding
IFC	International Finance Corporation
IMF	International Monetary Fund
KRU	Control and Revision Department
LITS	Life in Transition Survey
MOF	Ministry of Finance
MOU	Memorandum of Understanding
OECD	Organization for Economic Co-operation and Development
OSCE	Organization for Security and Cooperation in Europe
PCR	Post-Chernobyl Recovery Project
POPs	Persistent Organic Pollutants
PPF	Project Preparation Facility
SCC	State Control Committee
SIRP	Social Infrastructure Retrofitting Project
SOE	Statement of Expenditures
TI-CPI	Transparency International – Corruption Perceptions Index
TSA	Treasury Single Account
TTL	Task Team Leader
UNDP	United Nations Development Program
USAID	United States Agency for International Development
WB	World Bank
WMRO	World Market Research Online
WHO	World Health Organization

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**REPUBLIC OF BELARUS  
CORRUPTION VULNERABILITY SCAN**

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## EXECUTIVE SUMMARY

The Corruption Vulnerability Scan (CVD) is an internal Bank document aimed at providing a better understanding on the Bank's vulnerability in extending assistance to Belarus, and making suggestions as to how to reduce risks in the use of Bank funds, while improving results on the ground. The CVS team visited Belarus in March 2007. Its main conclusion is that the vulnerability to corruption of Bank funds and activities funded from loan proceeds in Belarus is low, as long as Bank fiduciary procedures are used and implementation is closely supervised.

The report is in three parts: Corruption and Anti-Corruption in Belarus, Public Finance Management and the Bank Portfolio.

In the first part, **perceptions of corruption** in Belarus are assessed and compared with other countries in the Europe and Central Asia (ECA) countries. In general, foreigners' ratings of corruption put Belarus at the bottom of the group, while Belarussian citizens reported levels of corruption near the median of ECA countries. Assessments of the business environment are generally poor, but surveys of firms and households are somewhat less negative. An explanation for this difference in perceptions may be that the nature and levels of corruption in Belarus are tightly controlled, as is the economy.

A new **Anti-Corruption Law** was enacted in 2006. It emphasizes prevention by spreading the fear of unavoidable punishment. High Government officials benefit from special treatment, however, as they can be prosecuted only after the President has given his personal agreement. Several agencies are in charge of implementing the law, including the Office of the Chief Prosecutor.

Progress has been made in recent years in **public finance management**, including incorporation of special funds into the budget and improving the operations of the Treasury. The budget remains an annual exercise, but a process of program budgeting is being initiated. Two different ministries are in charge of the investment and current budget, with little coordination among them. Controls are pervasive, but they are mostly focused on compliance with regulations. The implementation rate of the investment budget is high (97% in 2006). The most important factor in this high rate is that general contractors, which are in most cases state-owned enterprises, are selected for a specific project, before the project is included in the draft budget. The selection process is not transparent. Evaluation of the economic and social impact of projects is almost non-existent.

There are a large number of regulations governing **public procurement** in Belarus, but not a single law that provides a comprehensive framework for the regulatory system. Frequent changes in the regulatory framework make the procurement cycle difficult to manage, time-consuming and expensive. A number of prices are regulated, including in the construction industry. There is no public procurement agency in Belarus, but control over public procurement is pervasive, with six agencies involved. Contractors assigned to contracts above US\$7.5 million equivalent financed from the budget funds are approved personally by the President.

Besides a GEF grant, the **Bank portfolio** in Belarus includes two investment projects, which aim at improving the living environment of the population through more efficient use of energy. Project implementation is slower than anticipated for a number of reasons, including the lack of interest of foreign companies to bid for Bank-financed contracts in Belarus, weak capacity of the local private sector, the need to obtain a large number of authorizations, the inadequate quality of design documents, and poor contract administration. While the financial management systems used by the two projects and GEF grant are found satisfactory, little is done to assess physical progress against payments, or value for money. The certificate of acceptance has not been issued for a number of facilities financed under the first Bank-financed project, because a critical element, which was not included in the contract, is missing. This situation should be corrected without delay.

## **INTRODUCTION, MAIN FINDINGS AND CONTEXT**

### **Structure of the Report**

This Corruption Vulnerability Scan (CVS) has three sections. Part 1 examines the environment for corruption in which the World Bank is operating in Belarus, the levels of corruption as assessed by experts and reported in surveys, and the policy and institutional environment that supports or constrains corruption. Part 2 focuses specifically on the sub-set of the institutional environment most pertinent to Bank operations: fiduciary controls in Belarus, including budgets management, financial controls, and public procurement. Recognizing that portfolio size and performance are closely linked with the risk of corruption, Part 3 examines the implementation experience of Bank-financed projects in Belarus.

### **Introduction**

The CVS is an internal Bank's document aimed at (i) providing a better understanding of the Bank's vulnerability in extending assistance to Belarus; and (ii) making suggestions as to how to reduce the risks concerning the use of Bank funds, while improving the results on the ground. The CVS is intended to serve as an input for the forthcoming CAS. It is not an investigation into possible wrongdoings or portfolio audit, but rather a proactive examination of systemic vulnerabilities by looking at the broader environment for corruption, and institutional restraints against corruption, in Belarus.

The CVS takes into account work done by the World Bank Group and the IMF, including the Country Economic Memorandum (2005), the two reports on Strengthening Public Resource Management (2003) and on Improving the Business Environment (2003), the IFC report on the Business Environment in Belarus (2004), and the Financial System Stability Assessment (2005). The Bank has not yet prepared a Country Procurement Assessment Report or a Country Financial Accountability Assessment. A report on Selected Issues in Public Finance is under preparation. It will address three thematic issues: (i) Intergovernmental Fiscal Relations; (ii) Revenue Forecasting; and (iii) Capital Budgeting.

The CVS has been prepared by a team including Maria Vannari (team leader), Jerome Chevallier, Jim Anderson. It benefited from inputs by Irina Babitch (financial management), Sergey Prozorov and Irina Shmeliova (procurement). The team coordinated with the team led by Marina Bakanova, who is preparing the report on selected issues in public finance.

The mission to Belarus took place during the week of March 19-23, 2007<sup>1</sup>. The mission met with representatives from the Council of Ministers the key ministries and agencies concerned (Finance, Economy, Construction Supervision, Natural Resources and Environment, Energy Efficiency), the Budget Committee of Parliament, public agencies in charge of anti-corruption and public finance control (Prosecutor's office and State Control Committee), agencies and companies involved in Bank-financed project implementation and audit

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<sup>1</sup> Mission comprised Maria Vannari, Jerome Chevallier, Sergei Prozorov (ECSPS) and was joined by Elena Klochan and Ivan Velez, both from ECCU2. Mission assistance was provided by Ludmila Mazai (Minsk Country Office).

(Belinvestenergoberezhnie, Belproject and Deloitte), an unsuccessful bidder (Fobosintergas), and donors (UNDP, USAID and EBRD). The mission is most grateful for the quality of the discussions with all its interlocutors. The list of organizations and persons met is in Annex 1.

## **Main Findings**

The CVS team's assessment is that the vulnerability to corruption in Bank activities in Belarus is low, as long as Bank procurement procedures are used and implementation is closely supervised. In some cases, local enterprises, public or private, such as contractors or auditors, enjoy a de facto monopoly, because foreign firms are not prepared to invest in Belarus where there are limited business opportunities, or participate in tenders, when the contract amount is relatively modest. Other conflicts between national and Bank procurement rules also continue to present challenges to effective and timely delivery of Bank assistance to Belarus. Moreover, some factors that are associated with high levels of corruption – an intrusive business environment, roadblocks keeping civil society and the media from providing sufficient external oversight – are especially onerous in Belarus. The CVS's team assessment that vulnerability to corruption in Bank activities is low stems from the system of strong, and frequently used, repressive measures that have apparently kept many forms of corruption relatively under control.<sup>2</sup> This CVS has been careful to focus on corruption as a threat to the Bank-financed projects, and to avoid mingling corruption per se with assessments of the political situation in the country.

After a difficult decade, following the break-up of the Soviet Union, Belarus economic and social conditions have much improved in past years. The economy has been stabilized, and GDP growth has been substantial. Living conditions have improved, thanks in part to a broad safety net. Under President Lukashenko, who was elected for the first time as President of Belarus in 1994, the government has reverted to a statist form of command and control of the economy. All sectors are highly regulated and economic activities are controlled, which is stifling private initiatives. Sanctions for corrupt practices are harsh and public sector managers, with the exception of a small circle around the President, understand that that they have to be extremely cautious with the management of public funds.

The Bank portfolio includes two projects, which are both aimed at improving energy efficiency. The objectives of these projects are fully supported by the Government, and even more so now, after the January 2007 steep increase in the price of gas sold by Russia to Belarus. The first project was approved in 2001 and the second in 2006. Implementation of the first project was delayed, mostly because of the unfamiliarity of the project management team with Bank procedures. Good progress was made, but additional work is needed for a number of facilities to ensure that all systems rehabilitated with Bank financing are fully operational to avoid reputation risk the Bank might face if this is not done.

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<sup>2</sup> Experience elsewhere in the region in the 1990s has shown that while opening up an economy and political system, some of these repressive systems are necessarily deconstructed or made less effective – without concomitant attention to building the systems of accountability and transparency, corruption may well grow. This does not, however, appear to be imminent in Belarus.

## **Context**

### ***Economic developments***

Belarus enjoyed one of the highest living standards among the Soviet republics until the mid-1980s. It had a relatively well-developed industrial base and a high education level. The country was devastated by the explosion of the Chernobyl nuclear power plant in neighboring Ukraine in 1986, which contaminated about 20 percent of its territory. It became independent in 1991, and, as in the other former Soviet republics, its GDP was in free fall in the first half of the 1990s. Economic growth resumed, however during the second part of the 1990s, thanks in part to the re-establishment of special relations with Russia, which enabled Belarus to boost its exports. During the period 1996-2004, overall GDP growth averaged 6.6 percent per annum, driven by improvements in labor productivity, increases in capacity utilization and energy efficiency and pay raises in the public sector.

In the early 2000s, adjustments were made to address serious distortions in the economy. Main areas of reform included, the unification of the exchange rate and the phasing out of barter with Russia, stricter fiscal and monetary policies, and improved cost recovery and payment discipline in the energy and utility sector. Little progress has been made, however, in changing the economic system inherited from the Soviet Union. After an initial phase of capitalist reform in the early 1990s, the Government reverted to the old statist model. Enterprises and banks were renationalized. About 80 percent of all industry remains in state hands and banks are under strict government control.

Belarus is highly vulnerable to developments in neighboring Russia. On January 1, 2007, the Government of Belarus had to agree on a price hike for gas imports from Russia from about US\$46 to US\$100 per 1,000 cubic meters. The price of gas remains highly subsidized, however, when compared with the price paid by West Europeans (about US\$215 per 1,000 cubic meters of gas). The shock on the economy of Belarus is nevertheless a huge one. It will reduce external competitiveness and dampen economic growth. The Government estimated initially that the cost to the economy would be about US\$5 billion, or about 10 percent of GDP. It would seem, however, that the new prices have not yet been made effective, which would reduce the magnitude of the shock in 2007.

### ***Political developments***

Mr. Alexander Lukashenko was elected as Belarus' first President in 1994. Before the break-up of the Soviet Union, he had been elected as a Deputy in the Supreme Soviet of the Republic of Belarus in 1990. In 1993 he was elected to serve as the chairman of the anti-corruption committee of the Belarusian parliament. In that capacity he launched a fierce attack on the corruption and privileges of the Communist nomenklatura. He was elected President of Belarus as an independent candidate on a populist platform of "defeating the mafia".

President Lukashenko broadened the powers of the Presidency through a referendum in 1996 to amend the Constitution. Another referendum in 2004 removed term limits on the



presidency. According to the Organization for Security and Cooperation in Europe (OSCE), parliamentary elections in 2000 and 2004, and presidential elections in 2001 and 2006 failed to meet international democratic standards.

### ***Relationship with EU and other partners***

A Partnership and Cooperation Agreement was signed between the European Union (EU) and Belarus in 1995, but never became effective, after the moves made by President Lukashenko towards authoritarian rule. The EU has consistently emphasized the benefits Belarus would get from participation in the European Neighborhood Policy. Such benefits require, however, the return to a democratic form of government and an end to the isolation imposed by the country's authorities on its population.

The country strategy of the European Bank for Reconstruction and Development (EBRD) was reviewed by its Board in December 2006. The country's slow progress in democratic and market transition, and its inconsistent commitment to, and application of, principles of multi-party democracy, pluralism and market economy in accordance with Article 1 of the Agreement Establishing the Bank, have limited Bank activities to support to the private sector. At present, EBRD provides a line of credit to three private banks. Some local enterprises would like to benefit from EBRD direct support, but are reluctant to open up their books for fear of attracting too much government scrutiny.

The UNDP provides limited assistance, mainly to the health sector (HIV/AIDS and TB). The USAID's main focus is civil society and democracy building. The local context makes it extremely difficult for them to extend their assistance. The American organizations, which served as intermediaries, were forced to leave the country, or their license was not renewed. USAID has tried working through international organizations, including UNDP, WHO and IFC.

## **PART 1: CORRUPTION AND ANTI-CORRUPTION IN BELARUS**

### **Section 1: Analysis and perceptions of corruption**

The following paragraphs describe how the behavior of corruption is reflected in various cross-national indicators. There are three basic types of cross-national indicators: (a) expert opinions by foreigners, (b) survey of residents about their experiences and perceptions, and (c) aggregates that combine various other indicators. This section will focus on the first two, as aggregates are not useful for the purpose at hand<sup>3</sup>. Indicators are most useful when they clearly differentiate between corruption outcomes on the one hand, and the policy and institutional environment on the other. The analysis that follows examines separately indicators of outcomes, indicators of policy and institutional environment, and indicators that conflate the two. Notwithstanding external assessments of the non-competitive political situation, Belarus appears to be a country where day-to-day corruption is kept fairly under control.

#### ***(a) Expert opinions by foreigners: what do the foreign experts say about the overall level of corruption and the policy and institutional environment that may worsen corruption?***

Six sets of foreign expert opinions are available for Belarus. Some of these provide simple subjective assessments of “corruption”, while others use definitions that clearly include a broader policy-based concept.

#### ***Assessments of “Corruption”***

International Country Risk Guide’s (ICRG)<sup>4</sup> rating for corruption ranges from 0 (worst) to 6 (best). The ICRG assessment of corruption for Belarus has been a “2” every month since October 2001. (The change in that month was part of an apparent major realignment of ratings by ICRG covering a large number of countries. See Knack, 2006). This rating places Belarus at exactly the median for Europe and Central Asia (ECA) countries, with five worse, nine better, and six with the same rating (Bulgaria, Latvia, Lithuania, Russia, Serbia, and Ukraine).

Merchants International Group (MIG) produces an assessment of “Grey Area Dynamics” covering ten criteria, one of which is corruption. The assessment focuses on the risk

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<sup>3</sup> Aggregate indicators, such as the Worldwide Governance Indicators and the Transparency International Corruption Perceptions Index, are based mostly on expert opinions and have been criticized for lack of conceptual precision and other shortcomings which would only muddy our understanding the levels and trends of corruption in Belarus. The main ingredients for both of these aggregate indicators are the same expert opinion and survey-based measures that are discussed in detail in this report. See Stephen Knack, 2006. “Measuring Corruption in Eastern Europe and Central Asia—A Critique of the Cross-Country Indicators,” *World Bank Policy Research Working Paper* 3968; and Christiane Arndt and Charles Oman, 2006. *Uses and Abuses of Governance Indicators*. OECD.

<sup>4</sup> The ICRG Risk Rating System assigns a numerical value (risk points) to a predetermined range of risk components, according to a preset weighted scale, for each country covered by the system. Each scale is designed to award the highest value to the lowest risk and the lowest value to the highest risk. All countries are assessed on the same basis to allow for comparability.

of foreign investment. MIG downgraded Belarus slightly in 2005, to the level that is the worst in all of ECA.

### ***Assessments that mix corruption outcomes with the policy environment***

World Markets Research Online provides an assessment of the intrusiveness of the country's bureaucracy<sup>5</sup>. The amount of red tape likely to be encountered is assessed, as is the likelihood of encountering corrupt officials and other groups. Among ECA countries, Belarus is tied with five other countries at the bottom.

Freedom House – Nations in Transit (FH-NIT) has provided assessments of political systems, media, civil society, and corruption for all transition countries since 1999. Their assessment of corruption “looks at public perceptions of corruption, the business interests of top policy makers, laws on financial disclosure and conflict of interest, and the efficacy of anticorruption initiatives”.

FH-NIT has downgraded Belarus in their measure of corruption every year since 2003. Interestingly, however, the primary piece of evidence that they cite is that Belarus has been downgraded in Transparency International's Corruption Perceptions Index (TI-CPI). The TI-CPI itself is an aggregate measure based in part on the FH-NIT assessment. Thus, Belarus' slide in TI-CPI has been based in part on the downgrade in the FH-NIT assessment, and the FH-NIT assessment has been consistently downgraded citing the slide in TI-CPI (see Box 1 in Annex 3).

### ***Assessments of the policy and institutional environment***

The World Bank's CPIA (Country Performance and Institutional Assessment) is generated annually based on internal assessment of staff and can be considered an expert-opinion type indicator. There are a variety of specific indicators covering various aspects of governance, from gender equality to corruption. For some sub-ratings, such as gender equality, Belarus rates fairly well on a scale from 1 to 6, while the country rates fairly poorly for other aspects such as property rights and rules-based governance (2.0), and transparency, accountability and corruption in the public sector (2.5).

The CPIA sub-indicator for transparency, accountability and corruption in the public sector is the most relevant for this scan. The sub-indicator “assesses the extent to which the executive can be held accountable for its use of funds and the results of its actions by the electorate and by the legislature and judiciary, and the extent to which public employees within the executive are required to account for the use of resources, administrative decisions, and results obtained. Both levels of accountability are enhanced by transparency in decision-making, public audit institutions, access to relevant and timely information, and public and media scrutiny. A high degree of accountability and transparency discourages corruption, or the abuse of public office for private gain. National and sub-national governments should be

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<sup>5</sup> This definition is provided in Daniel Kaufmann, Aart Kraay, and Massimo Mastruzzi, 2006. “Governance Matters V.” *World Bank Policy Research Working Paper* .

appropriately weighted. Each of three dimensions should be rated separately: (a) the accountability of the executive to oversight institutions and of public employees for their performance; (b) access of civil society to information on public affairs; and (c) state capture by narrow vested interests. For the overall rating, these three dimensions should receive equal weighting.”

The latest rating for this sub-indicator is a 2.5, which is the worst in Europe—in ECA only Turkmenistan (1.0), Uzbekistan, (1.5), and Tajikistan (2.0) were rated worse, while Azerbaijan, Kazakhstan, and the Kyrgyz Republic received the same rating. Although the sub-indicator heading mentions corruption, the three sub-sub-indicators focus on accountability of the executive, access of civil society to information, and state capture by narrow vested interests. Accountability of the executive receives the lowest score of these three, owing to the unchecked power of the presidential administration.

Finally, the World Bank Group’s *Doing Business* indicators examine the processes involved in completing standardized tasks, such as enforcing a contract through the courts, dealing with taxes, trading internationally, etc. More cumbersome, costly and time consuming procedures generate incentives for firms to offer bribes to speed their way around the procedures. For many of these areas of dealing with the state, Belarus ranks poorly ( Figure 2 in Annex 3). This is especially true for the indicators for starting a business and paying taxes, for which Belarus ranks the worst in ECA and among the worst in the world. For other measures, however, Belarus ranks somewhat better: enforcing contracts through the courts is no more onerous, according to this indicator, than in half of ECA countries, and dealing with licenses and employing workers is even less burdensome for firms in Belarus than for firms in most ECA countries. The net effect, however, is that Belarus’ overall rank in the *Doing Business* indicators is abysmal.

***(b) Surveys of residents about their experiences and perceptions: what do Belarusian firms and households say about levels of corruption?***

There are relatively few recent cross-national surveys in Belarus, but two that do exist suggest levels of corruption that are not atypical of ECA countries. The first one (the EBRD-World Bank Life in Transition Survey or LITS) measures corruption in interactions between the state and citizens. The second one (the EBRD-World Bank Business Environment and Enterprise Performance Survey or BEEPS) reflects on corruption in interactions between the state and firms.

***(1) Corruption in interactions between the state and citizens***

The first analysis - the EBRD-World Bank Life in Transition Survey (LITS)- surveyed 1,000 households in Belarus and each of 26 other countries in ECA about various aspects of the way the household has fared during the transition from communism. The questionnaire also included questions on how frequently citizens must make unofficial payments when receiving certain government services or interacting with state officials (Figure 3 in Annex 3). As the survey also questioned respondents on whether they had been in official contact with the specified agency or service in the previous twelve months, the views expressed in the survey

are not merely perceptions, but most likely reflect actual experiences. In general, Belarusian citizens reported levels of corruption near the median for ECA countries. These survey responses stand in stark contrast to the assessments of foreign experts<sup>6</sup>.

*(2) Corruption in interactions between the state and firms*

The second analysis – the EBRD-World Bank Business Environment and Enterprise Performance Survey (BEEPS) - surveyed 300 firms in Belarus and 200-600 firms in each of 35 other countries, including all of ECA (except Turkmenistan), plus Germany, Greece, Ireland, Korea, Portugal, Spain, and Vietnam. The survey asked enterprise managers about a broad range of issues, of which corruption was a fairly small sub-set. Samples are selected the same way in every country and were identical in both 2002 and 2005 surveys.

Rather than giving an assessment of “corruption,” the BEEPS ask firms about many dimensions of corruption that they encounter in their interactions with public officials: How frequent are bribes paid? How large are the bribes? How problematic is corruption for the operation and growth of the firm? To whom are the bribes paid most frequently? The BEEPS focuses on corruption in the interface between firms and state officials, as reported by the firms themselves. Some types of corruption, such as leaders using the treasuries for their own benefit, are not within this interface. The BEEPS measures corruption outcomes, not the policy or institutional environment.

Figure 4 in Annex 3 shows how Belarus ranks compared to the other countries in the survey. Even for the same survey covering the same firms, assessments of Belarus vary widely. Firms in Belarus gave relatively positive ratings for “corruption as a problem doing business,” despite being at the median for the frequency with which they pay bribes, and in the worst third for the bribe tax (the share of annual revenue paid in bribes). For many sectors, bribery in Belarus is reported to be relatively infrequent, including tax administration, customs, and the courts. For procurement and business licensing, the frequency of firm-level bribery is somewhat higher, according to firms, although still less than the median of surveyed countries. Only for fire and building inspections do firms in Belarus report paying bribes more frequently than firms reported in other countries.

*Explaining the patterns revealed by experts and surveys*

While the various expert opinion type indicators of corruption generally rank Belarus very poorly, and assessments of the business environment are also generally poor, the picture painted by surveys of firms and households is somewhat less negative. Part of the answer for this puzzle can be illustrated by the BEEPS. While it is true that few firms in Belarus say corruption is a problem for their firm, this does not necessarily mean that corruption does not exist. A recent ECA study “Anticorruption in Transition 3—Who is succeeding ... and why?” explored this issue in depth and argued that the nature of corruption in Belarus, much like the

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<sup>6</sup> A series of surveys specific to Belarus conducted by IISEPS asked respondents to indicate the most acute problems faced by the country and its citizens. In June 2006, 27.6 percent of respondents indicated corruption and bribery are such a problem, down from 35.6 percent in June 2004. The relative rank of corruption increased somewhat, as the improvement for “pauperization” and crime were even larger than those for corruption. (Ioffe 2007.)

economy as a whole, was controlled. Belarus was second only to Russia in the percentage of firms that responded that bribery is frequent, yet corruption is not a problem for the operation and growth of their firms. Belarus was also among the 10 ECA countries with the most predictable bribes, according to firms that responded to the survey.

While it is often assumed that regimes that fare poorly in one way, such as human rights for instance, have also low ratings in other areas, such as corruption, this need not necessarily be the case. This CVS has been careful to focus on corruption as a threat to the Bank-financed projects, and to avoid mingling corruption per se with assessments of the political situation. Notwithstanding external assessments of the non-competitive political situation, Belarus appears to be a country where day-to-day corruption is kept fairly under control. The U.S. State Department's report in March 2006 calling Lukashenko "likely among the most corrupt leaders in the world" was widely reported in the press<sup>7</sup>. The report itself, however, generally focused on the lack of transparency, and even remarked at one place that "Lukashenko is not known for an ostentatious lifestyle". As to day-to-day bribery, another U.S. State Department publication states: "while the Embassy has received credible reports of corruption, particularly at the local level, U.S. firms have not identified corruption as a particularly significant obstacle to foreign direct investment<sup>8</sup>". These conclusions do not mean that corruption is trivial in Belarus; rather they suggest that the current system of strong centralized control has rendered levels of day-to-day corruption that are not notably worse than elsewhere in the CIS. As the system of centralized control over the economy and political system gives way to one that is more open, the levels of corruption could well increase in the short run unless concerted efforts are made to introduce new systems of accountability and transparency<sup>9</sup>.

## Section 2. The Anti-Corruption Law of 2006 and Related Acts

A new anti-corruption law was adopted in July 2006. The law sets a legal framework for the state policy in the area of anti-corruption. It declares that its purpose is to protect the rights and freedoms of the citizens and public interest from the threat or consequences of corrupt activities. The main accent is put on prevention of corruption by spreading the fear of unavoidable punishment among the population.

The law defines corruption as *abuse of power* or position by public officials (including by a foreign official acting on the territory of Belarus), which results in accepting any form of profit (in cash or in kind) in a form of a service, promise of an advantage or preferential

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<sup>7</sup> For example, the headline in the Washington Post read: "U.S. may consider new Belarus sanctions—White House report calls leader 'corrupt'." (March 18, 2006).

<sup>8</sup> *Doing Business In Belarus: A Country Commercial Guide for U.S. Companies* (2006) goes on to state: "Belarusian business representatives, particularly those involved in import and export transactions, however, complain often of pervasive corruption. The government is taking steps to amend the country's anti-corruption law to make it much harsher. The government regularly demands contributions from foreign and domestic firms alike for questionable charities, the annual harvest, and the president's election campaigns."

<sup>9</sup> See Mises Center (2006) for a discussion, including detailed examples, of corruption in Belarus. "Estimating corruption in Belarus is like estimating corruption in the Soviet Union. Some people believe that the communist party apparatchiks were clear acting within their own caste system. Others believe that it was the caste or the class system that made the party elite exploit the others. During the last decade corrupt practices became more ingrained in the strongly centralized system of decision making."

treatment or patronage for him(her)self or a third party; *bribery* of public officials (or a foreign official in a similar status) by offering them any forms of profit with the purpose that this official would either take or refrain from taking certain actions while on official duty.

No new agency has been set up for implementation of the law or coordination activities. The President has the right to set up or periodically call for an inter-ministerial commission to fight corruption and drug abuse to coordinate activities of multiple organizations, which are given an anti-corruption mandate by the law. There are three key players - Office of the Chief State Prosecutor, Ministry of Internal Affairs, and State Security Council. It is anticipated that specialized units (assigned to fight corruption) will be set up within each of these three structures. The law also calls for establishing three databases (one per each respective agency) coordinated by an inter-ministerial commission.

The law regulates conflicts of interest, but restrictions are limited to spouses and close relatives only. Close relatives are not defined in the law, but one would expect that a son is a close relative. Nevertheless, the President appointed one of his sons as his deputy at the Security Council, which he chairs, through a presidential decree issued in January 2007<sup>10</sup>.

Moreover, another law on introduction of changes in some of the criminal laws adopted in December 2006 provides for exemptions to a certain category of citizens who become subject to a special treatment if they are involved in criminal cases. Such category includes government officials whose positions are included in the President's registry of staff, members of the Parliament and the Republican National Assembly, elected officials of self-administrations, judges, members of the jury, staff of the prosecutor's central and regional offices. Personal agreement of the President is required to arrest and prosecute anyone included in this exceptional category. The new anti-corruption law does not re-define criminal activity.

The law regulates disclosure of information - all government authorities must fill out income and properties declarations with indication of source of income. However, this information is treated as confidential and is not disclosed to the public. The only information disclosed to the public is the declaration on the source of income by presidential candidates during the election campaign.

The anti-corruption law foresees "forgiveness" to an individual (who is a private citizen, not a government official) involved in corrupt activities, if such individual voluntarily reports it and claims that he/she was blackmailed by the government official and had to comply.

Also, the law itself includes only references to administrative measures applied to the government or public officials. The Criminal Code, however, includes five to twelve years in jail accompanied by expropriation of estate for accepting a bribe.

The Office of the Chief Prosecutor is the lead agency for implementing the anti-corruption law and coordinating the work of all others involved. It is also responsible for developing a state anti-corruption program for 2007-2010. The Office of the Chief Prosecutor

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<sup>10</sup> President decree No. 3 dated January 5, 2007

intends to address four categories of corruption activities, (i) government corruption, (ii) corruption in business, (iii) corruption in law enforcement agencies, and (iv) corruption in the social sectors (health, education). The current assessment of the Chief Prosecutor is that in terms of the sectors of economy, the agriculture sector is the most corrupt one where the bribes to the harvest recording inspectors are still quite wide spread.<sup>11</sup>

A broad public awareness campaign has been launched to inform the population on the consequences of corruption, including prosecution and punishment.

Implementation of the new anti-corruption law will have direct impact on the Bank-financed portfolio in a form of increased level of scrutiny and layers of control.

## **PART 2: PUBLIC FINANCE MANAGEMENT**

### **Section 1: Budget Preparation, Execution and Controls**

#### ***Budget preparation***

In recent years, the coverage of the budget has been extended through incorporation of special funds (Social Protection Fund and innovation funds) into the budget. A few extra-budgetary funds managed by some ministries still remain, but the total amount of these funds is small. In 2006, however, a new fund, the National Development Fund, was created with earmarked revenues to finance socially important causes. Allocation decisions for this fund are made by the President.

The budget remains an annual exercise and allocations are made through an incremental process. The capacity of the Ministry of Finance to develop a macro-fiscal framework is limited. The preparation of the capital and current budget is the responsibility of two different ministries, Ministry of Economy (MOE) and Ministry of Finance (MOF), respectively, with little coordination among them. In 2005, the MOF has initiated a process of program budgeting, and the system is expected to be generalized in 2007.

Parliament is involved in the budget preparation process early in the cycle. A working group, including representatives from several committees, is established in April. The working group reviews the macroeconomic framework prepared by the Ministry of Economy and the draft budget proposals prepared by the Ministry of Finance. At some stage during the process, the President reviews the draft budget with the working group, which is enlarged to include representatives from the regions (*oblasts*). The budget is approved at a fairly aggregate level by the Parliament. In May of the following year, the Parliament approves a budget execution law.

#### ***Budget implementation***

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<sup>11</sup> Source: Interfax-Zapad news, January 17, 2007, Minsk



Once the budget is approved, the MOF sets the quarterly allocations for each budget unit. There is little flexibility in budget execution. Allocations can be revised, but prior approval of the Ministry of Finance is needed. A presidential authorization is required to move funds between the capital and the current budget. Allocations to items, such as wages, pensions and social assistance are protected and cannot be reduced. Controls are pervasive and detailed. The amount of documentation required for authorizing payments is substantial.

Progress has been made in recent years in reinforcing the operations of the Treasury, but weaknesses persist in financial planning and cash management. In 2005, the Treasury introduced an automated system for contract registration and commitment control, which helped strengthen fiscal discipline and reduce arrears. Integration of remaining extra-budgetary funds is underway, and should be completed in 2008. Consideration is being given to depositing local revenues into the Treasury Single Account (TSA). The TSA is held by the National Bank. In addition to the National Bank, the Treasury relies exclusively on a state-owned bank (Belarusbank)<sup>12</sup> for its banking operations. Such exclusivity is risky for the Treasury, however.

The Ministry of Economy is responsible for monitoring implementation of the capital budget. It prepares monthly, quarterly and annual reports which are sent to the President. The monitoring is mostly concerned with financial execution of the budget. Physical implementation is also analyzed, but the evaluation of the economic and social impact of projects is almost non-existent. The implementation rate of the capital budget reached 97 percent in 2006. This high rate is explained by several factors, including the fact that contractors (general contractors) must be generally appointed before any project is included in the daft budget in August of the previous year, and advance payments may be as large as 50 percent of the contract, and sometimes, even larger. General contractors are almost always state-owned companies, which are handpicked and assigned to an investment project rather than selected on competitive basis, as was done in the former Soviet Union. The President approves the list of projects with the names of general contractors and allocated budgets. National statistics on public procurement exclude such contracts, which therefore provide distorted information regarding publicly funded investment projects available for competition to the private sector (see the table on procurement in Annex 4). Furthermore, there is no transparency in how the general contractors are identified and on what basis the annual batch of multi-million dollar contracts are distributed among them.

### ***Financial Controls and Audits***

The Control and Revision Department (KRU) of the Ministry of Finance is responsible for internal audit and inspection of all central government entities and line ministry internal audit units. It has a staff of 360 people, most of them located in the regions. It is mostly focusing on compliance issues. In 2006, it has reported irregularities for a total amount of 13 billion Belarus rubles, which is equivalent to a modest US\$650,000. Most of these irregularities concerned housing allocations or subsidies for utility bills.

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<sup>12</sup> “Belarusbank” is a joint-stock savings bank with majority of shares owned by the state

The external audit function is the responsibility of the State Control Committee (SCC). The SCC reports directly to the President. Its chairperson is appointed by the President. Its role is to ensure that any entity using budget funds or state property adheres to the regulations. Its work plan is revised twice a year. A Coordination Council coordinates all state control bodies. The SCC's staff includes about 300 people at the central level and 700 at the regional level. The SCC carries out about 10,000 inspections per year. Economic operators, including retail stores, may be inspected. If violations are found, sanctions are immediate. If a crime is found, the SCC refers the case to the courts. As for the KRU, compliance with regulations is the main concern.

## **Section 2: Public Procurement**

Public procurement is at the center of the way public money is spent. Budgets get translated into services in large part through the workings of the procurement system. Procurement should also be considered as an integral issue in governance and anti-corruption strategies. Procurement practices that are not accountable, transparent and ethical help to reduce an environment within which inefficiency, including corruption, thrives. The CVS is not a substitution of the country procurement assessment where the main four pillars of a public procurement system are covered and analyzed<sup>13</sup>. Therefore, it covered only a limited number of areas that either directly or indirectly affect the Bank portfolio, or can help to understand certain implementation problems, which the projects are facing (please also refer to Part 3 on Bank portfolio). Public procurement system in Belarus can be characterized as weak.

### ***Regulatory framework for public procurement***

The regulatory framework includes multiple decrees and regulations (by President, Council of Ministers or line ministries) governing procurement of particular type of goods, works and services, as well as procedures for organizing and conducting tenders.<sup>14</sup> However, it lacks a single comprehensive public procurement law. The bidding procedures differ depending on the type of goods works or services procured. There are also multiple exceptions to these regulations. They do not apply to a long list of locally manufactured goods, in particular. Procuring entities must purchase the items from this list of domestically manufactured goods, or request a waiver to procure under a competitive method. The list is approved by the President to protect the domestic industry. Other exceptions include the assignment of capital projects to identified contractors (either state owned or private ones).

There are no separate regulations governing selection of consulting services. The same procedures applicable to procurement of goods or works also cover consulting services.

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<sup>13</sup> The main pillars of public procurement system are (i) the legislative and regulatory framework; (ii) institutional framework and institutional capacity; (iii) procurement operations and market practices; (iv) the integrity of procurement systems.

<sup>14</sup> The new public procurement provisions were established by the presidential decree No.529 came in force on December 8, 2006 and related resolutions of the Council of Ministers. The procurement rules described in the report refer to the new provisions.

Participation of international firms in public procurement is allowed. However, cumbersome registration requirements, domestic industry protectionism as well as application of domestic preference<sup>15</sup> under all competitive procurement methods result in an extremely low participation (less than 2 percent) of foreign firms in public procurement (further details on registration requirements for foreign contractors are provided in Annex 4).

The Presidential Decree No.529 defines the following procurement methods for goods, related works and services: (i) Competitive Bidding, (ii) Request for Quotations, (iii) Competitive List, and (iv) Direct Contracting. Competitive Bidding is a default method, but exceptions are so many that, by number and monetary value, they exceed the rule to apply a competitive method.

There are no defined procurement methods for construction works. The effective legal regulation require to carry out competitive bidding for contracts above US\$45,000 equivalent financed out of the republican budget, specialized budget, off-budget and innovation funds and external loans (Decree No.58). For other sources of funds the threshold is more than US\$700,000 equivalent.

The procuring entity (or Purchaser) is defined as a legal entity, a budget organization, or an individual, who has received funds from the state and/or local budgets (including from extra budgetary and innovation funds, external loans, preferential credits or line of credit) for the purpose of procurement of goods, works and services. Private firms can receive public funds in Belarus and, in such cases, must apply public procurement rules.

### ***Institutional framework and institutional capacity***

There is no public procurement agency in the country. The procurement department in the Ministry of Economy is responsible for developing procurement related regulations and decrees, and collecting the data and statistics on contracts awarded on the basis of these regulations.

Procurement of goods, works and services is carried out by the *Tender Commissions* established by procuring entities on a permanent or ad-hoc basis, when Competitive Bidding or Request for Quotations methods are used<sup>16</sup>.

Tender Commissions for procurement of construction works are appointed by procuring entities<sup>17</sup> and may include representatives of the State Construction Supervision Department of the Ministry of Architecture and Construction.

The State Control Committee (SCC), the State Security Council and the Ministry of Internal Affairs may decide to be involved at any stage of procurement process to exercise its oversight function. In addition, internal audit departments of line ministries or national state

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<sup>15</sup> Domestic preference is applied to procurement of goods when submitted bids offer items of domestic and foreign origin. A fixed margin of 15% is deducted from the bids offering domestically manufactured items.

<sup>16</sup> Establishment of Tender Commissions is governed by the Presidential Decree No.529

<sup>17</sup> Council of Ministers' Resolution No.235

agencies may decide to participate at any stage of the procurement process carried out by subordinated organizations.

In special circumstances, the members of the tender commissions are approved by the President. It is not specified, though, what these special circumstances might be.

*Approval of procurement decisions and contract awards* depends on contractual value. For example, decisions of the Tender Committees on award of contracts above US\$7.5 million equivalent are approved by the President, and awards of contracts between US\$2.9 and US\$7.5 million equivalent are approved by the Council of Ministers<sup>18</sup>. The approval procedure for award of contracts below US\$2.9 million equivalent differs depending on the size and nature of the purchase. In particular, high-value equipment<sup>19</sup> procurement is subject to a specialized expertise by the National Academy of Science. Procurement of goods included on the list approved by the Council of Ministers' Commission on strengthening of the competitiveness of the national economy is subject to the Commission's approval. Additional approvals by the regional or city of Minsk's executive committees is required if the procurement is done for these regions or Minsk.

The review and approval of contract award decisions for medical equipment contracts above US\$115,000 equivalent and for contracts for pharmaceuticals above US\$14,500 equivalent are conducted by the specialized Republican Tender Commission. The Regional or Minsk city Tender Commissions carry out same tasks for contracts of lower value.

Multiple layers of mandatory approvals of procurement decisions may cause significant implementation delays.

*Eligibility for bidding* is determined by the estimated value of the contracts. For procurement below US\$115,000 equivalent only Byelorussian bidders offering goods, related works or services originating from Belarus are eligible to bid<sup>20</sup>. When the required goods, related works or services are not produced domestically or produced in insufficient quantities, an exception can be granted to the procuring entity to allow procurement of goods, related works or services of foreign origin. Procurement above the said threshold can be done with participation of foreign bidders. However, as indicated earlier in this report, foreign firms have little interest to bid under public tenders in Belarus. Russian firms dominate in this minority group.

*Continuous professional development* of staff involved in procurement activities may address many of capacity related issues. However, in-country or abroad procurement training opportunities are not widely used by the procuring entities. Training of staff is mainly done on the job and is based on self-education. Funds allocated for training, especially abroad, are very limited. International study tours are strictly regulated.

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<sup>18</sup> Decree No.529. Thresholds are set up in "basic units". The current value of a basic unit is BYR31,000 (Belorussian Rubles) or about US\$14.5@ 2,142.0BYR/US\$)

<sup>19</sup> Decree No.259 (Section I, Clause 1) defines high-value equipment as that costs more than 30,000 basic units (or US\$435,000 equivalent) per equipment item.

<sup>20</sup>Decree No.529

### ***Procurement operations and market practices***

*Multiple regulations and frequent changes in the legislation* governing public procurement, contract management and pricing (or “taxation” of the contracts) make the procurement cycle difficult to manage, time-consuming and expensive. One recent example is the presidential decree issued in August 4, 2006 (Decree No.499), which introduced a new tax in the amount up to 13.5 percent of the cost of production, to be added to the contract amount and earmarked for payments into a new Innovation Fund established by the government. This applies to the contracts co-financed by the World Bank.

Procuring entities have to constantly monitor new rules and the changes in the national legislation, assess the impact of such changes on project implementation and contracts administration, and adjust internal business processes to incorporate relevant changes in the bidding documents and contract forms. Procuring entities rarely have resources and in-house capacity to carry out such work. In most cases they lack funds to outsource this service to a specialized firm.

Another feature of the public procurement system is *controlled prices* (or tariffs) set up for “*socially significant*” goods and related services items. The list is approved by the President or, by delegation, the Council of Ministers.<sup>21</sup> Civil works are mostly affected by it. The Ministry of Architecture and Construction, together with the Ministry of Economy are responsible for regulating prices in the construction industry, except for construction projects financed by foreign investment. Council of Ministers’ regulation (No.235) spells out how the contract price is established and payments to the contractors are made. According to this regulation, the cost estimates and bidders’ prices are calculated on the basis of the approved project documentation using a base-index method. Prices of year 1991 are used as a base and are adjusted using the indexes approved and periodically updated by the Ministry of Architecture and Construction. This approach leads to underestimation of project and contract cost (windows replacement contracts under the Bank-financed Retrofitting project is an example).

Another area that affects Bank-financed contracts is *contracts registration and customs clearances*. Bank-financed projects are subject to all applicable custom duties, taxes, fees and other levies imposed on imported goods. The only difference is a minor simplification of document processing required for imported goods. For example, a contract certificate (*passport sdelki*) is not required<sup>22</sup>. With regard to goods registration there are no exceptions for Bank-financed projects.

Actually, if all documents are well prepared and customs duties and fees are paid, customs clearance can be completed within two-three working days. Certification process, including approval of the technical design for works contracts (including registration of

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<sup>21</sup> Law “On price formation“, May 10, 1999 ( Presidential decree No.285)

<sup>22</sup> Presidential decree No.7 (as amended), dated January 4, 2000: “On improvement of order on operation and control of foreign trade transactions”; and Regulation of the State Customs Committee No.32 dated July 7, 2001: “On order to foreign exchange control by customs offices”

equipment and goods supplied under such contracts) is done by the specialized committees and can take more than a month.

*Payments regulations* that affect the Bank-financed contracts are those related to foreign exchange transactions and comprise numerous legal acts imposing a number of restrictions on such transactions. The following areas are identified as those having significant impact on payment and delivery terms in the Bank-financed contracts:

- (a) Payments in foreign currency between Byelorussian residents are not allowed except for the cases identified in the law (Bank-financed projects do not fall under these exceptions, so the law applies in full)<sup>23</sup>;
- (b) The amount of advance payment in foreign currency to non-residents is not restricted by national legislation, but regulated by contractual provisions. Nevertheless, the terms for delivery must not exceed 60 days from the date of an advance payment for imported goods, and 90 days for works and related services<sup>24</sup>. The above terms maybe extended with a special permission from the Ministry of Trade. If this period exceeds 180 days approval of the National Bank is required<sup>25</sup>.
- (c) “Off-shore charges” at 15 percent rate of the paid amount are imposed on Byelorussian residents (firms and individuals) when payments are made to off-shore zones listed in the presidential decree No.353 (May 25, 2006).
- (d) Payment to non-residents in foreign currency for goods, works and related services originating from Belarus (including delivery of these items by local subcontractors or partners) is a problematic area not clearly defined by the national regulations. This affects foreign suppliers and contractors who are left with no choice but to enter into contracts jointly with local firms if they want to get a contract in Belarus.

### ***Integrity of the public procurement system***

The integrity of the procurement system is measured by (a) the existence of effective control and audit systems, (b) the existence and efficiency of the appeals mechanism, (c) the degree of access to information, and (d) the existence of ethics and anti-corruption measures. Regulations are posted on the government website <http://www.pravo.by>. Key regulations applicable to procurement of goods and works are listed in Annex 4.

(a) *Inspections and Audit of Procuring Entities* is done by many agencies and can be planned or ad hoc. There is a rigid government control over investment project activities; including up to six layers of external control over project implementation (applies to the Bank-financed projects as well):

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<sup>23</sup> Law “On foreign exchange regulation and control”, July 22, 2003

<sup>24</sup> Presidential decree No.7 “On improvement of order on operation and control of foreign trade transactions” ( Clause 2.6), January 4, 2000

<sup>25</sup> Presidential decree No.7 “On improvement of order on operation and control of foreign trade transactions” ( Clause 2.8), January 4, 2000; and Regulation of the Ministry of Trade No.1 dated January 4, 2002

- *Commission on International Technical Assistance under the Council of Ministers* carries out control following project's completion. It also requires semi-annual reports during project implementation to monitor the status;
- *State Control Committee (SCC)* can carry out control at any time based on their own schedule;
- *Integrated Control* can be undertaken by the decision of the Council of Ministers (CM) and carried out by the agencies appointed by the CM;
- *Police department on fight against economic crime* can undertake control based on own decision (if it finds an inspection necessary);
- *State Security Committee ("KGB")* can undertake control if it finds it necessary;
- *Ministry of Tax Collection* controls the use of budget resources.

In addition, an implementing agency is required to submit semi-annual project implementation reports to the Ministry of Economy and monthly or quarterly reports to the line Ministry. (More details on inspections and audit of procuring entities are provided in Annex 4).

(b) *The Appeals and Complaints* system<sup>26</sup> includes the right of the bidders to appeal to the head of the procuring entity, supervisory authority of the procuring entity, or file an arbitration case before the contract is signed. One exception is procurement conducted under competitive bidding method. In such cases appeals can be made at any time and the court has the right to cancel the award decision at any stage, including after tender completion, if it determines the process did not comply with the applicable regulations. Details of appeals and complaints mechanism are provided in Annex 4.

(c) *Advertisement of tenders* in the national press is the norm. However, since large investment contracts are excluded from competitive selection of a prime contractor, this applies to relatively small value contracts (besides contracts financed by donors).

*Electronic procurement* is non existent.

(d) *Anti-corruption law* was enacted in 2006 and described in Part 1, Section 2 of this report.

## **PART 3: THE BANK PORTFOLIO**

### **Section 1: Implementation experience**

The CVS team did not make a detailed review of contract files and comparison between the invoices submitted and payments made. It is not, therefore, in a position to assess whether there was any leakage of project funds during contract implementation. On the surface, it seems there is an issue with inefficient use of project funds due to weaknesses in procurement management and contracts administration, rather than opportunity for corruption.

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<sup>26</sup> Appeals and complaints are regulated by decree No.529 (Tender Provisions)

The Belarus portfolio includes two projects, the Social Infrastructure Retrofitting Project (SIRP) approved in June 2001 and the Post-Chernobyl Recovery Project (PCRP) approved in April 2006 and a (closing) small GEF grant provided to the Ministry of Natural Resources and Environment to address the issue of pesticides. Both projects are fully in line with the Country Assistance Strategy (CAS) for Belarus, which was reviewed by the Board in March 2002. In 1997, a Memorandum of Understanding (MOU) was signed between the Bank and the Government of Belarus. According to the MOU, the Bank's lending to Belarus was conditioned on the unification of the exchange rate in order to reduce the severe distortions in the economy. Significant progress was made on exchange rate reform prior to CAS approval, which enabled the Bank to proceed with a low case scenario of one project a year, centered on global public goods. While Belarus has made further progress on economic reforms, it has not yet met the triggers (satisfactory macroeconomic environment, adequate progress in improving the business environment and improved accountability in public finance management) for moving to the base case scenario under the 2002 CAS.

The two ongoing projects have similar objectives. They both seek to improve the living environment of the population through more efficient use of energy. The risks for the first project were considered at inception as modest. The procurement risk was assessed as high, however, because Belarus had limited experience in competitive procurement at international level. Before the project, the government agency (RUE "Belinvestenergosbereshenie" of the Committee on Energy Efficiency), which eventually became responsible for project implementation, awarded contracts only to state-owned contractors, in line with local practices. This changed during project preparation, however, as the agency had to use the World Bank's procurement guidelines starting from the PPF financing. Contracts were smaller than those envisaged under the project, however, and the project appraisal document (PAD) expressed concern with the limited capacity of local contractors. To ensure that financial procedures would be up to standards acceptable to the Bank, an action plan was agreed and implemented. A project implementation unit was established within the "Belinvestenergosbereshenie" of the Committee on Energy Efficiency and the Bank procedures were to be applied.

The risk analysis for the Post-Chernobyl Recovery Project focused on possible radioactive contamination in the project area and the demand for gas, as a substitute to wood for heating purposes. The assessments of financial management and procurement carried out during project preparation concluded that the arrangements which were put in place under the SIRP and would continue under the new project were acceptable. No issues had arisen in the audits of the SIRP either. As concerns procurement, key issues and risks were identified and centered on the participation of subsidiaries of Beltopgas, an agency of the Ministry of Energy. The overall project risk in the fiduciary area was rated as moderate.

The SIRP's implementation has been much slower than anticipated so far, which is understandable for a country with almost no prior experience with the Bank-financed projects. The loan became effective more than six months after Board approval. No less than three presidential decrees were needed to meet the general conditions for effectiveness. The most recent Implementation Status Results and Report (ISR), dated November 18, 2006, indicated a disbursement lag of 28 months. It also showed that, about one month before the initial closing date of the SIRP, the number of beneficiaries (111,200) was much lower than expected at the



end of the project (200,000). Energy savings were also much lower than expected (55,665 mWh versus 192,000 mWh). The project (SIRP) was nevertheless rated as satisfactory for both development objective and implementation progress. Critical legal covenants were reported as complied with. All aspects of implementation were rated as satisfactory, including co-financing, procurement and financial management. This does not seem to match the reality, which is characterized by chronicle delays with timely provision of co-financing funds leading to multiple amendments on each contract's completion date in majority of the cases. Since the contracts foresee monthly indexation of prices expressed in local currency, such multiple extensions of closing dates led to an increase in the final cost of investments. As the signed contracts were not completed on time, a one-year extension of the closing date was approved in December 2006. Supplemental financing was requested by the Government to cover the cost overruns and include additional sites to meet the project's development objectives. Closing date extension and supplemental financing could have been avoided through better procurement management and supervision by the implementing agency and the Bank.

The authorities have not issued the certificate of acceptance for a number of facilities financed under the SIRP. For instance, some boilers cannot operate because a critical element, which was not included in the contract, such as the connection to water or electrical source is missing. Lighting systems were renovated, but the electrical circuits were not updated. As a result, the systems do not meet current regulations. Such situation can put a reputation of the Bank at risk. Since the additional financing is envisaged, part of it can be used to ensure that all facilities financed under the project are fully operational.

The following problems have been identified during the CVS review<sup>27</sup> as project implementation problems while in any other country these would be corruption risk red flags:

- (a) Low interest of foreign companies to bid under Bank-financed contracts conducted under International Competitive Bidding (ICB) due to cumbersome procedures and high overhead costs associated with requirements to implement contracts in Belarus;
- (b) Weak capacity of the local private sector, as few contractors are qualified to meet ICB requirements;
- (c) Financial requirements which local bidders can not meet (turnover, minimum cash flow, ability to obtain bank guarantees);
- (d) Low advance payment (compared to local industry standards) and a mandatory requirement to have an advance payment supported by the bank guarantee for the same amount;
- (e) The need to obtain a great number of authorizations (land permits, construction permits, etc.), including general contractor state license for contracts above US\$2.5 million equivalent, which is allegedly almost impossible for a private firm to get without having "the right connections" to the government;

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<sup>27</sup> While conclusions are made based on the review of the SIRP, Chernobyl project will be facing similar problems due to the similar nature of planned procurement activities, unless the changes in how procurement process is organized and conducted are introduced to remedy the situation.

- (f) Poor quality of design documents and use of price indexation for cost estimates resulted in a large number of variation orders on the basis of sometimes questionable or unverified justifications and contract amendments to increase the contract price;
- (g) Language of procurement documents (ICB documents used to be issued in English language only since SIRP fell under pre-May 2004 procurement guidelines);
- (h) Long delays between bid evaluation and contracts' signing;
- (i) Large number of amendments to signed ICB contracts, mainly due to delays with co-financing funds and failure of local authorities to provide for a connection to utilities, or obtain required permits and licenses to start the works;
- (j) There seems to be no monitoring and analysis of actual payments made vs. physical progress (status of physical completion) under the signed contracts;
- (k) The implementing agency became too involved with contractors, such as trying to resolve contractors' problems with cash flow and finding sub-contractors' replacement, during contract implementation. Contract administration might have involved too many mutual favors, such as contractors not claiming the interest for delayed payment of invoices and the implementing agency not applying the contract's provisions related to liquidated damages in case of delays with the completion;
- (l) There were instances of disconnect between contract terms based on the provisions of the Bank's standard bidding documents and limitations imposed by local legislation (in particular, in regard to contract effectiveness conditions, payment and delivery terms). Legal advice was not available to the implementing agency in the area of changes in applicable rules and regulations. The latest example was a contract with a joint venture (Poland/Belarus) with the contract signed in Euro (which was the currency of the bid). While the Bank guidelines allow payments in the currency of the bid, the local legislation consider payments to the local partner of the joint venture as illegal. Payment of the entire contract amount to the Polish partner was envisaged as a solution to the problem on a condition that he pays his local partner for his share, but this failed through as such option would have been considered as money laundering<sup>28</sup>. After long delays and attempts to remedy the situation, the contract had to be cancelled as the joint venture was no longer interested to supply equipment under the quoted prices.

The CVS team recommends that implementation problems encountered by SIRP and described earlier in this section be reviewed by the sector unit in consultation with the country management and the Regional Procurement Manager. The loan agreement should be amended if needed to accommodate required changes and introduce more relevant procurement methods than currently used.

## **Section 2: Financial Management**

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<sup>28</sup> Any payments in Byelorussian roubles from abroad to a local company (except for Russia and Ukraine) are prohibited by the law.

The financial management of the three ongoing projects (including a GEF grant-funded project, which was managed by a project unit in the Ministry of Natural Resources and Environment - POPs) is supervised by the Bank office in Kiev. The Financial Management Systems, including accounting, reporting, budgeting and staffing of the project units are found satisfactory. These units have sufficient internal controls and procedures for project's implementation. All three Projects are in compliance with the financial covenants in the relevant Project and Grant Agreements. Each unit has a disbursement specialist, who is sufficiently qualified. The disbursement specialists are responsible for all accounting, reporting, including reporting, submission of disbursement applications and external audit.

Internal controls in the project unit for SIRD and PCRDP include bank reconciliations after each bank statements, reconciliation of monthly summary of transactions from the Bank to own records though access to client-connection, authorizations of disbursement applications, automatic generation and authorization of SOEs, reconciliation of bank balances after each transaction, and regular reconciliation between the two accounting modules used by the Project. In addition, each payment is made only after necessary certification by a technical specialist and a procurement specialist that the goods/services received are of appropriate quality and that they meet specifications in the loan agreement. PriorBank, where the special account for SIRD has been opened, is also provided with copies of contracts and acts of work done/services received, which enable the bank to ensure that correct payments are made.

Controls in the GEF-funded project include: necessary certification by technical specialists that the goods/services received are of appropriate quality; verification by consultants in the project unit of work/goods receipt to the terms stated in the contract; authorization of payments by the chief accountant of the Ministry of Natural Resources and the Minister; reconciliation of own records to the Bank's records through access to Client-connection; reconciliation of SOE to the bank statements each time during preparation; reconciliation of bank balances by review of bank statements received from the bank either by receipt of hard copy of bank statement or through client-bank program.

Separate Special Accounts are maintained for SIRD and POPs in a commercial bank in Belarus (PriorBank). Transit accounts have been opened and are maintained in the same commercial bank. The special account for PCRDP has not been yet opened. Belinvestbank has been pre-selected. The procedures for review of acceptability of this commercial bank are in process.

Project units submit regularly project management reports (each semester for SIRD and each quarter by POPs). The reports cover sources and uses of funds, uses of funds by project component, physical progress report and special account statement. These reports were found satisfactory. Minor changes were recommended by Bank staff to improve the content. The reports are submitted to Ministry of Finance, the relevant technical ministry, and other controlling authorities as required by the national legislation.

Deloitte and Touche has been appointed to audit the accounts prepared by the project unit for SIRD. The audit reports for the past three years were unqualified. No management letter was provided for the 2004 and 2005 accounts. A management letter was issued for the 2003 accounts. It noted (i) that project financial statements contained errors in closing balances; (ii) mistakes in submitted withdrawal applications; (iii) that the accounting system was not fully upgraded to do reporting automatically; and (iv) an incorrect exchange rate was used to present

year – end bank balances. The audit of the 2005 accounts of POPs was waived in 2006 due to insignificant disbursements.

## ANNEXES

### ANNEX 1. LIST OF PEOPLE AND ORGANIZATIONS MET

#### *Parliament*

Mr. Sergei Kiselev, Chairman of the Standing Committee on Budget, Finance and Tax Policy  
Mr. Viktor Marakhin, Deputy Chairman

#### *Council of Ministers*

Mr. Stanislav Chernousov, Deputy Head, Department of Fuel and Energy Sector  
Ms. Galina Gurjanova, Department of Health, Social Security and Chernobyl Challenges  
Ms. Viktoriya Goulko, Chief Expert, Division of Cooperation with IFIs

#### *State Control Committee*

Ms. Raisa Savritskaya, Vice-Chairperson  
Mr. Alexander Vlasov, Head of the Division for Supervision of Fuel and Energy Sector  
Mr. Victor Laptev, Deputy Head of the Division for Supervision of Fuel and Energy Sector

#### *National Prosecutor's Office*

Mr. Victor Morozov, Head, Department to Combat Organized Crime and Corruption  
Ms. Irina Dudareva, Head, Appeal Unit, Department for Ensuring Prosecutor's Engagement in Criminal Cases Investigation  
Mr. Alexander Vasko, Deputy Head, Department for Supervision of Banking Regulations Enforcement  
Mr. Igor Romanenko, Deputy Head, International Legislation Department

#### **Ministry of Finance:**

Elena Zhukova, Head, Division of Foreign Debt and Credit  
Inessa Prokhorova, Advisor, Department of Emergency Situations and Capital Investment Financing  
Karolina Voitko, Consultant, Division of Foreign Debt and Credit  
Maria Chaikovskaya, Deputy Head, State Audit Department

#### **Ministry of Economy**

Ivan Belchyk, Department for Cooperation with International Organization and TA Coordination  
Sergei Trafimovich, Head, Main Investment Department  
Viktor Filatov, Chief Economist, Department for Investment Cooperation and Free Economic Zones  
Tatiana Kozlovskaya, Head, Department of Trade and Public Procurement

#### **State Standardization Committee**

Valeriy Koreshkov, Chairman  
Victor Nazarenko, First Deputy Chairman  
Victor Degalevich, Head, Department of Construction Supervision  
Lev Dubovik, Head, Department of Energy Efficiency  
Andrei Minenkov, Head, Department of Scientific and Technical Policy and Foreign Economic Relations, Department on Energy Efficiency

***RUE “Belinvsetenergoberezhnie”***

Mr.Alexander Savanovitch, Director  
Mr.Vladimir Voitekhovich, Deputy Director  
Mr.Alexander Zhed, Procurement Specialist  
Ms.Ksenia Moroz, Procurement Specialist  
Ms.Maria Fedosyuk, Procurement Specialist  
Ms.Marina Borbat, Disbursement Specialist  
Mr.Andrei Minenkov, Head, Department of Scientific and Technical Policy and Foreign Economic Relations, Department on Energy Efficiency, State Standardization Committee

***Ministry of Natural Resources and Environment***

Mr.Alexander Apatsky, First Deputy Minister  
Ms.Alina Bushmovich, Lead Specialist, Waste Management Department  
Mr.Sergei Kuzmenkov, Deputy Head, Waste Management Inspection  
Ms.Olga Mitakovich, Lead Specialist, Center for International Environment Projects, Certification and Audit “Ecologiainvest”  
Mr.Yuri Soloviev, Project Manager, GEF POPs Enabling Activity

***European Bank for Reconstruction and Development (EBRD)***

Ms.Renata Iksar, Analyst

***USAID/US Embassy***

Mr. Chuck Howell, Country Representative  
Mr. Alexander Chirkov, Project Management Specialist

***United Nations Development Program ( UNDP)***

Mr.Levan Bouadze, Deputy Resident Representative  
Ms.Valentina Stalyho, Program Manager, Country Office in Belarus  
Mr.Vladimir Scherbov, Adviser to the UN Resident Coordinator

***Republican Design Unitary Enterprise “Belgosproekt”***

Mr.Gennady Kurochkin, Director  
Mr.Yury Belousov, Chief Engineer  
Mr.Gennady Zubov, Chief Engineer (project manager on Bank-financed design contract)

***FobosIntergaz***

Mr.Gleb Zhukov, Director

***Deloitte & Touche, Belarus***

Mr.Vitaly Radievsky, Director, Audit  
Mr.Viktar Kiyenia, Manager, Audit

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## ANNEX 2. LIST OF BACKGROUND MATERIALS AND DOCUMENTS REVIEWED

### World Bank Group:

- Financial sector assessment (June 2006)
- Country Economic Memorandum (Nov. 2005)
- Business Environment in Belarus (June 2005).
- Poverty Assessment (Nov. 2004).
- Strengthening Public Resource Management (Jun. 2003)
- ICT Infrastructure and E-Readiness Assessments in the Republic of Belarus (Apr. 2003)
- Improving the Business Environment (Jan. 2003)
- Country assistance strategy (March 2002)
- World Bank Group's Doing Business database
- EBRD-World Bank Business Environment and Enterprise Performance Survey and BEEPS at glance
- EBRD-World Bank Life in Transition Survey
- Project Appraisal Documents for Post Chernobyl Recovery and Social Infrastructure Retrofitting Projects; ISRs and progress reports prepared by the implementing agency

### IMF:

- Article IV Consultation (Aug. 2006)
- Selected Issues (Aug. 2006)
- Statistical Appendix (Aug. 2006)
- Monetary Transmission Mechanisms in Belarus, (Nov. 2006)
- Financial Sector Assessment Program May 2006)
- Financial System Stability Assessment (June 2005)

### Other Sources:

- Freedom House Nations in Transit
- Economist Intelligence unit
- Global Insight
- United States State Department "Doing Business in Belarus: A Country Commercial Guide for U.S. Companies (2006).
- Mises Center. "State of Corruption in the Republic of Belarus" (2006). Liberty-Belarus.info
- Grigory Ioffe "Unfinished Nation-Building in Belarus and the 2006 Presidential Election," *Eurasian Geography and Economics*, (2007), 48, No. 1, pp. 37–58.

### Official Documents:

- Belarusian legislation (in Russian): [www.pravo.by](http://www.pravo.by). Public procurement legislation (in Russian) at <http://www.pravo.by/classifier/classif.asp?code=04.01.06> ( public procurement legislation and procurement in civil works area)
- Anti-corruption law, July 2006
- Public procurement regulations (see Annex 4 for detailed list)
- State Control Committee inspection report on SIRP (December 2006)

**ANNEX 3: PERCEPTIONS OF CORRUPTION** – (see Part 1, Section 1 of the main text)***Box 1: A self-fulfilling spiral?***

The Transparency International Corruption Perceptions Index (TI-CPI) aggregates available assessments of corruption from expert opinion sources and from surveys to arrive at an index ranging from 1 (most corrupt) to 10 (least corrupt). One of the sources included in the TI-CPI is the assessment generated by Freedom House Nations in Transit (FH-NIT). The FH-NIT assessment of “corruption” goes from 1 (least corrupt) to 7 (most corrupt). While TI-CPI is a function of FH-NIT by construction, it is also apparently true that FH-NIT is a function of TI-CPI.

2003: FH-NIT downgrades Belarus to a 5.50 without giving a reason for the downgrading. The explanation for the rating is full of references that conflate economic and business environment weaknesses with corruption.

Later in 2003: TI-CPI, which includes the FH-NIT scores, ranks Belarus 53/133, with a score of 4.2.

2004: FH-NIT downgrades Belarus to a 5.75, citing the slide in TI-CPI: "Surveys conducted by international agencies indicate a relatively low level of grand corruption in Belarus. Thus, the 2003 Corruption Perceptions Index of Transparency International places Belarus above all former Soviet states and even some of the new members of the EU. This low level of grand corruption can be explained by the absence of powerful business groups and oligarchies, which leaves bureaucrats without a range of corruption opportunities common to distorted capitalist economies. Moreover, corruption-prone institutions--such as the Parliament and political parties--play no serious role in Belarus. Belarus's rating, however, has seriously deteriorated since the 2002 survey, sliding to 51 from 36."

Later in 2004: TI-CPI, which includes the FH-NIT scores, ranks Belarus 74/146, with a score of 3.3

2005: FH-NIT again downgrades Belarus to a 6.00, again citing TI-CPI: "Although Belarus remained above all other former Soviet republics in the 2004 Corruption Perceptions Index of Transparency International, its rating deteriorated dramatically from 51st place in 2003 to 71st in 2004. This continued its slide from 36th place in 2002."

Later in 2005: TI-CPI, which includes the FH scores, ranks Belarus 107/159, with a score of 2.6.

2006: FH-NIT again downgrades Belarus from a 6.00 to a 6.25, again citing the TI-CPI, starting the explanation as follows: "Belarus continued its precipitous decline in Transparency International's Corruption Perceptions Index in 2005; its rating deteriorated to 107th place, down from 36th place in 2002." Most of the rest of the explanation focuses on the poor ratings Belarus receives in Doing Business.

July 2006 (published in November 2006): TI-CPI, which includes the FH scores, ranks Belarus 151/163, with a score of 2.1. Moreover, TI-CPI decides to drop BEEPS from consideration in part because they don't like the responses for Belarus. The score for Belarus became a ranking based entirely upon foreign experts' opinion, since BEEPS was the only cross-national survey undertaken in these countries.



Figure 1. Assessments of "Corruption" and Related Policies by Foreign Experts

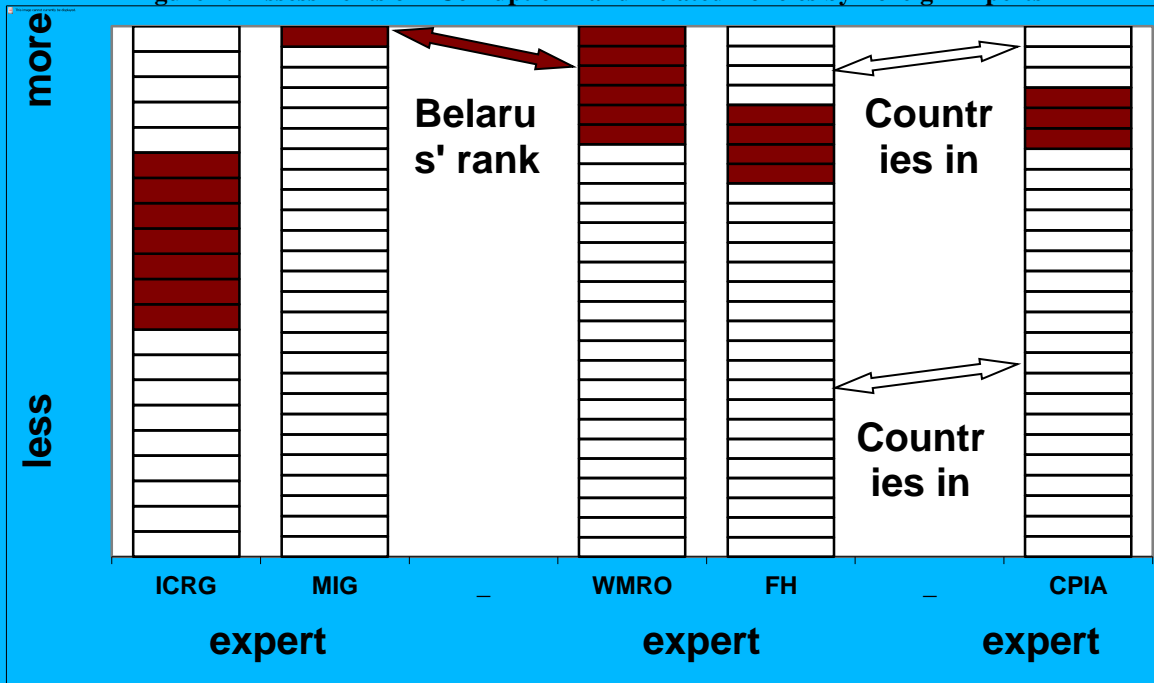


Figure 2. Red Tape and Incentives for Corruption (Doing Business), 2006

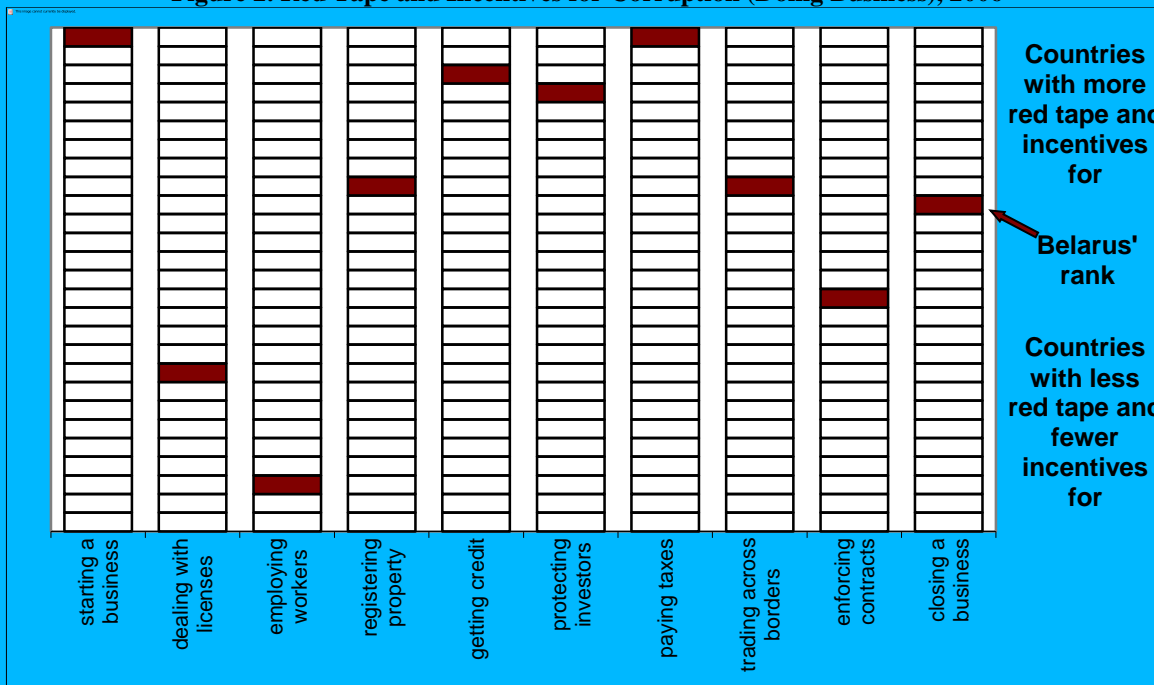


Figure 3. Household Level Bribe Frequency According to Citizens in Surveys, 2006

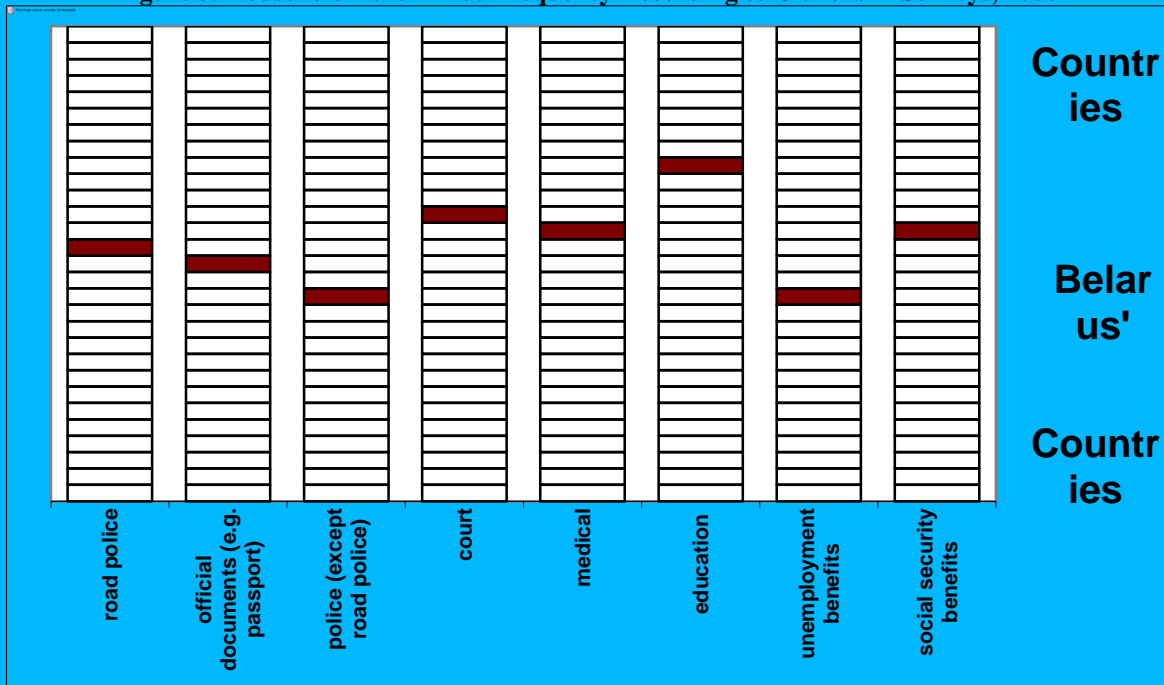
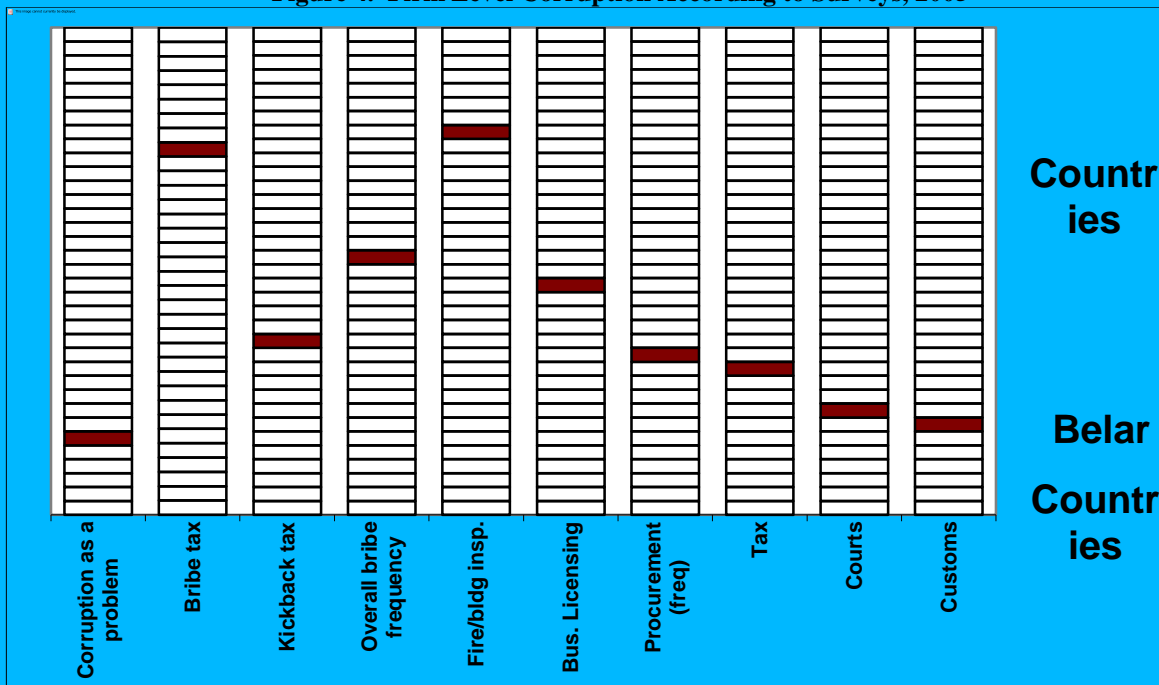


Figure 4. Firm Level Corruption According to Surveys, 2005



## ANNEX 4: PUBLIC PROCUREMENT

**1. Official Statistics on Public Procurement financed by the republican budget, specialized budget, off-budget and innovation funds and external loans (exclude investment works contracts assigned to identified prime contractors by decision of the Council of Minister and the President)**

	2003		2004		2005		2006	
	number	%	number	%	number	%	number	%
Number of tenders	85,911		163,276		204,871		244,044	
<b>Open Tendering</b> <sup>29</sup>	659	0.80	1,193	0.73	2,960	1.45	4,276	<b>1.55</b>
<i>Limited Tendering</i>	22	0.03	39	0.02	62	0.03	119	0.04
<i>Simplified Procedure</i>	1,158	1.30	1,175	0.72	1,036	0.50	1,137	0.46
<i>Negotiation</i>	357	0.40	732	0.45	5,483	2.68	7,466	3.05
<b>Direct Contracting</b>	83,715	97.40	160,137	98.10	195,330	95.34	231,046	<b>94.70</b>
Number of bidders:	101,163				247,667		303,814	
<i>local bidders</i>	98,255	97.10		97.90	242,943	98.00	300,846	99.00
<i>foreign bidders</i>	2,908	2.90		2.10	4,724	2.00	2,968	1.00
Russia and other CIS	2,033	69.90		53.50	3,227	68.30	1,303	44.00
other countries	875	30.10		46.50	1,497	31.70	1,665	56.00
Proportion of goods (works, services) of local origin				about 60		60.00		72.30
Number of concluded contracts	86,187		163,305		205,475		244,505	
Value of concluded contracts, in billion of B. Rubles	1.30		2.00		3.50		5.30	
Proportion of centralized procurement (number)				3.30		6.10		2.90

<sup>29</sup> Procurement Methods used for statistics are from the previous edition of the Public Procurement Provisions effective until Presidential Decree No. 529 (December 8, 2006).

	2003		2004		2005		2006	
	number	%	number	%	number	%	number	%
Proportion of centralized procurement (value)				23.40		32.10		23.80

The Ministry of Economy's explanation for the large number of direct contracts was that these are small value contracts only (below the open tendering threshold of about Euro7,500 equivalent) which do not require competitive selection.

## 2. Registration of Foreign Contractors

All contractors require a construction license in order to operate in Belarus<sup>30</sup>. In addition, for contracts above about US\$2.5 million equivalent, a general contractor's license shall be obtained. The law provides for a foreign entity to apply for a prime contractor's license in case such entity is a successful bidder in the international competitive bidding process conducted in accordance with the applicable national legislation. If any foreign bidder is awarded a contract and obtains a prime contractor's license, it shall establish and registry an office (a representation) in Belarus<sup>31</sup>. It shall be done prior any works on the signed contract can commence. The representative office is not considered a legal entity and can only act on behalf of the organization that it represents. The office shall be also registered as a tax payer in the tax administration and other agencies within tight period of time required by the legislation. It shall comply with all normative acts of Belarus in regard to accounting, taxation and other mandatory payments (for example, to Investment Fund) as per the national legislation currently in force.

## 3. Appeals and Complaints handling system<sup>32</sup> includes the following

(a) Procurement of Goods (and related works and services). The bidders have the right to appeal the award decisions made by the Tender Commissions to complain to the head of the procuring entity, supervisory authority of the procuring entity, or file an arbitration case before the contract is signed. One exception is procurement conducted under competitive bidding method. In such cases appeals can be made at any time and the court has the right to cancel the award decision at any stage, including after the tender completion, if it determines the process did not comply with the applicable regulations. This provision is not extended to any other competitive procurement methods, making it easier for procuring entities to deal with complaints. Similar principles were used to handle bidders' claims under the previous public procurement regulations. It is not surprising that the open tendering (competitive bidding) method is the least popular among the procuring entities who are trying to avoid it at all costs (see Annex 4 for statistics on the use of different procurement methods). Moreover, conflicting

<sup>30</sup> Presidential Decree No.17 dated July 14, 2003, and Council of Ministers' Regulation No.1386 dated October 20, 2003

<sup>31</sup> Council of Ministers' Regulation No.929 "Provisions on order on opening and operation of representative offices of foreign organizations in the Republic of Belarus" dated July 22, 1997

<sup>32</sup> Appeals and complaints are regulated by decree No.529 (Tender Provisions)

regulations governing procedures for award notification and timing of the contract signing following the award make the complaint handling mechanism less transparent and cumbersome for the bidders to follow. For example, the procuring entity must, within three working days from the date of award decision (or approval of award decision) under competitive bidding procedure, notify the bidders about the outcome. At the same time the same decree mandates that notifications are sent to all bidders within three working days following contract signing (or making a decision other than award recommendation).

Under Request for quotations method, notification letter accompanied by the signed contract is sent to successful bidder only. All other bidders are notified only after the contract signing. For all other competitive method, the award information is provided only upon request (of unsuccessful bidders) after the contract is signed.

Head of the procuring entity or his/her supervising entity has the right to suspend procurement process for 7-30 days following receipt of a complaint on an competitive bidding procedure. This does not apply to projects for which completion deadline is set up by the President or the Council of Ministers. Procuring entity is responsible for recording the complaints and justification of not using the suspension. Such justification may be appealed in court.

Signed contracts can not be terminated in case of substantiated complaint. Bidder may start the litigation process against the procuring entity or its supervisory organization and claim compensation of losses or damages under competitive bidding.

Also, the bidders have the right to report any violations of the Tender Provisions to control authorities such as the State Control Committee, the Chief Prosecutor's Office, the Ministry of Internal Affairs, etc., who, in turn, are responsible to examine the facts within 30 days. If any violations are confirmed prior to the contract signing, the award decisions of the open tenders can be annulled and the actual damages to the bidders can be compensated in cases prescribed by the applicable legislative acts.

(b) Procurement of Civil Works. The Tender Provisions on procurement of civil works do not define in details complaint handling mechanism and merely refer to legislation in force<sup>33</sup>.

#### ***4. Inspections and Audits of Procuring Entities***

Control over economic activities of procuring entities and, especially, implementation of capital investment projects is very heavy. Presidential decree No.673 "On certain measures to improve coordination of activities of controlling agencies of the Republic of Belarus and order to impose economic sanctions" dated November 15, 1999 is the main governing document. In order to coordinate work of multiple controlling authorities, the President has established a Coordination Council (the Council on coordination of controlling activities in the Republic of Belarus) which comprise executives from the Council of Ministers, President's Administration, Chief Prosecutor's Office, State Control Committee, National Bank, State Security Agency, Ministry of Internal Affairs, Ministry of Tax Collection, Ministry of Finance, Ministry of Economy and State Customs Committee. The Council is headed by the Chairman of the State

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<sup>33</sup> Resolution of Council of Ministers No.235 "on Tender Provisions" dated March 3, 2005

Control Committee (unless otherwise decided by the President). The members of the Council are approved by the President based on a recommendation of the Chairman.

The *control inspections* (audits) can be planned and ad hoc. The planned inspections (audits) are those included in a coordinating plan of controlling activities in the Republic of Belarus or a region or Minsk city provided that a controlling authority specifies the scope of inspection, entity which will be inspected and terms of reference for the inspection (audit). All other inspections are ad hoc.

The planned inspections of the same entity can not be carried out more than once a year.

The ad hoc inspections are conducted only as a reaction to on the instructions of the President himself, the Prime Minister or his deputies, the Chairman of the State Control Commission or his deputies<sup>34</sup>. The exceptions are the inspections required by the tax legislation. The controlling authorities must inform the Council and agree on ad hoc inspections. The following instances can trigger an unplanned inspection: (a) legal entity has been reorganized or is closing down, (b) business activities of entrepreneurs are stopped, and (c) one of the controlling authorities got information pointing to violation of the legislation or received a complaint (or an appeal) that requires an investigation.

The inspected entities receive an inspection report stating the findings and the decisions which they can appeal. The appeal can be made to a superior controlling authority or the Coordination Council, except for decisions on ad-hoc inspections conducted by the request of the President, the Prime Minister and his deputies, the Chairman of the State Control Committee and his deputies, and the Chairman of the Coordination Council.

Duration of inspections shall not exceed 30 days but may be extended by the head or the deputy head of the controlling authority if more time is required.

While the decree lists the main controlling authorities, it can be expanded to include organizations to conduct additional inspections in the area of their competence (for example, the Ministry of Architecture and Construction, Ministry of Health, etc.).

In addition, specialized audits can be conducted by the internal audit departments of the government agencies (for example, line Ministries) to review the work of their subordinated organizations who carry out procurement activities in accordance with the Tender Provisions (decree No.529).

### ***Key Regulations Governing Public Procurement in Belarus***<sup>35</sup>:

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<sup>34</sup> The complete list of who is authorized to request a controlling inspection is given in Presidential decree No.673, November 15, 1999

<sup>35</sup> There are other legal acts regulating contractual relations between the parties to perform their obligations (import operations, payment, licensing, etc.). A complete list of decrees and regulations applicable to public procurement can be found on the National Legal Internet Portal – [www.pravo.by](http://www.pravo.by). Resolutions of line Ministries and other Governmental agencies are available on their respective web-sites.

The basic regulations governing the public procurement in Belarus are

- (a) Decree of the President of the Republic of Belarus No.529 dated August 25, 2006 “On order to select suppliers (contractors, performers) in carrying out public procurement in the Republic of Belarus” (“Decree No.529”);
- (b) Decree of the President of the Republic of Belarus No.58 dated February 7, 2005 “On bidding in construction and invalidating particular decrees, provisions of the decree of the President of the Republic of Belarus" (“Decree No.58”)
- (c) Regulation of the Council of Ministers of the Republic of Belarus No.235 dated March 3, 2005 “On approval of provisions on order to form agreed (contract) price and payments between Employer and Contractor in constructing the objects and on order on organization and conducting of bidding on construction of objects, on amendments to Regulation of the Council of Ministers of the Republic of Belarus No.652 dated May 19, 2003 (as amended by regulations of the Council of Ministers No.813 of July 23, 2005 and No.1632 of December 7, 2006)
- (d) Regulation of the Council of Ministers No.1632 of December 7, 2006 “On measures to implement President’s Decree No.529 dated August 25, 2006”
- (e) Regulation of the Council of Ministers No.1633 of December 7, 2006 “On certain issues on procurement of goods (works, services) by unitary enterprises, state corporations, economic associations”
- (f) Regulation of the Ministry of Architecture and Construction No.4 as of March 3, 2005 “On invalidating particular regulations of the Ministry of Architecture and Construction on conducting bidding in construction”
- (g) Regulation of the Ministry of Architecture and Construction No.7 dated April 1, 2005 “On invalidating certain orders, introducing amendments and addendum to normative legal acts of the Ministry of Architecture and Construction of the Republic of Belarus on conducting bidding in construction”

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**ANNEX 5: VIEWS OF GOVERNMENT AND PRIVATE SECTOR REPRESENTATIVES ON BANK-FINANCED PROJECTS**

During the mission, the Government emphasized the high completion rate of state-funded investment (or capital) projects, in comparison with implementation delays on Bank-financed contracts. Main factors in their views are that (i) state owned companies are not allowed to participate in the Bank-financed contracts, (ii) bank guarantees (for advance payments and performance securities) are not required under state funded projects, and (iii) advance payments can be as high as 100% percent of the contract amount in the case of state funded contracts. They also stressed the unnecessarily high qualification requirement for Bank-financed contractors and the discipline of progress reports to the Council of Ministers and the President for the investment budget.

Private sector contractors<sup>36</sup> see the major issues affecting their interest to bid and implement Bank-financed contracts as following: (i) language of the bidding documents (is now resolved as May 2004 guidelines allow use of the national language); (ii) small advance payment (they would like to have at least 40 percent paid in advance without bank guarantee, or alternatively, a 40 percent advance with only 2-3 percent covered by bank guarantee) and bank guarantee requirements; (iii) high qualification requirements (turnover, liquid assets, number of similar completed projects in the last 3-5 years); (iv) difficulties in getting performance security; (v) large size of contracts due to the grouping of the sites/locations and the nature of the contracts (equipment supply and installation) that require sub-contracting, falls under the government's requirement to have a prime contractor's license which is almost impossible for a private firm to get; (vi) delayed co-financing payment (only 75 percent of each invoice from the loan account is paid on time, the co-financing is delayed; in case of advance payment it means that the bank guarantee needs to be provided for the full amount while only 75 percent of it will be actually paid to the contractor on time); (vii) delays with contracts' completion due to failure of local authorities to meet their obligations related to connections to water/electricity sources (contractor has to pay the VAT on the entire contract amount while 10-20 percent of the payment is withheld until the acceptance certificate is issued).

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<sup>36</sup> There are almost no fully private independent contractors in Belarus. Either there is a state share in one of the branches or small firms in a holding company, or a relative/family member of the influential government official is on the payroll. The government also regulates the salaries' ceiling in the private sector.