

ULAANBAATAR DARKHAN ROAD EXPANSION PROJECT – INSTITUTIONAL SUPPORT TO IMPROVE FUNDING FOR ROAD ASSET MAINTENANCE



Establishment and Operation of the Road Fund
11 November 2022

Agenda

- Part 1 - Current Situation
- Part 2 – Legal Amendments
- Part 3 – Operational aspects
- Part 4 - Fiduciary Controls

Background

- A 10 day mission was performed to Ulanbaatar in August 2022,
- The consultant met with the MRTD to discuss the desired outcome in relation to the establishment of the Road Fund,
- The changes were prepared in draft, but it was not possible to meet with MRTD staff at the time to discuss the changes and provide any clarifications that would be needed.

Purpose of the Road Fund

- What the road fund is expected to resolve:
 - Lack of road maintenance funds
 - Ensure that road financing is stable and predictable over time
 - That funds legislated for are collected and available
 - Provide a management structure for the allocation process
- While at the same time:
 - Ensure appropriate expenditure controls

Current status as assessed

- **Law on Autoroads:**
 - Establishes the autoroad fund
 - Establishes the roadcouncil
 - Identifies sources of financing for the fund
- **The Law About Special Fund**
 - Prevents the autoroad fund from becoming an organisation with its own staff
- As a result, it remains a budget line in the state budget

Currently envisaged sources of Finance (1)

- *25.1. The National auto road fund resources shall comprise of the following sources:*
- *25.1.1. not less 20 percent of excise taxes imposed on imported vehicles;*
- *25.1.2. funds from foreign loan, assistance and donation;*
- *25.1.3. funds allocated from the state budget;*

Currently envisaged sources of Finance (2)

- *25.1.4. charges for exploitation of international, national and special purpose auto roads;*
- *25.1.5. Fines imposed on persons who have committed traffic safety violations and violated the legislation on roads on the international and national quality and special purpose auto road*

Currently envisaged sources of Finance (3)

- 25.1.6. *fees and charges for international transportation vehicles transiting through the territory of Mongolia;*
- 25.1.7. *charges for service provided within auto road right-of-way in accordance with permits;*
- 25.1.8. *Others.*

Financing in practice

- The RF receives in practice:
 - Toll collected, though the toll collection is full of exemptions and is not always collected,
 - Funds from the state budget.
- None of the other sources of funding is either collected or transferred to the RF budget.

Financing in practice

- The legislation, despite its appearance to the contrary, does not provide a guaranteed source of finance for the road fund as:
 - *The State Central Administrative Body Responsible for Road Matters shall develop a proposal for funds to be deposited in the State Road Fund in accordance with relevant procedures and submit it to the State Central Administrative Body Responsible for Finance and Budget Matters.*
- **In short, allocations to the road fund are subject to the considerations of priority as part of the regular budget process and there is no predictable level of financing.**

Funds distribution

- **Law on Autoroads identifies purpose and distribution of state road fund monies as:**
 - To finance maintenance and repair of National and International Roads,
 - Sets the priority to daily and regular maintenance and emergency repairs,
 - Allows some funds to be spent on equipping state road maintenance companies
- **Additional in Resolution 312:**
 - Not less than 90% for maintenance
 - Maximum 10% for equipment

Funds distribution

- The regulation 312 requires that funds are distributed using ***“Basis Norm of Cost Estimation for Road and Bridge Maintenance and Repair” (ZZBD 84-021-2016)*** prepared by the Transport Development Center
 - This standard provides a theoretical framework that facilitates the budget preparation process
 - There is no requirement or link to actual road condition
 - The detailed budget for 2022 contains several items that in the view of the consultant may not be in compliance with legislation in force
 - The budget is to be reviewed by the Autoroad fund council and approved by the Minister.

Autoroad (fund) Council (1)

- Established by article 26.2 of the Law on Autoroads,
- Regulated by Order 282 of December 2018,
 - To be made up of road users and civil representatives to *“execute the public control on auto road readiness level, traffic safety and auto road fund revenues and expenditures”*,
 - Membership of the Council includes representatives of the MRTD and the Transport Development Center
 - Has not fully been established as yet and has never had a meeting
 - Can review the budget and make recommendations

Autoroad (fund) Council (2)

- Is expected to monitor revenue accumulation and make recommendations
- Provide external monitoring of maintenance and make recommendations,
- Make conclusions and recommendations of road readiness
- **The council cannot/does not:**
 - Have staff or a permanent secretariat,
 - Cannot do more than make recommendations,
 - Does not have any authority in relation funds distribution as this is governed by the formula in accordance with standard ZZBD 84-021-2016

Progress to date

- After thorough analysis and a discussion in August 2022, the consultant has prepared and submitted detailed draft legal changes to be adopted by the Government,
- These will create the enabling environment for a 'real' road fund,
- From the perspective of the project, the legal aspects have been completed. The next step is for the Government to format the text as per its legal drafting requirements and take it through the process for submission to Parliament

Legal changes in detail

- Significant and possible politically sensitive changes are required to primary and secondary law,
- To create the appropriate environment primary law must be amended first,
- Only after amendments to primary law have been adopted, there is a basis for the necessary amendments to secondary law and the establishment of institutions.

Law about Special Fund

- Enable the RF to become an organisation:
 - To ensure that the RF can become an organisation as intended, it will need to be **added to the list of exceptions** to the prohibition to establish a secretariat presented in **Article 22.3 of the Law about Special Fund**.
- Once this legal change has been achieved, the RF organisation can be established as a legal entity with the RF secretariat as the operational arm and the Road Fund Board as a governing body.

Changes to the Law on Roads and Secondary Legislation

- Extensive changes to the Law on Autoroads have been prepared to ensure stable financing of the RF,
- Similarly, changes to several regulations are required to remove contradictions and clarify what is required,
- Especially the primary legislation changes are sensitive and complicated, as they intend to remove the RF and its finance from the political arena.

Choice of financing sources

- **Road Maintenance financing must meet particular criteria such as:**
 - Must be stable over time and within the year,
 - Predictable,
 - As little as possible affected by the economic cycle,
 - Easy and cheap to collect,
 - Have a direct link with the purpose.

Sources of funding after legal changes

- Tolls (to be set by the Council according to needs),
- Annual Road User Charge (to be set by the Council according to needs),
- Charges for the use of the right of way (to be set based on a method to be developed).

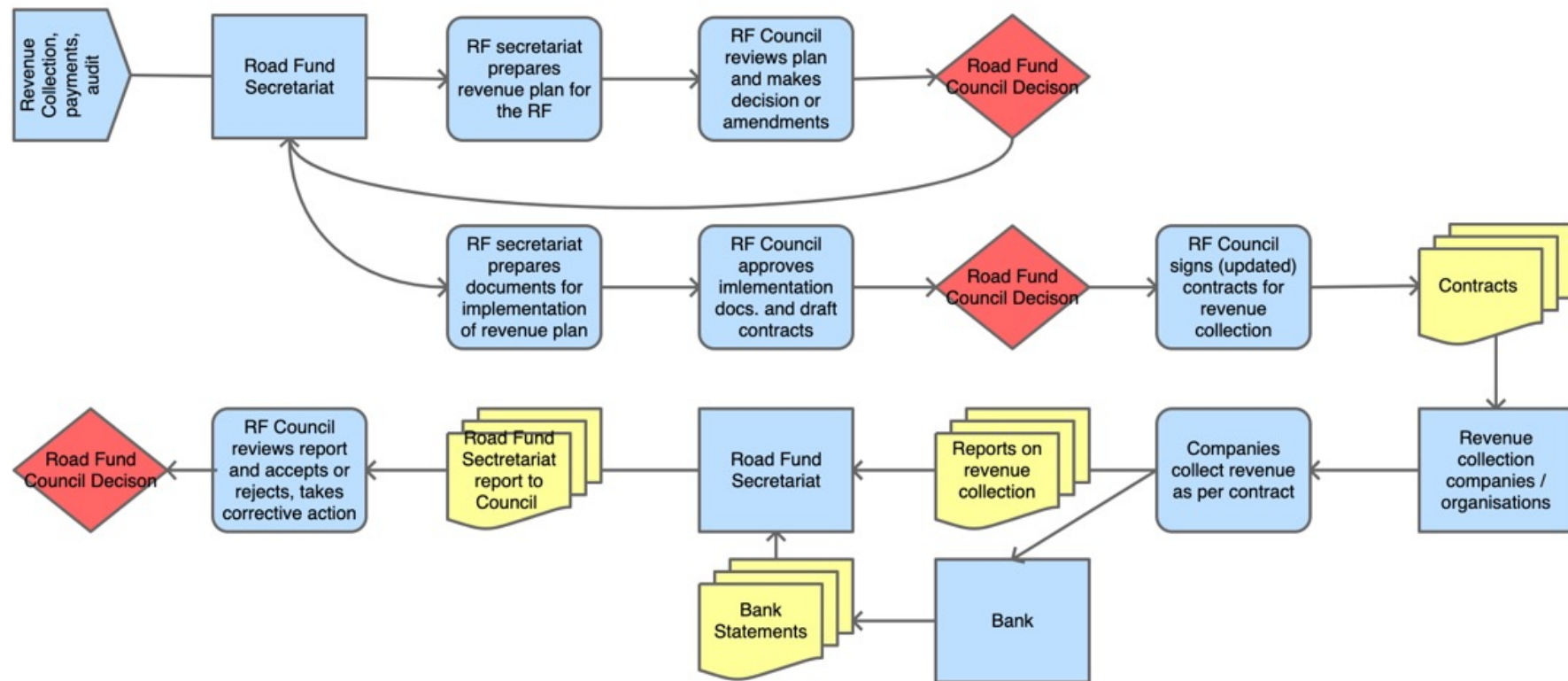
Role of RAMS

- RAMS can assist to direct road maintenance funding away from the theoretical model currently in use,
- This will allow the RF to justify the amounts it collect,
- It will allow a gradual improvement of the quality of the network over time by directing funds where they can be used most effectively.

Operational aspects of the RF

- Revenue collection mechanism:
 - The private sector for toll collection,
 - Through an existing electronic system such as “smartcar” or the vehicle inspection system for the annual road user charge,
 - Collection of the charges for the right of way can be the same system as used for the collection of land use taxes and related charges based on cadastral registration. (neither timing and potential revenue are currently available).

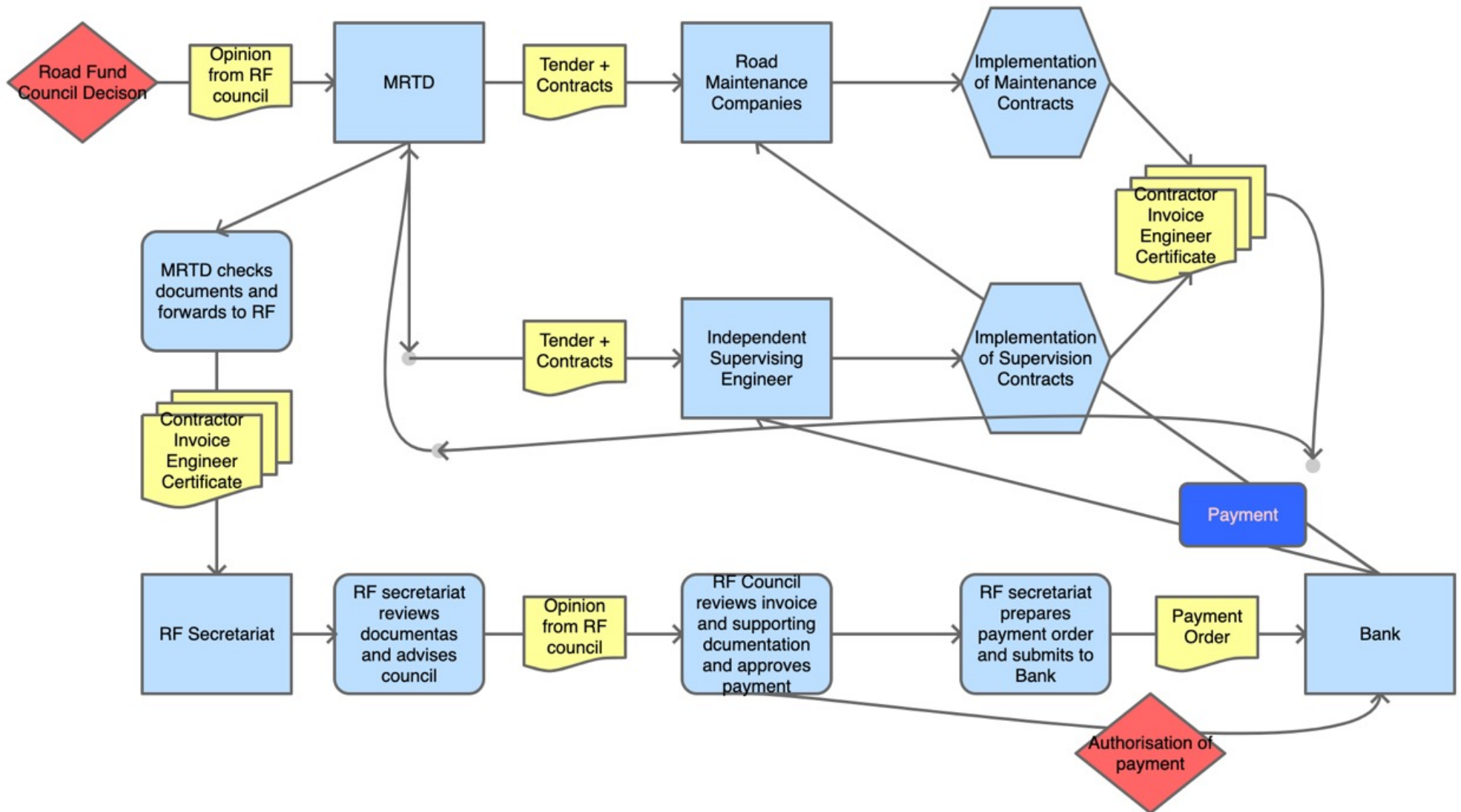
Revenue collection mechanism



Procurement & Contracting

- It is not intended that the Road Fund becomes a “Road Authority” type organisation that manages the maintenance and reconstruction,
- Instead, the RF will serve as a funds collection and disbursement agent, allowing it to operate with very few permanent staff and transparent processes,
- The relationship between the RF and the road fund will be based on a contract the stipulates the role of each party.

Contracting and disbursement



Fiduciary Aspects – Identified Risks (1)

- **Internal (organisational risks)**
 - Fraud (for example misdirection of funds through different means),
 - Clerical mistakes (wrong account numbers, wrong amounts).
- **Revenue risks:**
 - Private sector revenue collectors not collecting all revenue ,
 - Private sector revenue collectors collecting all revenue but not passing it on in time or in full,
 - Evasion of the charges by vehicle registration holders.

Fiduciary Aspects – Identified Risks (2)

- **Expenditure risks:**
 - Payments for work not performed or inadequately performed,
 - Payments for goods not in conformity with the specifications,
 - In case of Performance Based Road Maintenance contract, overpayments or deductions not in accordance with the contract,
 - Ineligible expenditure.
- **Expenditure risks are mostly generated at the procuring entity.**

Addressing Fiduciary Risks

- Fiduciary risks will be addressed through audits by private sector auditors under a non renewable 3 year contract on several levels:
- At the Road Fund:
 - Process or System Audit (covering procedures and controls)
 - Financial Audit (covering transactions)
- At the revenue collectors:
 - Financial Audit (covering transactions)

Process Audit (internal)

- Access to bank accounts, control over bank transaction approval keys,
- Payment approval processes,
- Handling of computer passwords and IT security,
- Document handling and retention, backup systems,
- Potential conflicts of interest of secretariat staff and Council members
- Conflict of interest and integrity policies, training of staff and Council members on the subject,
- Safe and other keys, including key register (who has which keys),
- Procedures for reporting irregularities, including whistle-blower protections.

Financial audits (internal)

- This is expected to be an audit of the transactions to ensure and certify that all transactions have been executed in the appropriate manner (with the correct documents and approvals) and are reflected correctly in the account as they have taken place.

Financial audits (external)

- External audits will be performed at the organisations that collect revenues on behalf of the authority to ensure that revenues are transferred to the bank account of the Road Fund in full and on time.