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ARREARS MANAGEMENT IN SOUTH SUDAN

DOMESTIC EXPENDITURE ARREARS CLEARANCE STRATEGY

Fiscal Accountability and Sustainable Trade (FAST)



April 2022

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April 30, 2022

Fiscal Accountability and Sustainable Trade (FAST)

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ACRONYMS

ACC	Anti-Corruption Commission
COA	Chart of Accounts
CPI	Consumer Price Index
DSA	Debt Sustainability Analysis
FAST	Fiscal Accountability and Sustainable Trade
FY	Fiscal Year
GDP	Gross Domestic Product
GOSS	Government of South Sudan
IFMIS	Integrated Financial Management Information System
IMF	International Monetary Fund
MDA	Ministry, Department, and Agency
MOFP	Ministry of Finance and Planning
MTBF	Medium-Term Budget Framework
NRA	National Revenue Authority
NRS	National Revenue System
PFM	Public Financial Management
PPADA	Public Procurement and Asset Disposal Authority
R-ARCSS	Revitalized Agreement on the Resolution of the Conflict in South Sudan
SIGFIP	<i>Système Intégré de Gestion de l'Information Financière</i>
SOE	State-Owned Enterprise
StAR	Stolen Assets Recovery
TIN	Tax Identification Number
TSA	Treasury Single Account
USAID	United States Agency for International Development

VVA	Verification and Validation Agent
VVP	Verification and Validation Process
WAEMU	West African Monetary Union

EXECUTIVE SUMMARY

Persistent expenditure arrears are typically a symptom of underlying weaknesses in a country's public financial management (PFM) system. Expenditure arrears can be the result of failures at any or all stages of the PFM cycle, including inadequate legal frameworks, unrealistic budgeting, weak or cumbersome expenditure controls, inefficient cash management, lack of or problems with a financial management information system (FMIS), or gaps in fiscal reporting.

– Prevention and Management of Government Expenditure Arrears¹

At the end of the civil war in 2018, the Government of South Sudan (GOSS) embarked on the Revitalized Agreement on the Resolution of the Conflict in the Republic of South Sudan (R-ARCSS), which established a range of sweeping PFM priority reforms to ensure effective, transparent, and accountable management of national resources. Each of these priority reforms directly relates to the Arrears Management Activity.

GOSS has faced challenges in sustaining efficient PFM practices, largely due to weak fiscal discipline and transparency, which impacts the ability of the Ministry of Finance and Planning (MOFP) to manage the country's complex budget. The functioning fiscal discipline of GOSS requires strengthening to appropriately manage public finances, particularly regarding legislation, budgetary controls, procurement laws, and regulations that support and protect the integrity of PFM systems. On account of the systemic lack of fiscal discipline, the Ministry of Finance and Planning (MOFP) has struggled to maintain GOSS PFM processes to adequately manage an Arrears Clearance Strategy (see Figure 1). The following five-step process distributes responsibility among areas where the MOFP is able to exert sufficient control and therefore allocates other steps to an external verification and validation agent (VVA).

¹ Prevention and Management of Government Expenditure Arrears, Suzanne Flynn and Mario Pessoa.

Figure I. Arrears Clearance Strategy



1. The **stocktake** of domestic expenditure arrears commenced in January 2022. With support from the USAID Fiscal Accountability and Sustainable Trade (FAST) Arrears Management Activity, the MOFP has assigned a six-member team to work with ministries, departments, and agencies (MDAs) to complete a specially designed arrears collection template. As of April 2022:
 - 50 percent of trained MDAs have submitted completed arrears collection templates, and MDAs have reported US\$1.05 billion of domestic expenditure arrears to date.
 - The MOFP is following up with MDAs that have not yet submitted an arrears collection template.
 - The stocktake exercise is planned to be completed by the end of May 2022.
2. The **verification and validation** process, undertaken by the VVA, will be multi-phased:
 - **Phase I.** Validate correctness and completeness of data submitted from MDAs on the arrears collection template
 - **Phase II.** Sort data into three categories for conducting in-depth verification:
 - High value, low volume
 - Medium value, medium volume
 - Low value, high volume
 - **Phase III.** Classify claims as:
 - Verified
 - Contestable
 - Rejected
3. The **rejections and appeals** process will allow MDAs the opportunity to review claims that have not been classified as verified and to provide additional supporting evidence or documents or other evidence to verify such claims.

4. Domestic expenditure arrears will be **prioritized** in accordance with GOSS policy decisions:²
 - Expenditures required to sustain lives, protect local supply chains, and ensure GOSS continues to “do business” (e.g., salaries and wages) will be prioritized.
 - Intra-government debts, such as arrears for MDAs to pay utility charges to the State’s electricity program, will be prioritized.
 - Medical claims will be excluded.
5. **Funding and liquidation** will be identified through the annual budget cycle.

It is recommended that the Arrears Clearance Strategy be supervised by the PFM Oversight Committee. The MOFP First Undersecretary should take responsibility to prepare reports, with assistance from related donor-funded activities, to present regular updates to the PFM Oversight Committee.

As of April 2022, the ability for the MOFP to work without influence from interested parties inhibits their ability to manage all the Arrears Clearance Strategy steps. It is strongly recommended that the PFM Oversight Committee identify an external VVA to undertake these steps, including the rejections and appeals prioritization steps. The VVA should be identified by August 2022 and is expected to complete its work over 12–15 months. At a donors’ meeting on March 11, 2022, the donors indicated their support for an external VVA.

Systematic corruption evokes indignation in populations, making it a factor in social unrest and insurgency.

–Carnegie Endowment for International Peace³

² World Bank, Supporting the Government of South Sudan's Public Financial Management and Procurement Reform (PI76036), November 2021

³ Carnegie Endowment for International Peace, June 2014

BACKGROUND

The newest internationally recognized country in the world is the Republic of South Sudan, which declared independence from Sudan on July 9, 2011. Early on, the new Government of South Sudan (GOSS) showed it was slowly establishing institutional strength and capacity in public financial management (PFM) systems. However, soon after independence, a civil war broke out in 2013 that lasted five years. During that time, most of the gains GOSS made in the economy and PFM systems eroded. After several attempts to end the war, the warring parties finally agreed and signed the Revitalized Agreement on the Resolution of the Conflict in South Sudan (R-ARCSS) in 2018; this resolution established a range of sweeping PFM priority reforms to ensure effective, transparent, and accountable management of national resources. Each of these priority reforms is directly related to the Arrears Management Activity (see Table 1).

Table 1. Reform and Arrears Management

#	REFORM PRIORITY	RELATION TO ARREARS MANAGEMENT
1	Implement the treasury single account (TSA)	Arrears build up because funds are not centrally managed and are then not available on time or in full for executing the budget. Currently, revenues are diverted to make payments not approved by the MOFP or not aligned with the approved budget. All revenues, including loans and other receipts, must be collected in TSA bank accounts that are controlled by the Ministry of Finance and Planning (MOFP) (treasury) and all payments must be made from TSA bank accounts.
2	Strengthen cash management	Arrears build up because daily cash positions are not accurately available for the release of payments. Also, the lack of credible estimates of cash flows (inflows and outflows) makes it difficult to tie them to allotment or commitment controls.
3	Relocate Loan Committee to MOFP	Loans, guarantees, or borrowing contracted by public agencies must be within limits identified in macroeconomic forecasts, including debt sustainability analysis (DSA). The MOFP must be empowered to be the apex agency for controlling public debts. When the MOFP does not centrally manage all PFM matters, loan arrears will build up.
4	Review, verify, and clear all arrears	This activity is a priority. It is essential that only verified arrears are paid. If GOSS continues to make payments that are not verified or are outside the budget thresholds, expenditure arrears will continue to build up.
5	Review and verify loans and contracts collateralized or guaranteed against crude oil	These are contingent liabilities that would add to budget pressures if invoked. The true extent and status of all such instruments need to be registered and reviewed to avoid contributing to the build-up of arrears.

#	REFORM PRIORITY	RELATION TO ARREARS MANAGEMENT
6	Strengthen the Anti-Corruption Commission (ACC) and the National Audit Chamber (NAC)	The ACC and the NAC play an important role in limiting the diversion of funds for unapproved purposes that do not serve the people of South Sudan. Efficient dispensation of ACC and NAC duties with independence from the executive branch of government and resources will ensure that only legitimate payments are made and nonlegitimate transactions are detected early through a robust and timely external audit. Penalties for fraudulent and corrupt practices are swift and will serve as deterrents.
7	Establish a Public Procurement and Asset Disposal Authority (PPADA)	Improper procurement practices lead to the build-up of arrears because procurements are not in line with the approved budget; these drain budget resources from legitimate transactions and important activities.
8	Rollout electronic payroll using biometric system	Salaries are significant arrears. An electronic payroll system will allow accurate salary estimates and will help eliminate salary payments that are not on the approved nominal roll.
9	Strengthen Fiscal and Financial Allocation Monitoring Commission	State transfer arrears must be prioritized if arrears are to be avoided. If the States cannot pay their bills, there is no way to avoid arrears.
10	Strengthen macro-fiscal framework	Credible, reliable, and timely macro-fiscal data is important for budget preparation, execution, and in-year modifications. Availability of macro-fiscal data, including forecasts, should at a minimum contain the real and nominal gross domestic product (GDP), petroleum production and sales, inflation data, non-oil revenue, the Consumer Price Index (CPI), and exchange rates.
11	Strengthen the budget process and budget credibility	The budget must represent the policy priorities of the GOSS and it <i>must</i> be adhered to. Expenditure arrears build up because there is almost no fiscal discipline across the GOSS.
12	Establish revenue management	Effective revenue management is essential to avoid the build-up of expenditure arrears. Efficient tax administration and revenue collection results in improved domestic revenue mobilization, thus providing resources for planned budget execution. When revenue collections are not efficient or are diverted for other purposes directly from revenue collection accounts, the non-availability of resources for budgeted expenditures will result in arrears.

GOSS has faced challenges in sustaining credible PFM practices, largely due to weak fiscal discipline and transparency which limits the MOFP's ability to manage the country's annual budget. The 2019 Open Budget Survey ranked South Sudan 106 out of 117 countries. It scored the country 7, 11, and 43 out of 100 in transparency, public participation, and budget oversight,

respectively.⁴ A recent International Monetary Fund (IMF) and World Bank assessment also highlights the extensive challenges GOSS faces in bringing about an efficient PFM system that would result in improvements in public service delivery.

The continuous build-up of domestic expenditure arrears contributes to the following risks: the overall credibility of the national budget, the GOSS's ability to deliver goods and services to citizens, and the country's ability to access international financial markets. The accumulation of domestic expenditure arrears disguises the actual size of the GOSS's deficit and debt, significantly reduces the impact of fiscal policy, and potentially undermines macroeconomic stability:

1. **Reduced economic activity.** Businesses and suppliers may become hesitant to do business with GOSS because of delayed payments and liquidity constraints that put them at risk of failure or closure. This is especially the case for small and medium-sized businesses that may not have the funds to help weather delayed payment for goods or services delivered.
2. **Reduced confidence in GOSS fiscal policies.** Domestic expenditure arrears are a signal to investors that a government may not be managing its obligations properly and that the true extent of the government's liability may be disguised.
3. **Higher costs to GOSS.** Arrears lead to more expensive government operations due to interest charges and penalties on outstanding payments to vendors.
4. **Increased costs.** Suppliers are inclined to bid higher to mitigate against risks of delayed payments, resulting in higher costs to GOSS.
5. **Secondary implications.** Suppliers may withhold payment of taxes and deductions until they receive payment from GOSS.
6. **Negative impact on livelihoods.** The welfare of pensioners and existing employees are negatively impacted when GOSS does not pay salaries and wages on time or when it does not make payments to small vendors.
7. **Budget implementation.** Domestic expenditure arrears increase challenges in budget planning and execution because some arrears may be off-budget and may not meet GOSS's priorities.
8. **Reputational risk.** GOSS not paying investors, creditors, and donors on time shows that the government is not well managed and does not honor its obligations. It may lead investors to increase borrowing costs and donors to decrease contributions due to the potential mismanagement of funds.
9. **Increased and perpetual corruption.** Suppliers will find ways to build relationships with people of influence, garnering favor in public procurement opportunities and enabling them to stay in business.

GOSS needs to urgently address the issue of domestic expenditure arrears. This document provides a comprehensive Arrears Clearance Strategy that GOSS, through the PFM Oversight

⁴ Open Budget Survey 2019: South Sudan: <https://www.internationalbudget.org/open-budget-survey/country-results/2019/south-sudan>

Committee, should endorse and mandate for implementation. The following sections of the strategy should be presented to the PFM Oversight Committee as an urgent matter.

EXTERNAL VERIFICATION AND VALIDATION AGENT

A well-functioning ministry of finance should function as the apex institution, managing an effective and efficient PFM system, and should have the ability to implement the Arrears Clearance Strategy. While the South Sudan MOFP has adequate legislation, leadership, and capable staff to run PFM functions satisfactorily, the MOFP is considerably hampered by interested parties such as politicians, businesses, and individuals. The legislation, budgetary controls, procurement laws, and regulations that support the PFM systems are routinely flouted. Due to the overt influence by interested parties and flouting of legislation, as of April 2022, it is extremely difficult for the MOFP to undertake the management of the Arrears Clearance Strategy and the verification and validation steps of the Strategy. To overcome the challenges imposed on the MOFP, it is recommended that an external, independent verification and validation agent (VVA) be identified to undertake steps 2, 3, and 4 of the Arrears Clearance Strategy. The VVA must be established as an independent body and provided with assurance that it can operate independently and without hindrance.

The following provides the terms of reference for an Arrears Clearance Strategy VVA.

TERMS OF REFERENCE: ARREARS CLEARANCE STRATEGY VERIFICATION AND VALIDATION AGENT

INTRODUCTION

The continuous build-up of domestic expenditure arrears puts the economic and social development of South Sudan in a perilous situation. GOSS has limited ability to deliver goods and services to citizens, and economic growth is stagnant. Reducing the current stock of arrears requires urgent and immediate attention, and the appointment of an independent VVA is an important step in reducing the current stock. The role of the VVA is to assist in undertaking three vital steps of the Arrears Clearance Strategy:

2. Validation and verification
3. Rejections and appeals
4. Prioritize arrears and plan liquidation

Engaging a VVA is a temporary activity USAID/Juba intends to contract to a private firm. The activity will dissolve on the completion of the validations and verification, rejection and appeals and prioritization processes of the Arrears Clearance Strategy.

PURPOSE OF THE VVA

The suggested structure of the VVA includes a team lead, two international experts, and two South Sudanese consultants. The VVA will conduct its activities over a 12–15-month period, and the PFM Oversight Committee will select the VVA.

As the R-ARCSS entered into force in March 2020, immediate needs to reduce runaway inflation constrained the ability of the Central Bank to finance the GOSS's fiscal deficit while protecting the value of the South Sudanese pound. While reiterating the commitment to reduce borrowing from the Bank of South Sudan, the Minister of Finance observed the following in his fiscal year (FY) 2018/2019 Budget Speech as published on the MOFP website:⁵ "Given our financing shortfalls, we have faced difficulties in meeting all our payment obligations. As well as being in arrears with salaries and transfers, we have also made little progress in clearing our stock of arrears for goods and services. Instead, we have accumulated more."

The VVA will validate and verify domestic expenditure arrears claims by reviewing supporting documentation provided by the ministries, departments, and agencies (MDAs), verify the qualifications and capabilities of vendors and contractors and ensure only verified domestic expenditures arrears are prioritized for payment. The VVA will also engage with MDAs during the rejections and appeals process and will provide recommendations to MDAs and GOSS for prioritization and payment of domestic expenditure arrears.

The VVA will ensure that the verification processes are structured and disciplined, and that appropriate risk management strategies and responses are deployed. This includes, but is not limited to, ensuring that processes are:

- **Transparent.** Provide appropriate and accurate information to decision-makers, those directly impacted by arrears accumulation (e.g., employees, suppliers), broader civil society, and development partners.
- **Ensure accountability.** Document details of validated and rejected domestic expenditure arrears claims so that accounting officers remain personally accountable for decisions of public expenditure in line with Section 51 of the PFM Act, 2011.
- **Fair.** Do not directly or indirectly discriminate against any persons or groups of people.

FUNCTIONS OF THE VVA

The VVA will:

- Undertake the verification of domestic expenditure arrears identified as part of the current stocktake process.
- Serve as an independent entity.
- Establish suitable, secure office accommodations outside of the MOFP or any other GOSS institution.
- Aid the First Undersecretary in making regular presentations to the PFM Oversight Committee on progress and the results of the rejection and appeals process of each MDA.
- Hold workshops to inform all MDAs of these processes.

⁵ Draft budget speech found at: <http://www.mofep-grss.org/wp-content/uploads/2019/07/Budget-Speech-draft-FY-19-20-Final.pdf>

- Call upon MDAs to submit documentation that supports their domestic expenditure arrears claims.
- Conduct site visits to inspect the delivery of goods, services, or construction contracts. These site visits will ensure that goods, services, perishables, and construction have actually been delivered or completed.
- Access and inspect records of other GOSS institutions (e.g., MOFP, Bank of South Sudan, and the National Revenue Authority [NRA]) to ensure payments to vendors have not been made outside the approved MOFP processes.
- Inspect vendor company details including their premises, published financial records, tax identification number, and any other information deemed necessary to ensure the company is not a “brief-case” company.
- Inform MDAs, through the PFM Oversight Committee, the reasons domestic expenditure arrears claims are contested or rejected.
- Meet with the MDA to discuss the contested or rejected claim if the MDA has opted to appeal.
- Develop a payment prioritization schedule.

ARREARS CLEARANCE STRATEGY

The build-up of domestic expenditure arrears is a common problem in developing countries. Several such countries have developed arrears clearance strategies. (See Box 1 and Box 2 for examples).

The GOSS Arrears Clearance Strategy will be supervised by the PFM Oversight Committee. The MOFP First Undersecretary will prepare reports with assistance from related donor-funded activities, such as the USAID Arrears Management Activity, to present regular updates to the PFM Oversight Committee.

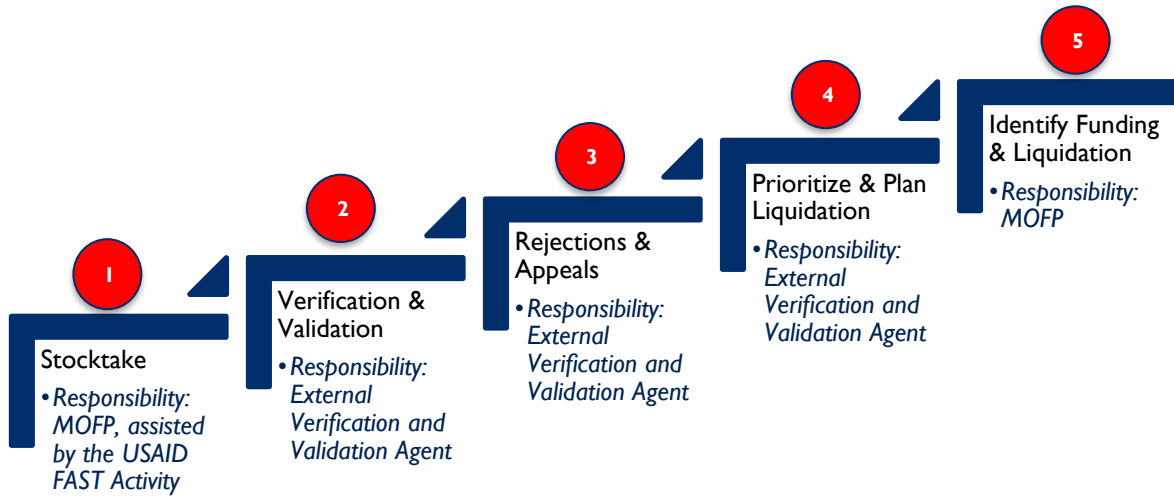
To ensure the veracity of the Arrears Clearance Strategy, a five-step process has been designed, as documented below:

1. **Stocktake.** A stocktake will consolidate appropriately classified lists of claims in MDAs to ready these claims for verification.
2. **Validation and verification.** Arrears claims submitted by spending agencies will go through a verification and validation process to confirm the correctness and veracity of the transactions. Thresholds will be established to ensure that efforts are concentrated on in-depth verification for all high-value claims contracts. Based on the data collected to date, arrears claims can be classified into three groups for conducting the verification process:
 - High value, low volume
 - Medium value, medium volume
 - Low value, high volume

Given the large number of claims, the VVA may divide up the arrears claims into these groups to focus greater scrutiny on the high-value claims. Less scrutiny will be given to the vast number of low-value claims.
3. **Rejections and appeals.** MDAs will have an opportunity to appeal rejected claims and submit additional supporting evidence.

4. **Prioritize and plan liquidation.** Appropriate classifications will be introduced at the stocktake stage and refined during verification. This will help ensure that reports provided on verified claims are suitable to analyze for prioritizing and planning the liquidation of expenditure arrears.
5. **Identify funding and liquidation.** Funding and payment of the stock of arrears needs to be accommodated in the annual budget's planned expenditure.

Figure 2. Arrears Clearance Strategy



The Arrears Clearance Strategy is supported by the USAID-funded FAST Arrears Management Activity.

Box I. The Senegal Approach to Clear and Prevent Expenditure Arrears

Unpaid bills had been a problem for the Government of Senegal for a number of years, reaching a crisis point in October 2008 when arrears rose to 7 percent of GDP. The arrears were partly a result of cash-flow difficulties stemming from increases in food and energy subsidies, poor budget management, and reduced liquidity in the West African Monetary Union (WAEMU). The government recognized the need to implement measures to address the problem.

At the outset, the government appointed external auditors to verify the outstanding payments. Valid claims were then scheduled for repayment through the budget process, and invalid claims were rejected. In addition, the government initiated the following measures:

Fiscal reporting. Reforms were implemented to improve the format and transparency of budget reports, including the past year and current year actual expenditure data, and were included in the annual budget law of an annex; the budget execution and forecast data of all agencies receiving funds from the budget in excess of CFAF 5 million was also included.

Financial management systems. The budget execution monitoring system (SIGFIP) was reconfigured to improve its efficiency, enhance the reliability of real-time data, and expand its coverage to enable monitoring at each stage of budget execution. Interfaces were developed with accounting software, and the system was rolled out to all accounting units.

Sanctions. Administrators who illegally created a liability for the government by knowingly committing expenditure in excess of authorized appropriations were brought before the financial disciplinary chamber of the court of audit and subject to penalties.

Clearance strategy. The stock of arrears was reduced by the end of March 2009 to one percent of GDP through reprioritization of investment spending, mobilization of resources from WAEMU financial markets, and support from donors, coupled with prudent and rigorous PFM systems.

Source: IMF, Senegal: Second and Third Review under the Policy Support Instrument, January 2009 and July 2009 available at: <http://www.imf.org/external/country/SEN/index.htm>.

Box 2. The Portugal Approach to Clear and Prevent Expenditure Arrears

In early 2011, the Government of Portugal defined a two-pronged strategy to clear accumulated arrears of more than EUR 5.3 billion (3.1 percent of GDP) comprising (1) the implementation of a new system of expenditure commitment controls to halt the accumulation of arrears and (2) a comprehensive plan to settle the stock of arrears over time. Following the implementation of the strategy, in December 2013, the arrears stock stood at EUR 1.9 billion (1.1 percent of GDP).

Legal framework and census of arrears. The government enacted legislation (1) specifying that payments are in arrears when they are outstanding for more than 90 days; (2) mandating the preparation of a monthly report showing outstanding invoices and classifying the arrears according to their typology; and (3) defining general and specific rules for the definition of arrears and the clearance process.

Reporting of arrears. A monthly census, which covers all entities of the general government, was initiated in June 2011. The three main areas of arrears, which account for more than 96 percent of the total, were concentrated in the health sector, local administrations, and the regional administration of Madeira.

Transparency. As an essential element of the strategy, all information on arrears was made available on the Ministry of Finance's webpage and is updated monthly.

Commitment control. Prior to the clearance of arrears, the government passed a law allowing new commitments only if the appropriate financial resources were available and introduced an accompanying verification system. To operationalize this rule, for each new contract with a supplier, a corresponding commitment number is assigned that links the budgetary and financial resource to that expenditure.

Clearance strategy. Four general rules prioritized the clearance of arrears: (1) the maturity of the arrears (older arrears should be paid first); (2) the incurrence of additional costs related to interest for late payment (prioritize the most expensive); (3) the risk of judicial litigation that could have an additional financial impact; and (4) the socioeconomic impact related to delays in payment, such as the risk of supplier bankruptcy.

Based on these rules, every entity was required to prepare a payment regularization plan defining how and when the arrears will be cleared.

Source: Government of Portugal, 2012

STOCKTAKE PROCESS

I Stocktake

A comprehensive stocktake to collect a full picture of domestic expenditure arrears is the first step of the Arrears Clearance Strategy.

A review of literature on GOSS domestic expenditure arrears did not reveal evidence of the actual number of domestic expenditure arrear claims or values. The literature reviewed provided estimates for domestic expenditure arrears as a percentage of GDP. However, South Sudan's GDP calculation is heavily dependent on oil prices that fluctuate with changes in international oil prices. This means that any estimates of domestic expenditure arrears calculated as a factor of GDP could be misleading. Thus, the estimates of GOSS domestic expenditure arrears cannot be used as a substitute for obtaining actual values and details. As such, the first step of the Arrears Clearance Strategy is to undertake a comprehensive stocktake of domestic expenditure arrears. The details collected during the stocktake will inform all remaining steps of the Arrears Clearance Strategy.

The stocktake process consists of a six-step methodology:

1. Hold MOFP coordination meetings.
2. Establish the MOFP Core Team.
3. Develop the domestic arrears collection template and instructions.
4. Distribute MOFP circulars to all MDAs about the arrears collection exercise.
5. Train all MDAs on the arrears collection template.
6. Provide ongoing support to MDAs to complete the arrears collection template.

Thanks to the efforts of the First Undersecretary and the MOFP Core Team, steps 1 through 5 of the stocktake are complete. The stocktake of domestic expenditure arrears commenced in January 2022. With support from the USAID FAST Arrears Management Activity, the MOFP has assigned a six-member team to work with MDAs to complete a specially designed arrears collection template. As of April 2022:

- 50 percent of trained MDAs have submitted completed arrears collection templates.
- MDAs have reported approximately US\$1.07 billion of domestic expenditure arrears to date.
- The MOFP is following up with MDAs that have not yet submitted arrears collection templates.
- The stocktake exercise is planned to be complete by the end of May 2022.

MOFP COORDINATION MEETINGS

The First Undersecretary championed the Arrears Management Activity from the get-go and agreed to the stocktake methodology steps and to establish the MOFP Core Team. The meetings allowed the FAST team to get an initial understanding of the possible reasons for the accumulation of arrears, extent of such arrears, availability of underlying documents or information, and the resources that may be required to collect arrears information.

The MOFP leadership shared their concerns that no comprehensive domestic expenditure arrears data exists. The MOFP leadership also explained that only expenditure claims that were actually paid are currently recorded in the Integrated Financial Management Information System (IFMIS). Therefore, IFMIS will not provide any details on domestic expenditure arrears, which illustrates the importance of the domestic expenditure arrears stocktake exercise. At the end of the arrears clearance process, the MOFP will have verified data to be able to record domestic expenditure arrear claims in IFMIS.

ESTABLISH MOFP CORE TEAM

The MOFP Core Team consists of six officials and is responsible for liaising and coordinating with other MDAs. Responsibilities of the Core Team include:

- Sending a circular to MDAs to introduce them to the arrears collection exercise.
- Arranging meetings for the FAST team with officials in MDAs, including the MOFP.
- Assisting MDAs in filling out the arrears collection template.
- Collecting completed arrears files from MDAs.
- Assisting the analysis of shortcomings in arrears data.
- Following up with MDAs to complete gaps in arrears data submissions.

DOMESTIC EXPENDITURE ARREARS COLLECTION TEMPLATE

The domestic expenditure arrears collection template is a **user-friendly** template with dropdown menus to ease completion. The template captures data on multiple parameters, including age, vendor details, value, currency, IFMIS coding block, reasons for non-payments, and status of payment. The template includes the following principles:

Comprehensiveness. Collected data spans across several parameters to allow categorization, evaluation, analysis, and classification of arrears.

Box 3. Template Characteristics

- Allows the collection of comprehensive data.
- Application availability at input nodes, e.g., MS Excel.
- Easy recognition of headers.
- Easy availability of information for populating data fields.
- Ability to upload ratified data directly in IFMIS or another database.
- Maximum use of dropdown selections to achieve data standardization.

Use of an easily available application for data collection. Microsoft Excel was used as the base application for building the template as it is generally available in MDAs. Building a template in Microsoft Access or any other application would have been time consuming and difficult for MDAs to load on their computers.

Familiarity of parameters for data input. The finance staff at MDAs should be able to comprehend, collect, and populate the requested data in the template. The data for each field in the template is generally available on the payment documents that are awaiting settlement.

Ease of upload to IFMIS. The template's parameters (fields) to upload approved or ratified arrears transactions directly into the South Sudan IFMIS needed to be compatible with the IFMIS. Segments in the template and IFMIS include the coding block, description, invoice number,

vendor number, IFMIS commitment number, and value. The stocktake data is not in IFMIS because it has not been previously collected. At the end of the arrears clearance process, the MOFP will record verified domestic expenditure claims in IFMIS.

Standardization of information/data. By maximizing the use of dropdown selections, options in populating data are more standardized across different MDAs.

Adding descriptions to accounting codes. The chart of accounts (COA) contains the accounting codes as well as each associated definition. Merging the accounting code and its definition for dropdown selection allows MDAs to easily recognize codes from descriptions and vice versa.

Transaction-wise collection of data. Data is captured as individual transactions and not based on unpaid contract or budget balance, although the reference of the underlying contract should be provided if possible. For example, if there are four unpaid invoices on a contract, each invoice would be captured as four distinct transactions.

Table 2. Domestic Expenditure Arrears Collection Template (MS Excel)

FIELD	INPUT OPTION	PURPOSE
Financial Year	Dropdown	Identify financial year in which transaction was incurred and to identify/analyze age
Vendor Name	Manual	Identify the vendor that has claimed payment for delivery of services, works, or goods
Invoice Number	Manual	Reference number to identify claim of payment to the source invoice or bill provided by vendor or employee
Date of Invoice	Manual	Actual date of each invoice
Amount of Invoice	Manual	Amount claimed as payable based on invoice, bill, or any other claim document
Currency	Dropdown	Currency in which amount has been claimed in invoice
IFMIS Coding Block <ul style="list-style-type: none"> • Fund • MDA • Activity/Program • Location • Expenditure 	Dropdown	String of accounting codes used for capturing data in IFMIS and based on the approved COA for FY 2021/22 Accounting codes will help in analysis of arrears data and will also open possibilities to upload data directly to IFMIS
Description of Expenditure	Manual	Typically, will be the narrative for the reason for incurrence of expenditure, e.g., rent payment for ministry office, fuel costs for vehicle, etc.
Payee Category	Dropdown	Type of entity to which the arrear is owed, e.g., individual, employee, corporate, firm, international organization, etc.
IFMIS Vendor Number	Manual	Identification through vendor number generated in IFMIS
Tax Identification Number (TIN)	Manual	Tax identifier

Reason for Non-payment	Dropdown	Identify the reasons that led to creation of arrears, e.g., delay in invoice processing, insufficient budget, lapse of appropriations, etc.
Supporting Documentation	Dropdown	Information on availability, non-availability, or partial availability of supporting documents
Current Status	Dropdown	Information on whether the arrears amount is fully or partially unpaid
Amount Previously Paid	Manual	Information on any interim or partial payment that has been made against the invoice if partial payment selected in preceding cell
Contract Number	Manual	Reference number of the underlying contract against which the invoice has been generated by vendor (creditor)
Date of Signing Contract	Manual	Reference to date of contract signature or effectiveness
Contract Currency	Dropdown	Currency of the contract amount
Contract Value	Manual	Total value of the underlying contract. This would be useful to identify the unpaid amount on the contract and the extent to which contract was completed.
Remarks	Manual	Any information provided that may be useful for assessing the nature of the claim or its value

MOFP Circular on Arrears Collection Issued to MDAs

The MOFP prepared and distributed a circular on the Arrears Collection Activity. The circular was provided to all MDAs and covered the following points:

- Introduction to Arrears Management Activity and its importance.
- Definition of arrears.
- Request to nominate staff for undertaking the arrears collection exercise in respective MDAs.
- Date of trainings on the arrears collection template.
- Focal point in the MOFP for coordinating the arrears collection process.

MDA Training on the Arrears Collection Template

The MOFP Core Team provided half-day training sessions to 71 MDAs. The objectives of the training were to:

- Introduce participants to the domestic arrears management activity for South Sudan.
- Guide the participants on how to collect and capture data in the arrears data template, including how to interpret and use the accompanying instructions.

The participants in the training sessions included officials from the accounting and finance sections of MDAs.

Participants received information on:

- USAID FAST Arrears Management Activity, such as background, objectives, timelines, and deliverables under the Activity.
- Methodology for the collection and use of data, the arrears collection template, and its accompanying instructions file.
- Basic overview of how arrears are created and what kind of arrears would generally appear during the data collection process.
- Details about individual fields in the template, including the dropdown list to select relevant options. Live examples were used to indicate how to populate various fields including invoice details (number, date, value), vendor details (name, registration, type of entity), IFMIS coding block, type of transaction, status of transaction, and contract details.
- Directions on how to use information on documents or contracts to enter data in the arrears template.

Participants received the “Instructions for Collecting Arrears Data” presentation and were asked to refer to the instructions file to seek clarity while filling in data and to understand why data needs to be collected on an individual transaction basis and not based on “unpaid aggregates” of past contracts.

Soft copies of the arrears collection template and the instructions file were distributed to participants on flash drives.

Ongoing Support to MDAs

The MOFP will provide ongoing support to MDAs to assist them in completing the arrears collection template with complete and reliable data. The ongoing support may include:

- Visits to MDA offices
- Help with understanding requirements
- Assistance to complete the arrears collection template

In addition, a monitoring tool has been developed to support and coordinate the arrears collection process and to track sub-activities including:

- Nomination of MDA staff
- Training on the arrears collection template
- Submission of completed arrears templates
- Review of submissions for completeness, accuracy, and reliability
- Return of submissions (if any) for corrections post preliminary review
- Re-submission of arrears data from MDAs post correction
- Verification of arrears data

VERIFICATION AND VALIDATION

2 Verification & Validation

The verification and validation exercise will classify claims into three categories:

1. Verified
2. Contestable
3. Rejected

The validation and verification of domestic expenditure arrears claims is an important and critical step in the Arrears Clearance Strategy. The validation and verification process is a multi-phased approach:

- **Phase I.** Validate correctness and completeness of data submitted from MDAs on the arrears collection template
- **Phase II.** Sort data into three categories for in-depth verification:
 - Low value, high volume
 - Medium value, high volume
 - High value, low volume
- **Phase III.** Classify claims as:
 - Verified
 - Contestable
 - Rejected

PHASE I VALIDATION

This phase will confirm the correctness and completeness of data submitted by MDAs on the arrears collection template.

PHASE II CATEGORIZE AND VERIFY

The validated data post-Phase I will be divided into three categories based on thresholds. The categorization will ensure that the VVA directs its efforts toward the detailed verification of large-value transactions or contracts.

During the verification stage, all claims will be checked for correctness, accuracy, tenability, and legality based on the underlying documents for each claim. The documents could possibly include invoices, delivery documents, completion certificates, and signed contracts.

Given the history of the Dura Saga and the Letter of Credit scandal, there may be attempts to defraud the GOSS treasury through fraudulent domestic expenditure arrears claims. While all claims will be subject to verification, it is important that all high-value claims be subjected to deeper verification processes to uncover details that may not be visible in claim documents. These additional processes may involve physical verification of actual construction or delivery, checking documents at the shipping entity, removing the ownership veil, checking for capital and personnel adequacy, or implementing external validations, including third-party confirmations.

The approach classifies primary arrears data into three groups:

- High-value claims (greater than US\$75,000)
- Medium-value claims (less than US\$75,000 and greater than US\$2,500)
- Low-value claims (less than US\$2,500)

Based on the latest submitted claims data, high-value claims (greater than US\$75,000) constitute 23 percent of the number of arrears claims but account for over 98 percent of the aggregate value of submitted arrears claims. Similarly, low-value claims account for just 0.04 percent of the aggregate value of claims but account for over 40 percent of the total number of claims.

Besides routine verification based on documents, a sample of transactions will be selected and put through an in-depth verification. The in-depth verification process will include verification of financial, physical, personnel, or legal capabilities of the vendor; background of owners; physical verification of the construction or delivered items (to the extent feasible); third-party verification; and other verification steps as necessary.

The table below depicts the possible approach to classify arrears data for in-depth verification. A transaction’s value and volume for in-depth verification detailed in the table is indicated as the minimum. The VVA will need to expand the sampling for the in-depth verification results if a certain class of transaction issues negative results, which could include, for example, certain types of expenditures (travel, rent, construction, food supplies, etc.), specific vendors, or budget entity.

Table 3. Possible Strategy to Classify Arrears for Verification

CATEGORY	TRANSACTION VALUE AND VOLUME	SAMPLING FOR IN-DEPTH VERIFICATION	EXAMPLES
A	Low value, high volume	15% random + 5% biased selection	Per diems, stationery purchase, repairs
B	Medium value, high volume	50% random sample + 20% judgmental selection	Fuel supplies, rent, machine overhaul
C	High value, low volume	100%	Road construction, consulting assignments, food supplies

Verification of Salaries, Incentives, and Allowances

- Copy of pay sheet.
- Attendance records.
- Employee on the approved nominal roll.
- Income tax deductions must be transferred to the taxation department.
- Evidence of pension deductions.
- Salary arrears that do not meet minimum requirements will be returned to MDAs.
- MDAs will have an opportunity to challenge the rejection.

PHASE III CLASSIFICATION

After verification, domestic expenditure arrears claims will be classified as:

- **Verified claims.** Claims that meet all the applicable tests of verification and have adequate documentation to recognize the amount as a liability.
- **Contentious claims.** Claims that have incomplete supporting documentation, and adequate information could not be obtained to validate the claim legally as an arrear.
- **Rejected claims.** Claims that do not include legitimate documentation, and additional substantive checks did not provide any reason for accepting the claim as a liability.

Verification Guidelines

- The MDA Undersecretary or equivalent is ultimately responsible for ensuring their MDA cooperates with the processes of the Arrears Clearance Strategy.
- The responsibility for producing the supporting documents and information rests with the official leading the finance function at each MDA.
- The minimum requirements for supporting documentation at the validation stage include:
 - Invoice
 - Goods receipt notes
 - Contract
 - Approvals to pay
- MDAs will have an opportunity to provide supporting information and documentation.
- The VVA will provide the PFM Oversight Committee with details if and when the VVA suspects that false documents, information, data pertaining to the arrears claims, or an attempt to defraud the Treasury has been made.
- Only original documents will be accepted except in cases where there is sufficient reason to believe that the primary documents were destroyed (in fire or natural disaster). Nevertheless, the final decision to pay such claims would vest with the MOFP.
- The legal validity of the payable claims should be verified by checking that the transaction was duly authorized by a responsible officer in accordance with authorization rules prevailing at the time of incurrence.
- Evidence of a verified contract, approved budget for the expenditure, and compliance with prevailing procurement laws and regulations must exist.
- Evidence will be sought for delivery of goods, completion of construction, or provision of services. The evidence must be endorsed by a responsible officer.
- In cases of doubt or for material transactions, evidence must be reconfirmed from vendor records. These could include shipping documents, bank documents, port dispatch notes, insurance documents, and warehousing registers.
- For high-value or questionable claims, corroborative evidence must be sought from vendor financial statements or banking channels to verify financial, physical, personnel, or legal capabilities to deliver contractual conditions for which the arrears are being claimed.
- For material transactions, officials will ask for the vendor's financial records to identify if the amount claimed as arrears was recorded as an asset or receivable in the vendor's accounting records.
- In more complex transactions, particularly those related to major construction or other development projects, a certificate of completion produced by relevant experts will be sought as evidence. There must be sufficient fund/budget to undertake a physical inspection or to employ experts if such needs arise.

- The following checks should be made to confirm the contracted company is not a “brief-case” company:
 - Company is registered in South Sudan.
 - Has physical office space in South Sudan.
 - Has employees.
 - Has sufficient capital.
 - Has a TIN.
 - Is still in business.
 - Has a website.
 - Physical evidence of delivery, particularly for construction contracts.
 - Company or company directors are not on a sanction list.
 - How the business has survived with such high levels of debt outstanding from the government.

REJECTIONS AND APPEALS

3

Rejections & Appeals

The rejections and appeals process allows MDAs to engage further with the VVA to provide additional evidence to support their contested or rejected domestic expenditure arrears claims.

The rejections and appeals process will involve the following.

The VVA will advise MDAs in writing, through the PFM Oversight Committee, of the status of their domestic expenditure arrears claims that have passed through the validation and verification process. The VVA will provide the PFM Oversight Committee with reports on MDAs’ domestic expenditure arrears claims and indicate how the claim was assessed as either verified, contestable, or rejected.

Verified domestic expenditure arrears are claims that meet all verification and validation criteria. These claims will be recommended to the PFM Oversight Committee for payment when funding is identified.

Contestable domestic expenditure arrears are claims that meet some, but not all, verification and validation criteria. The verification and validation process (VVP) identified some weaknesses in the supporting documentation supplied as evidence of the claim’s veracity. However, the evidence provided indicates that, given the opportunity, the MDA may be able to provide additional supporting documents that will enable the claim to be reclassified as **Verified**. The VVA will request the MDA to provide additional supporting evidence within 15 days to enable the claim to be reassessed. The VVA may invite the MDA to meet with them to discuss certain aspects of the contested claim. This process may result in the claim being assessed as either **Verified** or **Rejected**.

Rejected domestic expenditure arrears are claims that provide none or insufficient evidence to satisfy the verification and validation criteria. The VVP assessment indicates that the weaknesses in supporting documentation supplied as evidence caused the claim to be **Rejected**. The MDA will be informed of the status of rejected claims and may appeal the assessment. The appeal

process will require the MDA to provide a written response within 15 days indicating the reasons for the appeal and provide further substantive evidence to enable a reassessment of the claim. The VVA will assess any additional supporting evidence provided to enable further validation and verification. The VVA may reassess the claim as **Valid** or again **Reject** the claim.

PRIORITIZE AND PLAN LIQUIDATION



Prioritize & Plan Liquidation

Claims will be prioritized in accordance with GOSS policy.

GOSS has made policy decisions to prioritize domestic expenditure arrears as follows:⁶

- Arrears in expenditures required to **sustain lives, protect local supply chains, and ensure the government continues to “do business”** should be prioritized for liquidation.
- Salaries and wages are in the interest of “sustaining lives” as the main poverty-reducing instrument available to GOSS.⁷
- Medical claims have already been identified in discussions with GOSS officials as a category of expenditure that will not be considered in the definition of arrears for arrears management.
- Intra-government debts, such as arrears for MDAs to pay utility charges to the State’s electricity company, can be prioritized for clearance administratively through the annual budget at minimal net cost. Often, when state-owned enterprises (SOEs) are owed by the government, there is also a tax debt owed by the SOE to the government. A tax-debt swap arrangement may clear the current arrears balances, but any such arrangement must be considered as an extreme, exceptional, and one-off transaction, which is treated as “handle with care.” Such transactions should not be used lightly. Should such arrangements pervade, the resulting implications for voluntary tax compliance and governing SOEs may be significant. This type of swap arrangement will only apply to SOEs and not any private firm or person.

Appropriate prioritization will be expanded once the stock of arrears is better understood. This expansion will build on principles of sustaining lives and livelihoods (i.e., sustaining and strengthening local supply chains) and keeping the business of government running. Additionally, prioritization will be based on the following:

⁶ World Bank, Supporting the Government of South Sudan’s Public Financial Management and Procurement Reform (PI76036), November 2021

⁷ <https://www.imf.org/en/Publications/CR/Issues/2021/04/01/Republic-of-South-Sudan-Staff-Monitored-Program-and-Request-for-Disbursement-under-the-Rapid-50331>

- **Socio-economic impact.** Although splitting bills and applying partial payments are not recommended administratively as they introduce inefficient handling and greater risk of fraud and error, partial payments may be warranted to sustain local supply chains (“everyone gets something”).
- **Vintage.** Older obligations should have priority over newer obligations.
- **Cost.** Arrears that accrue interest and penalty charges should have priority.
- **Risk.** In addition to risks to lives, livelihoods, and government disruption, arrears that may result in legal action or escalate the cost of future supplies to the government should be prioritized.
- **Currency.** This will be determined appropriately in collaboration with GOSS.

It may also be possible for GOSS to seek postponement of obligations to pay international organizations. In doing so, GOSS will need to proactively demonstrate it has a strategy to arrest its financial degradation and ensure its ability to pay in the future. Such postponement does not give GOSS more money, just more time to pay.

IDENTIFY FUNDING



Identify Funding

Funding and payment of the stock of arrears needs to be accommodated in the annual budget planned expenditure.

It is recommended that GOSS should adopt a centralized management and control approach for the budget line for domestic expenditure arrears repayment to avoid recycling arrears (paying old arrears while accumulating new ones). A special disbursement unit within the MOFP payment processing section should be established that only deals with the payment of arrears. MDAs will not be responsible for the payment of arrears. Payments will only be made against the list of validated and verified claims. Funds that are earmarked for arrears settlement will be ring-fenced within IFMIS through accounting codes.

It is recommended that MDAs that incur new arrears should be subject to the provisions of the PFM Act of 2011 that prohibit such practices.

A payment processing team will be established in the MOFP that is specifically tasked with processing domestic expenditure arrears. In general, the MOFP will need to strengthen fiscal discipline surrounding the payment process to eliminate the interference and pressure-payment processing that staff are currently subjected to from interested parties, such as vendors and politicians. The domestic expenditure arrears payment team needs to be set up so they can process payments unhindered and in line with controlled payment processes.

The annual budget and medium-term budget framework (MTBF) must make explicit provisions for the clearance of arrears. A line-item provision, representing a percentage of budgeted expenditures, will be identified in the MOFP's annual budget. This line item will use the appropriate codes from the COA to facilitate effective control and to eliminate the opportunity to use that budget line item for other purposes.

Offsetting the settlement of arrears to the private sector against tax obligations will not be part of the liquidation plan. Offsetting payments undermines transparency and accountability. All payments and revenues must be accounted for on a gross basis. Any subtraction from tax liabilities undermines tax compliance and encourages the future accumulation of tax arrears. To avoid liquidity problems in GOSS's cash flow, the payment to suppliers holding arrears will be coordinated with the payment of these suppliers' tax obligations and be concomitant, especially in the case of large amounts of outstanding arrears.

It seems unlikely GOSS will have sufficient liquidity to extinguish all domestic expenditure arrears within 12 months. Once the total value of the stock of domestic expenditure arrears is known, it is recommended that GOSS negotiate a schedule of payments with creditors according to a pre-defined calendar. This timeline may pose a liquidity problem for some creditors who may be unable to wait for payment in tranches. As part of the liquidation plan, GOSS will prioritize payments to smaller vendors.