

May 5, 1958

GENERAL ACCOUNTING OFFICE
SUMMARY OF
NONMILITARY ASSISTANCE PROGRAM
FOR LAOS

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GENERAL ACCOUNTING OFFICE

SUMMARY OF

NONMILITARY ASSISTANCE PROGRAM

FOR LAOS

As requested by the Staff Director of the House Committee on Appropriations there is presented herein a brief synopsis of the assistance program for Laos as administered by the International Cooperation Administration and its predecessor agencies.

Audit By General Accounting Office

In the fall of 1956 representatives of our office, as part of our regular audit of ICA country programs, visited several countries in the Far East with particular concentration on Korea and Vietnam. Because of the past association of Vietnam, Cambodia and Laos as the Associated States of Indochina and because we were including a summary of past aid activities to Indochina in our report on Vietnam, we deemed it appropriate to include brief outlines of the Cambodia and Laos programs based on examination of ICA Washington records, as supplements of our report to the Congress on Vietnam. A draft of our report on the three countries was sent to ICA in July 1957 for its review. The agency's comments were not received until January 1958.

During the intervening period information came to our attention from various sources concerning disturbing aspects of the program in Laos. In December 1957 we decided that in the light of our audit responsibilities it was necessary to make a special field examination of the program at the

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ICA mission in Vientiane. Arrangements were made to have such an examination made by our Far East Branch, and the Director of ICA was so notified. At the same time it was decided to issue separate reports to the Congress on each of the three Indochinese countries. The reports on Vietnam and Cambodia are in the final stages of processing and should be released shortly.

The examination in Laos was made in March 1958, and a draft report thereon was received by us in late April. We are currently reviewing this draft and updating our previous audit work at the Washington office of ICA. Our plans are to combine the field and headquarters work into a single report to the Congress covering the Laos program. Release of this report depends very largely on how long ICA requires to review the draft and forward its comments to us.

The summary of the program given hereafter has been taken from our audit data gathered to date.

Background and Level of Aid

United States aid to Laos began in fiscal year 1951 and was furnished as part of an economic and technical assistance program for the three Associated States of Vietnam, Cambodia, and Laos on a unified basis. Aid for the three countries under this program totaled 115 million dollars, of which it has been estimated that 70 million dollars was attributable to Vietnam, with lesser amounts for Cambodia and Laos, the latter having received the smallest portion.

Following the granting of full independence effective in January 1955, the United States initiated separate and expanded assistance programs in each of the three countries. In the three year period 1955-1957, assistance to Laos has totaled about 135 million dollars.

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Purposes of Aid

ICA has informed us that for overriding political and military considerations the United States is committed to support a Lao army of approximately 25,000 men at a cost of over 25 million dollars a year. The level of aid has been based principally on the cost of maintaining the Lao military forces for which the United States assumed the full burden of support. More than 85 percent of the local currency resulting from United States dollar aid was programed for this purpose. Military hardware for the Lao army is furnished under the military assistance program administered by the Department of Defense. This program is not included in this summary. ICA has intensified its activities for economic and technical development by financing various projects, of which transportation and public administration were the largest.

Nature of Aid Program

The main objective of the ICA program has been to generate local currency (kips) for military support including troop pay, maintenance, housing, etc. According to ICA its established procedures for generating local currency, namely procurement authorizations for financing the import and sale of commodities, would have been too slow in obtaining the kips necessary to meet military payments. Also, the economy of Laos could not absorb imports in the amounts required to generate the needed kips. For these reasons the agency considered it necessary to provide the greater part of aid in the form of cash grants.

Under this form of aid United States Treasury dollar checks are given to the Government of Laos which in turn deposits a corresponding amount of

kips in a special counterpart account from which they are withdrawn for the intended purposes. The Government of Laos borrows the required kips from the National Bank of Laos. The dollar funds serve as currency backing until they are converted into kips by sale to importers; the kips thus produced are applied to repay the borrowings. Approximately 95 million dollars - 70 percent of the total dollar aid for the three years 1955-57 - have been in cash grants.

Cash grants have been supplemented by financing of commodity imports under the regular procedures - about 25 million dollars in the 3-year period. The kips generated from these imports have likewise been deposited in the special counterpart account.

Approximately 10.6 million dollars have been devoted specifically to economic and technical development, principally for improving and maintaining the country's road system, providing equipment and supplies for the civilian police organization, improvement of navigation on the Mekong river, projects in the field of public administration and other smaller projects.

The composition of the aid program for each of the three years, as to dollar funds and allocation of the resulting local currency, as of June 30, 1957, is summarized below.

<u>Dollar funds</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>Total</u>	<u>Percent of total</u>
	(in millions)				
Generation of local currency:					
Cash grants	\$28.2	\$33.7	\$32.7	\$ 94.6	70.0
Commodity import program	3.4	12.9	8.5	24.8	18.4
Project assistance	1.4	6.6	6.3	14.3	10.6
Administration	.3	.2	.9	1.4	1.0
	<u>\$33.3</u>	<u>\$53.4</u>	<u>\$48.4</u>	<u>\$135.1</u>	<u>100.0</u>

<u>Generated local currency</u>	<u>Dollar equivalent</u>	<u>Percent of total</u>
	(in millions)	
Deposits to special account	<u>\$98.5</u>	<u>100.0</u>
Withdrawals:		
Military support	84.4	85.7
Public administration projects	4.0	4.1
Transportation projects	3.0	3.0
Other projects	4.4	4.5
Other items	.5	.5
	<u>96.3</u>	<u>97.8</u>
Balance on deposit	<u>\$ 2.2</u>	<u>2.2</u>

Special Problems in Laos

The aid program has been hampered by conditions which, while common to all underdeveloped countries, assumed particular importance in the case of Laos.

The new state of Laos has little to recommend its economic future. Landlocked, the mountainous area within its borders measures approximately twice the size of Pennsylvania. Ninety percent of the estimated population of 1,500,000 are reported to be subsistence farmers, generally illiterate and primitive in culture. Only eight percent of the land is cultivated. The gross national product, mostly foodstuffs, is estimated at about \$100,000,000 annually.

The new government was seriously lacking in trained administrators and technical skills; the economy of the country was primitive and there was an absence of economic and statistical data. The requirements of foreign exchange for imports, the support of a relatively large standing army, the furnishing of essential government services, which heretofore had been the responsibility of France, and the need to develop a backward economy were considered beyond the capabilities of the country. The dissolution of the Indochinese monetary union necessitated the development of new financial and commercial facilities.

On top of these conditions the government was harassed by conflict with the Pathet Lao which occupied two northern provinces and refused to abide by the Geneva Agreement of 1954. Hostilities were brought to an end in October 1957 through an agreement by which the Pathet Lao leadership was given a place in the cabinet of the government.

The International Cooperation Administration has had great difficulty in staffing a mission in Vientiane, the capital city. Living conditions in Laos are probably worse than in other underdeveloped countries. Housing is inadequate and expensive. Educational and recreational facilities are almost completely unavailable. Sanitation is a major problem of everyday living.

Observations on Administration of Program

Due in part to the special problems just mentioned, the administration of the program has been beset by serious deficiencies. On the other hand, the agency contends that the preservation of the independence of Laos has been the primary objective of the program and that to date this objective has been accomplished. ICA has been fully aware of the deficiencies in the program since its early days and, together with the State Department, has been exerting continuous efforts to overcome them. Special study groups, internal audit and evaluation teams have examined the program and made recommendations for improvements. We have also been told that meetings at high diplomatic levels have been held in an endeavor to resolve the basic issues that contribute to the deficiencies. As far as we know, progress to date has not been satisfactory.

In economic development some achievements have been made. The highway between the two principal cities has been reopened. Shipping on the Mekong river has been improved. The building of small dams has expanded irrigation areas. Malaria control and yaws eradication have improved health conditions at the village level. However, some of the larger projects have fared poorly in terms of administration, and accomplishments to date represent only a beginning in a backward country like Laos.

The more important areas of concern in the administration of the program may be grouped in the following categories.

1. Need for monetary reform

The official exchange rate which governs the deposit of counterpart funds is 35 kips to the United States dollar. This rate is unrealistically low, the free rate in neighboring Thailand and Hong Kong being about 100

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to 1. The use of this official rate substantially increases the cost of United States aid, particularly since the primary objective of the aid has been to generate local currency for military support. This rate has also contributed to certain abuses such as profiteering, diversion of commodities, and political influence in obtaining import licenses.

ICA has considered the exchange rate the root of its problems in the assistance program. In spite of many consultations with the Lao Government about fixing a more realistic rate, no progress appears to have been made. A plan offered by United States officials at high level meetings in Washington in January 1958 was rejected by Lao representatives. We understand that further discussions have been postponed until after the May elections in Laos.

2. Malpractices in the importation of commodities

Inadequate administrative machinery in the Lao Government, coupled with the unrealistic exchange rate, encouraged various forms of malpractices, mainly in the use of cash grants.

a) Improprieties in the issuance of import licenses

Issuance of import licenses by the Lao Government to use the foreign exchange made available by ICA is subject to approval by ICA. However, there have been no systematic import plan, no adequate statistical data to determine commodity requirements, no definite criteria for identifying legitimate importers, and insufficient trained personnel to properly administer the operation.

Investigations by ICA disclosed that officials of the Lao Government have been financially interested in certain importing firms; this is

reportedly an acceptable practice in the area. On a number of occasions the ICA mission has been bypassed in the approval of licenses; the mission was informed that on some occasions internal political necessities impelled the issuance of licenses without ICA approval. Although an American management firm under a contract financed by ICA has been working with Lao authorities for the past two years to develop better administration of the import program, serious deficiencies still exist.

b) Diversions and overpricing of commodities

Diversion occurred in two ways - commodities consigned to Laos were diverted en route, and commodities which reached Laos were illegally shipped out of the country. This practice has been attributed to several causes: (1) inability of the Laos economy to absorb commodities in such large amounts, (2) unstable political and economic conditions making it desirable for people to transfer money out of the country, (3) the low exchange rate affording opportunities for attractive profits through sale of commodities in Thailand and Hong Kong. Diversions were facilitated by the inability until several months ago to obtain through-bills of lading to Laos, thereby enabling the importer to take delivery in Bangkok.

Other irregularities took the form of overpricing commodities by falsifying invoices and also by delivering inferior goods. The excess amounts were usually deposited outside the country, sometimes reportedly with the collusion of the suppliers.

3. Ineffective control of commodity program

Control procedures of ICA have been ineffective to cope with the various malpractices. The mission has been unable to carry out systematic end-use inspections because of (1) lack of personnel, (2) the reluctance of the Lao Government to permit such inspections, and (3) lack of information on commodities purchased with cash grants. Of the relatively few inspections made, several evidenced unsatisfactory use of ICA-financed goods or improprieties in one form or another, but little positive action appears to have been taken. At the time of our field examination, no end-use inspections were being made, principally because the Embassy had restricted mission representatives from contacting Laotian nationals.

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4. Military budget support

In 1955, when ICA agreed to finance Laos military costs, the country's forces were in excess of the level determined necessary by the United States Government. Although in 1956 Laos agreed to reduce its army to the stipulated level, the mission had no reliable means of determining its strength. Principal liaison was maintained through the French training mission.

In the first year of program operations, ICA made no provision for screening allowable expenditures. The ICA mission was not considered responsible for the operation. In December 1955, a separate advisory group was formed, but the group has not had financially trained personnel to make the necessary reviews. Information from several sources indicated that the costs of military support may have been too high and that significant savings may be realized through a review of expenditures.

ICA provides 100 percent of the costs of the military establishment. Laos was considered unable to make a financial contribution. The United States has not deemed it advisable to request Laos to increase tax revenues or resort to deficit financing to enable it to make a financial contribution or make part of the troop payments in kind.

5. Project assistance

a) Maintenance of national roads

This vital project was slow in getting underway because of delays in contracting for required technical service. Subsequently the execution of contracts with three separate firms caused an overlapping of functions. We are informed that a new plan has been arranged which should correct this condition. Mission investigations revealed that considerable quantities

of ICA-financed road equipment had been abused and property control records were inadequate. Our inspection confirmed these reports.

b) Civil police administration

This project was designed to expand and consolidate the civil police forces, improve their mobility and communications, and train its personnel. While this force has been expanded from about 800 to 2,900 men, we were advised that only about 400 have had basic police training. In addition to ICA, both France and Great Britain were engaged in training elements of the police force, but apparently there was insufficient coordination among the three groups. Factors adversely affecting success of the project were the lack of a clear definition of the force's mission, inadequate maintenance of ICA-furnished transport equipment, and reluctance by the police to permit ICA mission personnel to inspect records pertaining to United States-financed equipment.

The Laos program has served predominantly as an instrument of United States foreign policy and security interests, and thus it is not within our province to appraise whether program objectives have been accomplished. From an economic viewpoint, continuation of the program will be costly and improvement in its administration will be slow. Based on our examination, we believe it is doubtful whether Laos can become economically self-sufficient in the foreseeable future.

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