

RISK ASSESSMENT AND RISK MANAGEMENT PLAN (SUMMARY) ¹

1. **Background.** As required by the Second Governance and Anticorruption Action Plan ² of the Asian Development Bank (ADB), this assessment covers risks in the areas of public financial management, public procurement, and combating corruption in Papua New Guinea (PNG). It also summarizes the results of governance risk assessments for the transport and energy sectors, which are expected to comprise roughly 80% of ADB lending operations during the country partnership strategy, 2016–2020 period.

2. **Public financial management.** PNG has made progress in strengthening its budgeting system through broad adherence to three successive 5-year medium-term fiscal strategies since 2002. However, while the budget process aligns allocations well with priority sectors, many of the projects which are funded have often not had sufficient levels of preparatory and feasibility work undertaken to enable timely implementation. This misalignment requires government agencies to rush designs, cost estimates, and tenders, which often leads to delays in contract implementation. Delays lead to underspending, and the practice of “parking” funds in trust accounts. Other concerns include a lack of adherence to established rules and processes and the weakness of government agencies with regard to accounting and financial reporting, cost recovery mechanisms, the role and management of state-owned enterprises (SOEs), community service obligations, and the financial capacity of lower-level governments.

3. **Public procurement.** The Government of PNG reformed its procurement processes in 2003–2009, which included the creation of the Central Supply and Tender Board to develop and oversee the procurement system. However, capacity limitations within the board and within implementing agencies responsible for procurement continue to delay project execution and reduce transparency. Additional concerns exist about project management, supervision, and monitoring, as well as the limited albeit growing capacity of private sector contractors. The main challenge is to ensure that the institutions and staff involved have the capability to put into practice the rules, procedures, and controls that are already in place. This makes the continued development of a professional cadre in public procurement important, as is the need to undertake skills development of frontline staff to properly execute government procedures. Particular vulnerabilities in the procurement system include (i) low internal audit capability and poor procurement planning in public sector agencies, and (ii) inadequate monitoring of implementation of procurement decisions and appropriate quality assurance of services provided.

4. **Combating corruption.** Despite recent attempts to create new anticorruption institutions, the general perception remains that corruption is endemic in PNG.³ Various cultural factors are difficult for the government or ADB to address in the near term, but legal structures and institutions do exist to improve transparency. The questions turn to implementation capacity. Anticorruption rules suffer from poor enforcement and a culture of impunity, and the limits of political commitment. Accountability institutions exist and have powers to investigate corruption but suffer from limitations in resources, staff, and capacity. ADB will continue to work with key development partners such as the Australian Department of Foreign Affairs and Trade

¹ This is a summary of ADB. 2014. *PNG Country Governance Risk Assessment Report and Risk Management Plan*. Manila. It also draws on two sector Risk Assessment and Risk Management Plans (RARMP's) in the transport and energy sectors, also prepared in 2014. The analysis follows ADB's Second Governance and Anticorruption Action Plan framework (available upon request).

² ADB. 2006. *Second Governance and Anticorruption Action Plan*. Manila.

³ ADB 2014. *Private Sector Survey: An Assessment of Constraints to Private Sector Investment in PNG*. Port Moresby: Private Sector Development Initiative and Institute of National Affairs.

and the World Bank to develop strategies to enhance government fiscal and anticorruption practices.

5. **Sector operational risks.** In addition to the generic risks described above, operations can face risks that are specific to individual sectors that could affect the successful implementation of the new country partnership strategy. The following is a summary of risks as they apply to the PNG country partnership strategy, 2016-2020 focus sectors of transport and energy:

- (i) **Transport sector.** ADB-financed transport projects in PNG have shown improvement in several respects over recent years, including less time needed to sign loans once approved, more accurate cost estimates, and improved disbursement rates. Nonetheless, projects supported by ADB continue to face a number of key challenges, including frequent mismatches between government agencies' requests for specific projects and budget appropriations. This creates undue pressures to meet tender and procurement requirements. Poor information from the Department of Works and Implementation Road Asset Management Systems hampers detailed project design, with allocations often remaining unspent and deposited in poorly managed trust funds that lack strong accountability mechanisms. Delays by executing agencies in meeting procurement requirements, combined with capacity limitations in private sector construction and land compensation issues, further delay implementation.
- (ii) **Energy sector.** ADB's activities in the energy sector are primarily conducted with PNG Power (PPL). Past internal audits of ADB assistance found no clear indications of fraud or corruption. This cannot, however, be assumed to mitigate all risks. The resources, staff, and responsibilities of the Ombudsman Commission and the auditor general only permit limited oversight of procurement practices. Further, while a financial management assessment of PPL revealed that its financial management is generally satisfactory, improvements could be made in the areas of internal control relating specifically to account reconciliation procedures, prevention of restatement of accounts at regular intervals, and integration of systems into the Oracle-based accounting system. Further, while PPL is an SOE with an implied cost-recovery business model, it is generally unable to generate sufficient revenue from user charges to cover its entire recurrent and capital expenditures. This has often led to depriving assets of maintenance, and ultimately threatening service quality and sustainability of investments. Although PPL is an independent SOE, it is highly prone to political interference in its operations and, most notably, its investment decisions.

Risk Management Plan

Actions to be taken by ADB	Selected Indicators
Public Financial Management	
Priority areas of future assistance will include strengthening public financial management through design and implementation of capacity development programs in the areas of (i) planning framework, prioritization, and project selection; (ii) investment programming; (iii) maintenance funding; (iv) due diligence in project preparation; (v) expenditure controls; (vi) financial reporting; (vii) trust account management, controls, accounting, and reporting; (viii) financial accountability of statutory authorities; and (ix) transparent and accountable natural resource revenue management. ADB public sector management technical assistance will also include support for improved infrastructure design and project readiness in its priority assistance sectors.	Establishment of transparent and accountable sovereign wealth fund Successful piloting of statutory authority financial monitoring framework to at least 20 agencies
Procurement	
At the project level, ADB will ensure appropriate mechanisms are put in place to address weaknesses in procurement controls. This will include efforts to ensure (i) executing agencies' websites disclose updated and detailed information on project implementation; (ii) timely disclosure of information on selection of consultants and contractors through local media; and (iii) the quantity, quality, and cost of civil works to be independently verified. ADB will also support the CSTB and government agency procurement offices in infrastructure tender preparation, contract management, and record keeping, and support the Government of PNG's efforts to establish a company blacklisting system identifying underperforming contractors.	Average infrastructure procurement timeline reduced to 26 weeks by 2020 (2014 baseline: 52 weeks) Average number of contract variations per project reduced from four to one by 2020
Corruption	
Project implementation units funded by ADB will enhance their efforts to establish robust mechanisms to mitigate the risk of the manipulation of processes for personal gain. This will include efforts to encourage government agencies to institute regular internal audits, which will be complemented by ADB directly contracting external audits with international standard audit firms for all project-funded activities. On an ongoing and continuous basis, ADB will provide support for institutional capacity development, staffing, and resources of accountability institutions.	Number of institutions submitting unqualified annual reports 6 months after fiscal year close reduced to zero by 2020
Sector Level – Transport and Energy	
To ensure procurement and corruption risks are appropriately managed within ADB's key executing agencies, ADB will apply the following measures: (i) international supervision consultants to monitor all construction and operational activities complemented by close supervision from ADB and other development partner staff; (ii) contracts financed from ADB funds will include provisions specifying the right of ADB to audit and examine the records and accounts of all contractors, suppliers, consultants, and other services; (iii) there will be independent external auditing of contracts, project accounts, and financial statements; and (iv) forensic audits will be conducted of suspected corruption cases. ADB will also assist in strengthening public financial management by providing technical assistance to support infrastructure budget planning and coordination. These efforts will include assisting DOWI to develop and manage a comprehensive RAMS database on national highways and rural roads, and ensuring all project designs have incorporated design standards that are resilient to the impacts of climate change. ADB will undertake enhanced engagement between safeguards specialists and the Department of Lands prior to loan mobilization and effectiveness, including support for initiatives to standardize compensation procedures. ADB will undertake initiatives to develop management skills and access to finance among medium-size and large contractors.	Contractor performance database established and is utilized in bid evaluation Existence of standard tender documentation within agencies being used during procurement processes All transport projects appearing in the national budget have been prioritized and submitted by DOT (2014 baseline: 60%)

ADB = Asian Development Bank, CSTB = Central Supply and Tenders Board, DOT = Department of Transport, DOWI = Department of Works and Implementation, PNG = Papua New Guinea, PPL = PNG Power, RAMS = Road Assessment Management System.

Source: Asian Development Bank.