SECTOR ASSESSMENT (SUMMARY): PUBLIC SECTOR MANAGEMENT[1]

Sector Road Map

1. Sector Performance, Problems, and Opportunities

1. Strengthening public financial management (PFM) is a key to broader public sector management reform in Papua New Guinea (PNG). Following a decade of deterioration, PFM arrangements have improved since 2005 albeit from a low base. The government has pursued a PFM reform program since 2003, when PNG was emerging from a recession and public finances were under serious strain because of poor fiscal discipline, weak expenditure management, and a high debt. A March 2009 assessment of public expenditure and financial accountability (PEFA) confirmed progress in several PFM areas.[2] Macroeconomic stability has improved, with budget surpluses achieved since 2004. The debt burden is significantly lower and more balanced. A proportion of the windfall revenue from the commodity price boom during 2005 to 2008 has been set aside for future use. Budget preparation is more orderly, transparent, and consultative. Ongoing improvements in the openness of budget preparation, as required by the Fiscal Responsibility Act, 2006, have enhanced opportunities for women's organizations, as well as gender-equity advocacy and civil society groups, to participate in national planning and budgeting processes. Headway has been made on clearing backlogs of public accounts. More active engagement by the Parliamentary Public Accounts Committee and the Auditor-General's Office are important indicators of improving financial accountability.

2. Despite these improvements, PFM remains weak, which impedes the government's ability to control expenditures, disburse the budget as approved, and provide essential services. Fundamental arrangements are in place, but implementation weaknesses mean that the systems and procedures for expenditure and payroll control cannot be relied upon to ensure appropriate accountability. Transparency in budget execution is weak, as the unauthorized diversion of funds, including resources for regional development, undermines budget integrity. Hence, it is difficult to track expenditures to ensure the budget is delivered as approved. Accounts remain open and active long after the end of the financial year. Delays in preparing and releasing public accounts and audit reports have undermined oversight. Statutory authority accountability is particularly weak.

3. Effective PFM is a necessary precondition for achieving success in other sectors and thematic areas including gender equity. For instance, addressing issues related to road maintenance, the provision of health services, and HIV prevention requires mechanisms to allocate budgetary funds for these purposes at different levels of government. These mechanisms must then ensure that such funds are available as planned and when required. To achieve this requires effective resource allocation in accordance with sector and detailed managerial priorities, equity in the allocation of public financial resources, mechanisms to ensure the release of funds with minimal leakage, and the availability of cash as required. Effective PFM systems should deliver these processes; where not present, as in PNG, these processes are impeded.

[1] This summary is based on Government of PNG, Department of Finance. 2008. *2008 Public Expenditure and Financial Accountability (PEFA) report*. Port Moresby. Unpublished.
[2] Department of Finance. 2009. *Papua New Guinea: Public Financial Management Performance Report*. Port Moresby.

2. Government's Sector Strategy

4. The PNG Development Strategic Plan, 2010–2030[3] acknowledges the weaknesses in PFM and has set ambitious targets for improvement based on the World Bank worldwide governance indicators and PEFA indicators. A detailed action plan for public expenditure reform was prepared under the 2003 public expenditure review and rationalization (PERR) process. However, momentum has diminished since 2005, principally because higher-than-expected revenues reduced reform imperatives and the original PERR focus has less relevance in the current environment. PERR participants—the government, the Asian Development Bank (ADB), the Australian Agency for International Development, and the World Bank—agreed in March 2007 that the process should be refocused and revitalized.

5. In response, development partners prepared a framework for fiscal enhancement (FFE).[4] The FFE identified three areas where the efforts of the government, supported by development partners, could be focused in macro-fiscal and public fiscal management: (i) managing volatility by maintaining long-term fiscal sustainability and safeguarding windfall revenue; (ii) strengthening service delivery by prioritizing budget expenditures, and effectively implementing them; and (iii) reinforcing the integrity of budget systems and processes by delivering comprehensive, transparent, and accountable budgets.

6. The FFE identifies nine action areas with assigned levels of priority: (i) reducing the cyclicality of the fiscal stance i.e. cool down the economy when it is in an upswing, and stimulate the economy when it is in a downturn; (ii) managing and safeguarding windfall revenue; (iii) improving budget formulation and costing of service delivery objectives, and adjusting budget composition to support better service delivery, including at the sub-national level; (iv) deepening the operational value of oversight agencies and support for internal audits; (v) reducing debt risk and establishing a sustainable borrowing and investment framework, including in relation to statutory authorities; (vi) improving the alignment of development and recurrent budgets and trust account spending to enable prioritization across the whole budget; (vii) removing obstacles to budget implementation; (viii) engaging community and civil society as partners in monitoring the transparency and quality of public expenditures; and (ix) managing risk through better internal accounting. Priority one action areas (i–iv) are considered to have the greatest potential benefit for PNG and a higher level of urgency for implementation support than priority two areas (v–ix).

7. Development partners engaged with the government in late 2009 on the action areas in the FFE. However, more work remains to be done, particularly in finalizing a strategy for FFE implementation and integrating implementation with existing frameworks such as the Financial Management Improvement Program (FMIP)[5] and a potentially refocused PERR implementation committee.[6]

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[3] Government of Papua New Guinea, Department of National Planning and Monitoring. 2010. *Papua New Guinea Development Strategic Plan, 2010–2030.* Port Moresby.

[4] ADB, Australian Agency for International Development, World Bank. 2009. *Framework for Fiscal Management Enhancement in Papua New Guinea.* Port Moresby.

[5] The government initiated the FMIP and subsequent Financial Management Project with development partner support. The FMIP provided a policy framework, plans, and an institutional focus for reform of financial management. The Financial Management Project covered (i) improved planning and budgeting systems, (ii) improved budget execution and accounting systems, (iii) enhanced information technology systems, (iv) the provision of training and strengthening of human resource management, and (v) enhanced change and program management.

[6] Chaired by a deputy secretary of Treasury, the PERR implementation committee identifies, prioritizes, and monitors reforms.

3. ADB Sector Experience and Assistance Program

8. PFM was one of four focal areas in the PNG country strategy and program, 2006–2010 (CSP).[7] The FMIP and the PERR program were to provide the main conduits for ADB's engagement. In late 2006, the processing of supplementary financing for the Financial Management Project involved assessing the status of the project, which revealed critical weaknesses.[8] In response, ADB and the government identified remedial actions, but they were unable to confirm these actions and the processing of the supplementary financing was discontinued in early 2008. Meanwhile, because of the identified project weaknesses, FMIP implementation has fallen further behind schedule. Following the discontinuation of the supplementary financing, the government has continued to finance implementation of the integrated financial management information system.

9. The CSP results framework identified nine PEFA indicators that were expected to improve through, in part, support from the FMIP and the PERR program. However, as the 2009 PEFA assessment found, the progress of PFM reform stalled from 2005 to 2008. The failure to achieve PFM-related CSP results was due primarily to (i) emerging "resource curse"[9] manifestations, including the weakening of reform incentives caused by large revenue flows from the resource sector and expectations of even larger flows through the liquefied natural gas project; (ii) a lessening of high-level reform leadership; (iii) the loss of PERR momentum; and (iv) significant delays in implementation of the FMIP and the integrated financial management information system.

10. ADB's experience with PFM reform in PNG shows the following:

- (i) Reforms must be driven by the government. Attempts to impose external solutions have been largely unsuccessful, whereas government-led reforms—even if they take longer—tend to be successful and sustainable.
- (ii) Change is not easy and takes a long time, but can be achieved and made sustainable.
- (iii) Capacity must be built in parallel with other reforms and should be an ongoing process. Lack of skilled employees in the government continues to be a problem, which is exacerbated by high private sector demand for personnel with financial skills.

11. ADB's role in PFM remains pertinent. In supporting the 2005 Paris Declaration on Aid Effectiveness,[10] recipient countries (including PNG) are committed to publishing timely, transparent, and reliable financial reports. Development partners (including ADB) are committed to relying on country PFM systems to the maximum extent possible. However, developing countries and development partners are not on track to meet the Paris Declaration commitments. On 4 September 2008, developing countries' ministers and heads of development partner agencies, including ADB, agreed to accelerate and deepen implementation of the Paris

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[7] ADB. 2006. *Country Strategy and Program: Papua New Guinea, 2006–2010.* Manila.

[8] Weaknesses included the absence of an overarching PFM reform strategy, mixed stakeholder support, a lack of project and change management capacity, overly ambitious implementation scope, inadequate implementation planning, the absence of detailed change management and training plans, flaws in contracting and consulting arrangements, under-resourcing of counterpart implementation teams, funding uncertainties, and inadequate project financial management arrangements.

[9] The "resource curse" refers to the paradox that countries with an abundance of non-renewable natural resources, like minerals and fuels, tend to have less economic growth and worse development outcomes than countries with fewer natural resources.

[10] Paris Declaration on Aid Effectiveness. 2005. http://www.oecd.org/dataoecd/11/41/34428351.pdf

Declaration. Relevant commitments include strengthening PFM systems, aiming to provide 66% of aid through program-based approaches, and channeling at least 50% of government-to-government assistance through country fiduciary systems.[11] In that connection, ADB relies heavily on government procurement and auditing arrangements, but less so on accounting systems.

12. ADB will continue to support PFM reform in accordance with government strategies. Acknowledging that the PFM environment has changed since the CSP was developed in 2006, ADB and other development partners prepared the FFE and will be targeting PFM support to the action areas identified in the FFE.

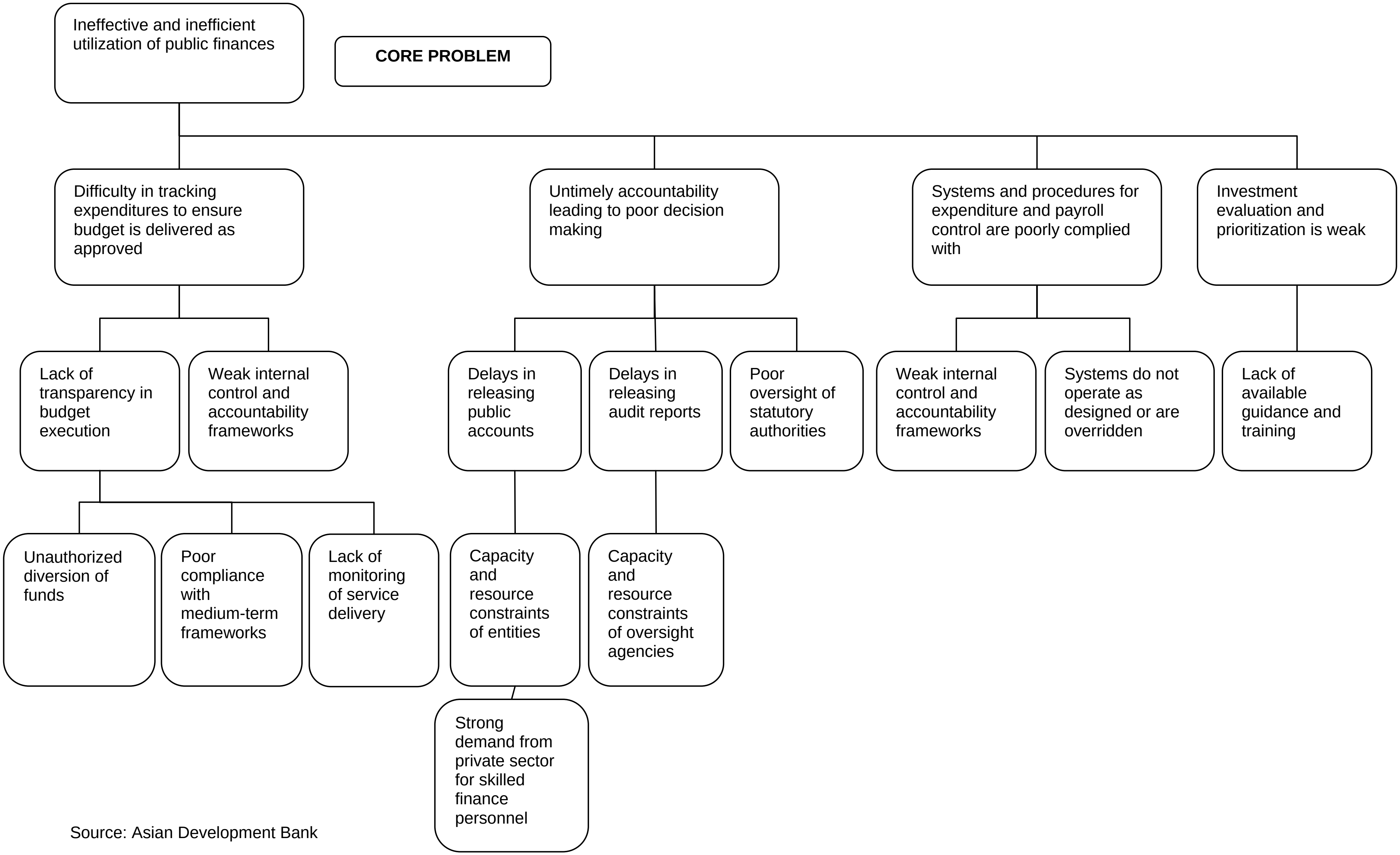
13. During 2010–2012 ADB will support stronger oversight of statutory authorities, better project evaluation and prioritization, and enhanced monitoring of sub-national service delivery.[12] Following the completion of this support, ADB will continue to target selected FFE themes over the period of the new country partnership strategy. FFE support will be primarily through technical assistance and will focus on areas that support ADB's operations in PNG.

14. More broadly, ADB's interventions will contribute to a more efficient and effective government administration and improved aid effectiveness. In relation to the first outcome, PEFA indicator changes will be monitored to assess the preservation of standards of accountability and transparency, and the maintenance of controls on the use of public funds. In relation to the second outcome, effectiveness will be measured by the extent of alignment of ADB assistance with expenditure priorities and the reliance ADB places on government procurement systems.

15. In terms of broader public sector reform, ADB also supports state-owned enterprise reform and the implementation of public–private partnerships. More details on ADB intervention in these areas are in the private sector assessment.[13]

[11] Accra Agenda for Action. 2008. http://www.undp.org/mdtf/docs/Accra-Agenda-for-Action.pdf
[12] ADB. 2009. *Papua New Guinea: Supporting Public Financial Management.* Manila (TA 7427-PNG, for $1,000,000, approved on 10 December 2009, financed by the Japan Special Fund).
[13] The private sector assessment is included as a linked document to the PNG CPS, 2011–2015 (Appendix 2).

Problem Tree for the Public Sector Management Sector



Source: Asian Development Bank

Sector Results Framework (Public Sector Management, 2011–2015)

Country Sector Outcomes		Country Sector Outputs		ADB Sector Operations	
Outcomes with ADB Contribution	**Indicators with Targets and Baselines**	**Outputs with ADB Contribution**	**Indicators with Incremental Targets (Baselines Zero)**	**Planned and Ongoing ADB Interventions**	**Main Outputs Expected from ADB Interventions**
More effective and efficient utilization of public finances for service delivery and infrastructure provision	ADB Country performance assessment indicators 8a (from 3.0 in 2011 to 4.0 in 2015) Number of provinces aligning at least 50% of recurrent expenditures (as measured by the NEFC cost of services estimate) with the priority areas of road maintenance, education, health, agricultural extensions, and village courts (from 2 in 2011 to 10 in 2015) Number of SOEs rated as effectively meeting their service delivery targets (from 2 in 2011 to 5 in 2015 Increased private investment in infrastructure through PPPs (from 0 in 2011 to 50 million in 2015)	Strengthened public financial management systems with appropriate budget and accountability structures, and transparent processes. Well-managed state-owned enterprises that operate on commercial terms Policy and regulatory framework on PPPs provided and well managed	Rating on country performance assessment indicators 13a, 13b, and 13c (from 3.0, 3.4, and 3.5 in 2011 to 4.0, 4.5, and 4.5 in 2015) Number of public expenditure and financial accountability indicators 1–28 maintained at grade C or above (from 18 in 2011 to 27 in 2015) SOEs (i) with a statement of corporate intent that include a mix of SMART financials and/or non-financial performance measures (from 0 in 2011 to 5 in 2015); and (ii) delivering CSOs that are contracted to the government on a full cost recovery basis (from 0% in 2011 to 50% in 2015) Kina value of projects implemented through the PPP arrangement (from 0 in 2011 to K50 million in 2015)	**Planned key activity areas** High-level economic advisory services provided through the Pacific Economic Management TA **Pipeline projects with estimated amounts** Support for stronger oversight of statutory authorities, better project evaluation and prioritization, and enhanced monitoring of sub-national service delivery ($1 million) **Ongoing projects with approved amounts** Procurement training delivered by ADB's Central Operations Services Office Facilitating public–private partnerships SOE reform	**Planned key activity areas** Increased capacity to manage resource volatility **Pipeline projects** Oversight of statutory authorities strengthened Project evaluation and prioritization improved Procurement practices assessed and improved Monitoring of sub-national service delivery enhanced Road map for domestic bond market development prepared Project development facility established and in use for financing PPP transaction preparation Implementation of new CSO framework **Ongoing projects** Improved procurement capacity Adoption of PPP legal framework and establishment of PPP unit. Design of new CSO framework

ADB = Asian Development Bank, CSO = community service obligation, NEFC = National Economic and Fiscal Commission, PPP = public–private partnership, SMART = specific, measurable or meaningful, achievable, relevant, time bound, SOE = state-owned enterprises, TA = technical assistance.