

**SUBMISSION TO THE SENATE STANDING COMMITTEE ON FOREIGN
AFFAIRS DEFENCE AND TRADE: THE DELIVERY AND EFFECTIVENESS OF
AUSTRALIA'S BILATERAL AID PROGRAM IN PAPUA NEW GUINEA**

Investing in Institutional Linkages in PNG

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(Paul Flanagan wrote his first policy paper on PNG in 1978. He did this while working in the Overseas Aid Section of the Australian Department of Finance, and prepared the report for his then division head, Bernie Fraser. He first visited the country in 1978 as a guest of the local Lions Club –travelling to all major urban centres over a month as well as the remote areas outside of Tari with his Uncle Kevin who was a Catholic priest in the area from 1970 to 1974. He did his combined economic and political science honour's thesis in 1983 on the PNG Southern Highlands Integrated Rural Development Project. He worked in a range of policy and program roles in Australia's overseas aid organisation (ADAB, AIDAB and AusAID) from 1986 through to 2002. These roles included being the first Director responsible for establishing the new aid program to Timor Leste; several years as Director of aid programs to Africa and the Middle East; being Director of the sectoral advisory team on environment, agriculture and physical infrastructure programs; Director of the section in charge of the annual budget, corporate planning and effectiveness review; and acting Branch head for over a year for humanitarian, multilateral and NGO programs. In the Australian Treasury, after time heading the strategic tax policy area, he headed the International Finance and Development Division from 2008 to 2011. He was then seconded to the PNG Treasury as Team Leader and Senior Advisor in the SGP program from February 2011 to August 2013 (with the only other substantive SES2 APS in PNG at the time being the High Commissioner). He returned to the Australian Treasury as Chief Advisor, Foreign Investment and Trade Division retiring in June 2014. He started at the Development Policy Centre at the ANU in August 2014 as a Visiting Fellow, focusing on PNG public policy issues. He visits PNG regularly and writes on economic policy issues in PNG. He has just set up a separate company so he can work with the ANU on contract.)

EXECUTIVE SUMMARY: INVESTING IN INSTITUTIONAL LINKAGES IN PNG

- 1) The central focus of our bilateral aid program in PNG should be on helping PNG spend its own resources more effectively.
 - i) Aid is a small (less than 10%) and declining share of PNG's revenues.
 - ii) PNG and Australia share most priorities – political, economic and social. As PNG moves to a population of 30 million by 2050, it is vital that we have a prosperous and stable neighbour on our doorstep. We should focus on supporting PNG to deliver on its own priorities – including private sector driven growth – in ways which encourages PNG's economy to integrate with the Indo-Pacific region..
 - iii) PNG's capacity to deliver programs is in decline.
- 2) Governance assistance should be the primary pillar in our aid program with PNG – this is the means of helping PNG spend its own resources more effectively and to pursue policies that foster inclusive growth.
 - i) Australia lost its way on support for this key area a few years ago but it is now back on track.
 - ii) Governance assistance helps build the environment that allows the private sector to grow. This goes beyond support for vital areas such as law and order. It extends to supporting macro-economic stability (fiscal, monetary and external), creating market frameworks that support inclusive businesses and trade, providing essential economic infrastructure and fostering entrepreneurial leadership.
- 3) Institutional linkages programs are the most effective way of providing governance assistance
 - i) Long-term institutional linkages mirror the long-term challenges facing PNG.
 - ii) They provide a basis for a strong partnership approach, building on our shared ties, history and common interests.
 - iii) They can apply across the public, private, educational and community sectors.
 - iv) These institutional linkages programs must be adapted to specific challenges – and support local champions.
 - v) Allocating at least one half of the bilateral aid program to institutional linkage programs is value for money as small but sustainable annual improvements in PNG's own expenditures will represent a high and long-lasting rates of return for Australian aid.
 - vi) Considerable investment is required in improving PNG's private sector environment.
 - vii) Australia still has much to learn about how most effectively to support such programs.
 - viii) Measurement and performance indicators are particularly challenging for reasons of both measurement but also secrecy.
- 4) Australia can also contribute to building institutions through high level policy dialogue especially in the area of supporting the private sector.

1. The central focus of our bilateral aid program in PNG should be on helping PNG spend its own resources more effectively.

Australian aid at the time of independence in 1975 accounted for over half of all PNG central government revenues. Initially, this was in the form of untied budget support. Through time, the type of aid moved towards program and project aid. Primarily due to PNG's growth, aid is now a small (less than 10%) and declining share of PNG's revenues. PNG is no longer dependent on Australian aid to meet its priorities. At best, bilateral aid can be a catalysing complement to PNG's own activities.

We do not need Australian government aid to fund more textbooks or medicines – PNG has the resources to do this themselves. This submission will make the rather radical suggestion that at least one half of the entire aid program should be spent on a particular form of governance assistance – institution strengthening across the public, private, education and community sectors. Arguments for why this is appropriate, why it represents value for money and how it can be supported by both countries will be presented in this submission.

Why is it appropriate to allocate at least half of bilateral aid to institution strengthening?

PNG and Australia share most priorities – political, economic and social. At a strategic level, there are very few differences. Both countries want PNG to develop. Both countries want PNG to remain a constitutional democracy with regular fair elections. Both countries give priority in government expenditure to areas such as education, health, infrastructure, law and order and supporting the economic sector. Both seek inclusive, peaceful and sustainable development. There are of course differences at the margins where national interests may diverge – arguably Manus Island refugee processing is a current example, as has been some approaches towards dealing with corruption and the priority allocated to gender issues. However, overall, there is so much in the way of shared priorities that both countries can find ample scope to have Australia's aid program directly supporting PNG's priorities.

When I first visited PNG soon after independence, the population was around 2.5 million people. Since then, the population has approximately trebled to around 7.5 million people. This implies an extraordinary requirement every year for extra schools, teachers, health facilities, nurses, policemen and food. While some criticise PNG for its failure to continue basic services, the other side of the coin is that it is a remarkable testament to PNG that it has broadly continued to survive, and in some areas at least, increased the provision of services. PNG, a relatively poor country, has to support a new population of over 200,000 people every year. As PNG moves to a population of 30 million by 2050, it is vital that we have a prosperous and stable neighbour on our doorstep. We do not want over 10 million people living in absolute poverty only 10km from Australian land – which would be the case if the incidence of absolute poverty is not lowered from the current levels of around 40 per cent. Private sector driven growth will be vital for such a shared objective. This will include encouraging PNG to pursue policies which will integrate it with the opportunities of the broader Indo-Pacific region. As in Australia's past, there are powerful political pressures towards protectionism in its various forms which could damage PNG's prospects.

PNG's capacity to deliver programs is in decline. At the time of independence, one of the great legacies of Australia's period of colonial administration was the social capital invested in public institutions, including those vital for creating an enabling environment for the private sector. There were an estimated 3,000 Australian public servants working in PNG at the time of independence. Understandably, there was a strong localisation policy applied by the new government, and these

numbers dropped dramatically. However, many of the new public service leaders had been brought through an administrative system which had prepared them through both on-the-job training as well as various administrative colleges. Through time, these central institutions of the PNG state have drawn on this original social capital. Not enough was known of building sustainable institutions at the time of independence, and arguably Australia did not do enough in the decades following independence. The consequences of this slow decline is, for me, most powerfully captured in the words of senior PNG public servants interviewed at the start of this century. A copy of these interviews in 2004, by Lynn Pieper, is attached as Appendix 1 to this paper. Unfortunately, some of the hoped for reforms did not occur in the years following 2004, and some of the suggestions for support on pages 6 to 11 can be informed by additional experiences.

The long-term decline in the quality of institutions in PNG is its greatest development challenge. Without strong government institutions, there will be a weakening of the enabling environment for the private sector to provide the jobs and incomes that will form the backbone of PNG's advancement. Strong institutions are also vital for delivering on broader social outcomes that are built into PNG's constitution and development plans. Strong institutions are vital for converting PNG's wealth into the aspirations of its people¹.

2. Governance assistance should be the primary pillar in our aid program with PNG – this is the means of helping PNG spend its own resources more effectively and to pursue policies that foster inclusive growth.

Australia lost its way on support for this key area of governance a few years ago but it is now largely back on track.

Australia's aid program once understood that supporting governance institutions was the essential ingredient for reducing poverty. Such assistance is indirect – it is not as immediately satisfying as providing books or medicines to the poor in PNG. However, international experience suggests that support for good governance can be the most effective form of aid assistance. In AusAID's Policy Branch in 2001, I was pleased to lead a small team that helped produce the publication "Reducing poverty: the central integrating factor of Australia's aid program". The Foreword stated:

"This policy paper strengthens the framework under which the aid program addresses poverty. The four poverty pillars outlined in the paper are strongly linked to the sectoral priorities of the aid program, with a particular emphasis on the principles of good governance. Good governance means competent management of a country's resources and affairs in a manner that is open, transparent, accountable, equitable and responsive to people's needs. Although aid clearly has a role to play, the policies of our partner governments will be critical for mobilising domestic resources and international investment that are traditionally much, much greater than aid flows. Growth, the most effective weapon in the battle against poverty, is best achieved in an efficient, open, market-based economy. For markets to function, social norms and legal systems are needed that respect contract and property rights. Without the fundamentals of good governance, other direct approaches to poverty reduction may not be sustainable." Alexander Downer Minister for Foreign Affairs April 2001

The 2006 AusAID publication "Australian aid: Approaches to supporting governance" stated:

¹ 'Why Nations Fail' by Daron Acemoglu and James Robinson emphasises institutions are important for development and how they function depends on how political elites shape them.

“A far greater influence on reducing poverty than any basic resource transfer is the quality of governance and effective economic, legal and social structures.”

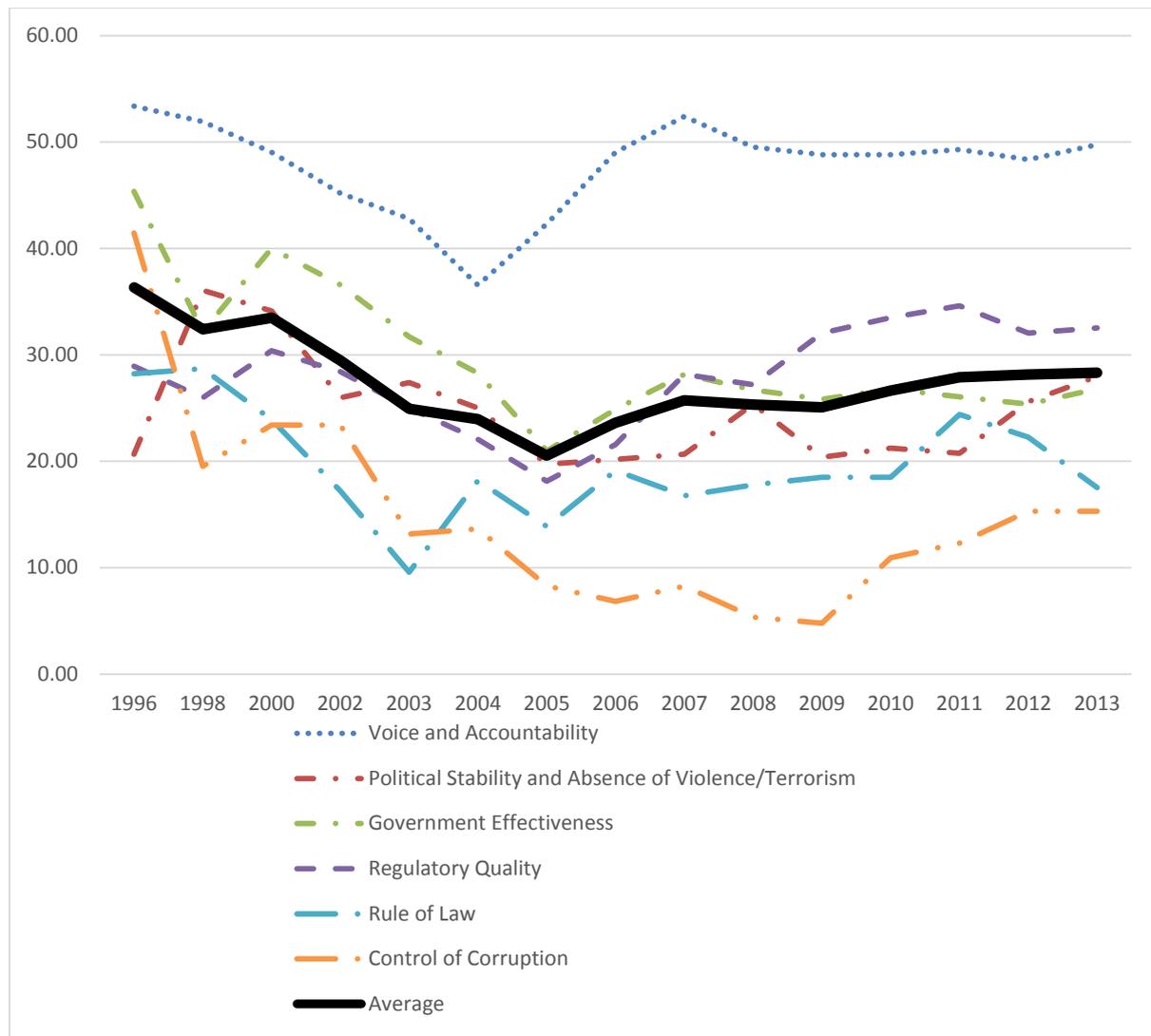
The 2008 PNG-Australia Partnership for Development had as one of its five “Priority Outcomes”: An Efficient and Effective Public Service, with one of the specific targets being “Improved public sector management, measured by an improvement in the WBI Government Effectiveness Score” (more on this score later).

In the context of PNG, the move away from governance was most clearly indicated through the decision to drop governance as one of the pillars of the Partnership for Development with PNG. The rationale for such reductions were related in part to reviews where justifiable concerns were raised around the dispersion and effectiveness of technical assistance in PNG. The 2011 Adviser Review recommended 181 (or 37%) of the 487 advisor positions in PNG be phased out (Table 1 of the report). However, the rationale for the reductions were not always well justified. For example, in a Devpolicy Blog on 24 January 2013 <http://devpolicy.org/governance-in-png-what-can-donors-do-20130124/> AusAID’s Principal Sector Specialist on governance showed a very similar graph to the following (although now updated to include 2013 data) with the conclusion:

“The data suggest that there has been little if any improvement in PNG governance over the last 15 years. The World Bank’s Worldwide Governance Indicators² show all six categories of governance are worse today than they were in 1996. These figures make grim reading for AusAID. So the question is, with what we now know, what can we do differently? “

² These indicators are available at <http://info.worldbank.org/governance/wgi/index.aspx#home>. In anything as difficult to “measure” as governance, there are inevitably critics of this measurement tool. However, at least this tool does attempt to quantify key elements of governance and track changes through time. I have also used a simple weighted average measure to make more obvious the overall trends – although clearly some of the indicators will be seen by some as more important than others.

Graph 1: PNG Governance Indicators - 1996 to 2013 – rankings basis



However, another look at the data suggest a possible very different interpretation. This is easiest to see by looking at the solid black line showing the average for the indicators. In 1996, PNG’s average percentile ranking was around 36% - so 64% of countries were doing better than PNG on these governance indicators. For the years from 1996 to 2005, all six categories of indicators did indeed decline (as well as the average). By 2005, it could be argued that 80 per cent of countries did better on governance than PNG. This is significant drop in rankings. Based on the interviews with senior PNG public servants included in Attachment 1, this decline had arguably been going on since at least the late 1980s. However, between 2005 and 2013, all six categories for measuring the quality of governance in PNG had actually improved (as well as the average). Clearly, still more needed to be done (with the improvement back to only around the 28th percentile), but there is a distinct kink in the graph around 2005 from decline to incline. So was anything being done that could help explain this change from substantial falls in performance to gradual improvement?

My contention is that the government at the time decided to very substantially increase its support for governance programs, especially institution-strengthening programs. Following concerns about the “arc of instability” in our region, and having sent troops into both Timor Leste and the Solomon

Islands, there was a strong consensus across the Australian government that actions should be taken sooner rather than later to support other countries in the region, especially PNG. A new type of institution linkages program was established in 2003 – the Economic Cooperation Program (ECP) – which subsequently evolved into the Strongim Gavman Program (SGP).

Despite the actual positive change in the governance indicators evident from 2005, AusAID moved away from such forms of support (and although it was of course a government decision to change focus towards more direct forms of poverty alleviation, it was how this was being implemented that added to the issues). While working in PNG as Team Leader for the SGP staff secondment program between the Australian Treasury and PNG Treasury from 2011 to 2013, I often felt under attack by AusAID staff. There were constant requirements to demonstrate our “direct line of sight” to poverty reduction – a difficult job for any Treasury. The number of advisors were being cut back and key positions were being lost in areas such as our support and capacity building role for the PNG Budget and good macro-economic policy – areas vital for building the enabling environment for the private sector, growth, and long-term sustainable poverty reduction.

Fortunately, the current government's new approach to aid has reinstated much of the importance of governance programs:

“Governance affects virtually all aspects of a country's prosperity. An effective public sector and functioning, predictable institutions provide the foundations for economic growth, private sector investment and trade. Australia is supporting the building of institutions that have a direct role to play in promoting stability, inclusive economic growth and poverty reduction, and in strengthening gender equality and women's empowerment.” <http://dfat.gov.au/aid/topics/investment-priorities/effective-governance/Pages/effective-governance.aspx>

There is once again recognition that governance assistance helps build the environment that allows the private sector to grow. This goes beyond support for vital areas such as law and order – which are recognised as a major cost to doing business in PNG (yet alone all of the other consequences for freedom, including freedom from domestic violence). It extends to supporting macro-economic stability (fiscal, monetary and external), creating market frameworks that support inclusive businesses and trade, providing essential economic infrastructure and fostering entrepreneurial leadership.

3. Institutional linkages programs are the most effective way of providing governance assistance

Within the aid literature, there are extensive discussions about the effectiveness of advisors and capacity building activities. There is not agreement on a preferred approach. Part of the problem is that “technical assistance”, “advisor support” and “capacity building” can cover off a very wide range of activities. The approach being suggested in this paper is a more narrowly focused type of assistance, drawing on a reading of the literature, previous experience administering a range of advisor support programs as well as having been Team Leader in an institution strengthening project in PNG. The suggested approach is for a substantial re-invigoration and expansion of institutional linkages programs between PNG and Australia.

The following extract from Lynn Pieper's paper highlights the “how” is vitally important for governance activities:

“In most cases, the **areas of focus are correct, but implementation approaches are ineffective**. More often than not, consultants leave nothing behind, either because

they have been unable to encourage local commitment to following through, or because there is no consistency in the models, plans and approaches introduced. All interviewees describe advisers from earlier years being much more closely integrated and collegiate in their approach.”

An institutional linkages program aims to address a number of these deficiencies. For example, in the case of my experience based around an institutional linkages program between the two Treasuries over the last decade, there is a chance for greater continuity. My predecessor (and a position cut through the advisor review) did substantial work on the PNG Sovereign Wealth Fund. I continued this work as part of the PNG team. My successor is working currently on revised legislation due to be considered by the PNG Parliament next session. Through time, there is also a consistency of approach as there is a common reference point of how a “Treasury” should operate. Of course there are differences, and it is vital to understand different cultural elements. However, there are some common functions and requirements on Treasuries throughout the world that provide a basis for continuity.

As noted above, this type of program was picked up in a relatively small way through the Enhanced Cooperation Program (ECP) in 2003 – involving around nine central agencies in Australia seconding short and long-term staff, backed up by exchanges and other possible funding support. This was a relatively small part of the entire pattern of advisory support to PNG – in 2011, of the 487 advisors in PNG, around 38 were SGP. Through time, this form of institution strengthening moved away from supporting “in-line” positions towards a more challenging “capacity building” or “institution strengthening” focus. This was in part due to sensitivities of some of the policy work – and lessons were picked up through time on how it was usually best to let local staff do the final negotiations with Ministers on politically unpopular advice. There was also local resentment towards external advisors filling possible future career promotion possibilities, as well as an inevitable sense of nationalism (for example, in my time in the Australian Treasury, I would have felt very uncomfortable about having someone from the UK Treasury permanently seconded to “capacity build”). The new role was more challenging as the formal lines of authority no longer automatically linked positions into information flows and authority functions. With time and the crucial role of building relationships, most advisors were able to successfully adapt to the new challenges. For example, my wife’s ANZAC biscuits were a key to opening doors and building trust in the early days of the appointment – and as I draft this submission literally as the dawn rises on ANZAC day 2015 – there are nostalgic memories of the linkages³.

By definition, an institutional linkage program should transcend any particular individuals. As one advisor moves on, another will be available (although possibly in another role). In the case of the two Treasuries, there were frequent references to the breadth and length of the relationship built up over the last decade. There would be shared memories of people that had been in PNG, and were known to the new advisors. The short-term secondments back to the Australian Treasury were very highly valued – and were often to areas that included former long-term advisors. PNG staff would often remain in contact with advisors once they had returned to Australia. At more senior levels, there was sometimes comfort in knowing that one could pick up a phone and talk to a peer about common problems.

³ Indeed, I have considerable sympathy for the view that the battles fought in PNG such as Kokoda are as important as Gallipoli in defining our national character. Institutional linkages projects would do homage to the Fuzzy Wuzzy angels and carry the torch thrown to us from Flanders Fields.

Long-term institutional linkages mirror the long-term challenges facing PNG. They provide a basis for a strong partnership approach, building on our shared ties, history and common interests. The commitment must be long-term. The decline in the ability of the public sector to effectively deliver services arguably lasted from at least the late 1980s through to 2005. Rebuilding institutional capacities often take longer than the decline. As shown in Graph 1 above, PNG remains on average below the 30 percent ranking list for governance indicators – even relative to peers, there is scope for considerable improvement.

Institutional linkages activities can apply across the public, private, educational and community sectors. My experience most directly links to a public sector to public sector institutional linkages arrangement. However, as noted in other submissions, this type of activity can equally operate in other arenas. For example, the ANU's linkages with PNG's National Research Institute, University of PNG and Femili are examples of what is possible. There are many church programs that also have elements of institutional linkage arrangements. Various orders continue to provide support for their partners in PNG in a range of ways. Arguably, depending on the level of decentralised decision-making, many private firms operating branch offices in PNG (such as ANZ and Westpac) have many institution linkage elements.

A key ingredient for success appears to ensure the linkages are built with a similar organisation in Australia. This makes intuitive sense, but is also supported by some evaluation work. A 1998 AusAID "PNG Cluster Evaluation of three institutional strengthening projects" covered a problematic project with the Tax Office (with the contractor being a private sector accounting firm – Price Waterhouse Urwick), a much more successful project with the Bureau of Customs and Excise (where the contractor was the Australian Customs Service) and a successful Community Teachers' College Lecturers' Professional Development Project" (where the contractor was the Queensland University of Technology). These projects did not involve long-term institutional commitments – although the Customs to Customs linkages are now picked up through the SGP.

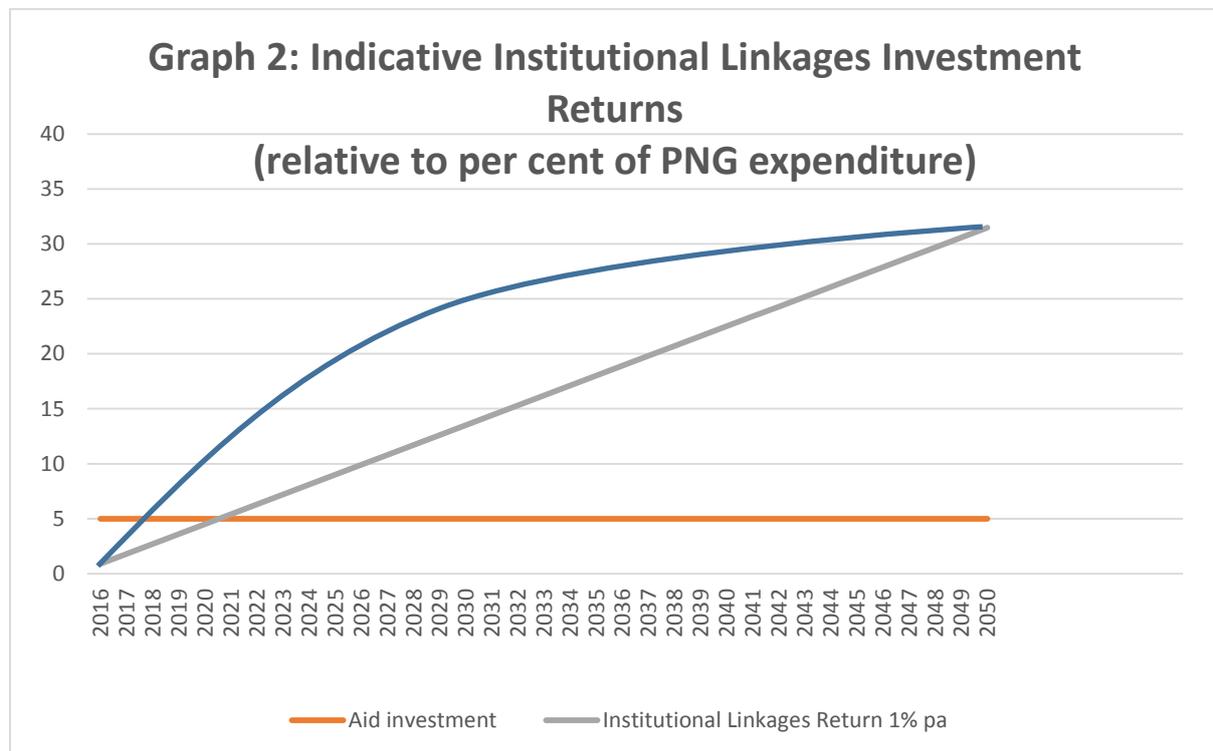
These institutional linkages programs must be adapted to specific challenges – and support local champions. There clearly is not one size that will fit all and contexts will change through the years. The underlying element of shared respect, common interests and values, and a commitment to maintain the relationship through time despite various individuals moving on should be common elements. There will be occasions where some relationships are thriving and could justify additional support, such as during times of significant reform. On other occasions, the role may be simply to support the institution while investing in building support for reform options if the political opportunity presents itself for local staff to take forward⁴. I agree with comments by Dr Tess Newton Cain from the Lowy institute on the governance policy blog above:

“state mechanisms can indeed be supported (by identifying and supporting normative champions who can then develop normative communities around them) through flexible, agile and nuanced activities grounded in meaningful relationships as nurtured over time – surely this is the key to ‘building on what’s there’”.

So if there is to be support for institution strengthening activities, how large should they be in Australia's aid program? As foreshadowed above, I would support a move over time for over half of our bilateral aid assistance to be delivered through such a mechanism.

⁴ And of course, this is what institutions in Australia often do. My role for six years in the Australian Treasury was head of the Strategic Tax Policy area – largely investing in building a critique of the tax system that would help provide the narrative for reform picked up by the Henry Tax review.

Devoting at least one half of bilateral aid to institutional linkages programs is arguably the best value for money that Australia can obtain. My view is that such expenditure can make an important difference at the margins of the effectiveness of PNG's own expenditure. If such assistance could help improve the effectiveness of PNG's own expenditure by even a conservative amount – say only a 1 per cent improvement each year, then this would represent very high returns from aid. Why is this so? 90 per cent of all public expenditure in PNG is funded by the PNG Government. A 1 per cent improvement in the effectiveness of such expenditure would represent an overall gain of around 0.9 per cent in the delivery of government services (including good policies in areas such as creating a better business and trade environment). Spending half of Australia's bilateral aid program represents around 5 per cent of PNG's current public expenditure. The following graph presents a simplified⁵ comparison of the costs and returns from such an undertaking. The institution linkages program is shown as rising to half of Australian bilateral aid, equivalent to 5% of public expenditure in PNG (it currently is arguably around 1-2 per cent). In the early years, these costs may well be higher than the conservatively estimated benefits of a 0.9 per cent annual gain in the effectiveness of PNG's own expenditures. However, over time, even with incremental improvements, the benefits will exceed the costs within a few years (six in the graph). The blue curved line suggests a more likely line where faster gains are made in the earlier years as the easier areas of reform are picked up. Within a decade, returns would be around double the aid costs and the overall gains would continue building. The real cost-benefit gains from such an approach is if the program is sustained over decades. As noted above, the decline in the effectiveness of PNG's public administration took arguably two decades. The task of rebuilding can be more difficult than the task of falling down.



⁵ The graph does not include the program design elements which would take one or two years. The pattern of change will also be far from smooth – and will depend greatly also on external circumstances and other factors. The base for the vertical axis is held as “unadjusted” expenditure – it is assumed that the gains will be in the effectiveness of expenditure or policies rather than increased expenditure.

Is a 1 per cent gain in effectiveness per annum possible or feasible? My view is that the figure is conservative, at least for a couple of decades. There is considerable scope for improvement and much of this is not in areas that are politically contested – the so-called “white space” of public policy and administration. Clearly, experience indicates that there are many challenges in building institutions. Often this involves change, and change can be hard. An overwhelming impression when working in the PNG bureaucracy is how many laws and procedures are left over from 1975. There is almost a “burden of 1975” of what would now be regarded as antiquated procedures. There have been dramatic improvements in areas of public administration, as well as public policy more generally. The upward move in governance indicators from 2005 (noted above) also suggests that gains may be faster than 1 per cent per annum (although I would not wish to over-state the reliability of the indicators as it is so difficult to measure governance quality). At some stage, other changes from within PNG could substitute for many elements of the program – especially if educational institutions are strengthened and the graduates can more readily adapt to modern institutions, including the requirement that they adapt and evolve. Through time, this could involve fewer long-term advisors in the mixture of an institutional support program, and more specific assistance as well as peer support (hopefully mutual).

The gains implied by the graph are related to a notion of a 1 per cent gain in the effectiveness of PNG's own expenditure. This is most easily thought of as increased abilities to design, select and effectively tender for priority economic infrastructure, or for better universities, or for better delivery of health services. Some of the largest potential gains are, however, more from improvements in the policy settings vital for PNG's development. Examples are provided below of potential gains in the area of supporting the policy environment for the private sector, as well an anecdote of how even one policy gain was larger than the entire Australian aid program.

One possible concern with such an approach is whether this would simply be seen as a form of “boomerang aid” by PNG, or something that doesn't give adequate acknowledgement of PNG's independence. Comments have been made that PNG does not want more advisors and technical assistance. For me, these issues are in part related to who is asked and how they are asked. For example, obviously there were some influential players that were opposed to the immunities initially provided to the Australian police under the ECP. Realistically, PNG has not changed the constitutional impediments to such a presence. However, when talking to people in PNG, especially those familiar with the changes that seemed to start occurring with Australian police “walking the beat” with their PNG counter-parts, is the sense that a return of such assistance would be greatly appreciated. Senior public servants are more likely to appreciate the role of advisors than Ministers – there are understandable issues of national pride noted above. However, Australia has also conveniently side-stepped requests for such assistance. Headlines in PNG's main newspapers after one set of PNG Australia Ministerial talks was about “Kiaps return”, with generally very favourable comment about such an agreement. This was consistent with messaging that PNG Ministers wanted Australia to support its moves towards decentralisation with increased advisory support. These requests were side-stepped and adapted. This story is not suggesting that “Kiaps return” is the right policy – just that sometimes requests for more Australian advisors have been made but these were not convenient for the aid paradigm at the time. An “institutional linkages” program will indeed be subject to the criticism of “boomerang aid”. If the context was a growing aid budget then the large increase could have been presented as an additional element to top up and re-inforce the existing program. However, given the current regrettable budgetary context, the concerns could in part be countered by arguing that the gains for such assistance in improving the effectiveness of PNG's own resources being spent within PNG are significantly greater than the “boomerang” element. The linkages program should also typically involve secondments of PNG staff to agencies in Australia as

well as selective institutional funding (for example, information records systems). Politically, it may also need to include an acknowledgement that such assistance is being provided in part as Australia did not fully perform in its preparations of PNG for independence – for example, the situation may be different if more PNG nationals had been able to graduate from universities long before independence.

A clear opportunity exists through institution strengthening programs to improve the private sector environment. PNG performs poorly on one of the most comprehensive measures of a conducive environment for supporting the private sector – the “Doing Business” indicators prepared by the World Bank⁶. Of the 189 countries surveyed, PNG ranks 133rd – two places worse than last year. Given the importance of creating an environment to support contracts for the private sector to thrive, it is especially concerning to see that PNG rates 181st on the “enforcing contracts” criterion. The poor performance on “Getting credit” would inevitably adversely impact on small business creation – a situation reinforced by the low ranking on “Starting a Business”.

Looking into the basis of the indicators (which can be done through the website link below), the types of measures suggest administrative and legislative actions that often should be very doable. This should be a clear area for examining a program based on several institutions (such as ASIC), including some where the responsibilities sit at the state level.

TOPICS	DB 2015 Rank	DB 2014 Rank	Change in Rank
			↓
Starting a Business	130	122	-8
			↓
Dealing with Construction Permits	141	139	-2
			↑
Getting Electricity	26	27	1
Registering Property	85	85	No change
			↓
Getting Credit	165	163	-2
			↓
Protecting Minority Investors	94	91	-3
			↓
Paying Taxes	110	108	-2
			↓
Trading Across Borders	138	136	-2
Enforcing Contracts	181	181	No change
			↓
Resolving Insolvency	141	140	-1
			↓
Overall	133	131	-2

⁶ Once again, there are critics of these indicators which are available at <http://www.doingbusiness.org/>, but they are at least an attempt at quantifiable measurement and provide, at least to some extent, an ability to track performance through time. My broad view is that the indicators are adequate for PNG, although there are possibly more issues with them in the context of other Pacific countries.

Australia still has much to learn about how most effectively to support such programs. My personal experience in the SGP was often one of frustration about the declining support for such programs, both at post and from Canberra (off-set by strong support within the PNG Treasury). The central agency commitment to such a partnership arrangement had dropped off in the decade since the urgency of interventions around Timor Leste and the Solomon Islands. Such activities will not be successful unless there is a reinvigoration of that central agency support – and this must extend well beyond DFAT. A series of chosen institutions in Australia need to acknowledge that such an institutional linkages program will be part of their core business. This will need to be sustained through decades. Even within the Australian Treasury, after the best will in the world, there were debates about whether such work was “core business”. Despite specific additional funding for such work (enough for a Pacific Division in Treasury), competing demands at the time of the Global Financial Crisis and a lack of other resources meant that previously additional and ear-marked budgets for institutional linkages in the region were essentially pocketed. There is also a need for better training and support for officers that might be strong on technical skills, but less experienced in capacity building. Indeed, some of the advisors sent across were arguably not suitable for the capacity building role. The importance of language skills has also been underestimated – stronger skills in Tok Pisin English can help significantly with building relationships and being part of the team even in offices where all formal communication is in formal English. Security arrangements are important and may become an increasing issue. My view is that the security situation can be managed, but it takes resources and time, and there is inevitably a tail-end of risks. My predecessor had to deal with some 11 car jackings within his team of 7 advisors – one including a stabbing. Fortunately, during my time as Team Leader, the security arrangements were strengthened including through the option of having security escort vehicles. Even then, there was one close incident (which could have been fatal) and one very experienced former advisor who was still in-country (his spouse was still working in PNG) sustained a machete wound to his leg. Appropriate remuneration arrangements will be vital – in a world of demand and supply, it is interesting that there are significant problems in attracting SES officers to take a position in PNG (and for institutional linkages programs, experienced managerial staff will be a vital component). In my situation, there was a financial gain of slightly less than 10 per cent per annum in our combined incomes from taking the secondment arrangement after including all allowances (both cash and in-kind), the tax-free status (which should be removed including for NGOs) and the loss of my partner's income. On purely financial considerations, monetary gain was not sufficient to compensate for the loss of security, restrictions on lifestyle, OH&S issues in the office, distance from family, and health issues (partial loss of hearing for me from a tropical infection, a serious tropical illness for my wife). Rather, it was my long-term interest in working in PNG and a sense of adventure that drove the decision. Although the position was advertised nationally, no one apart from myself applied. We found an able successor to myself, but he was not from the Australian Treasury. There will be required changes to attract senior staff – most of these probably will be non-financial and relate to issues such as employment opportunities for spouses and impacts of a secondment to PNG for one's career. Comparing the SPG package with those available to staff at post, my strong preference would have been on the full package that posted officers at the same level obtained. However, people going to PNG will need to understand that it is a demanding environment, and if motivated only by financial gain, they will be unhappy and not be the people such a program should be looking for. With all of that said, as an economist, a price will need to be found to match supply with demand. So, for example, although the tax-free status should be removed, this will need to be fully compensated for in other ways. Management could also be explored through improving incentives for integration (such as having local institutions pay the equivalent local cost of a position) and clarification of reporting arrangements between the local institution and Australia.

Measurement and performance indicators are particularly challenging for reasons of both the lack of short-term quantifiable measurement indicators but also secrecy. Choosing to focus on institution strengthening will make work on performance indicators harder as this is an area where there are very real difficulties in attributing outcomes to inputs associated with governance. For example, how to we measure the effectiveness of the Australian Treasury? How effective was the Henry Tax Review especially if we remember there was a timeframe of several decades for possible implementation – similar to the Asprey Committee's 1975 recommendations to introduce a broad based consumption tax (failed in 1985 and finally done with the GST in 1999). There is commentary about the dangers of measurement, and how this can distort the most important actions for development. In a March 23 2015 response to an article by Bob McMullan that touched on the issue of the "tyranny of the measurable", I commented:

"The 'tyranny of the measurable' is indeed a dilemma for someone such as myself who also applauds the virtues of evidence-based policy decision making. Good public policy and governance should be driven by evidence, and hard numbers tend to drive out "soft" information. Joel highlights how this may affect education sector funding relative to health funding. This is even more the case for governance activities. These are very difficult to measure – although the World Bank at least makes an effort through its support for worldwide governance indicators. Time scales are very long – well beyond a usual election cycle, especially if trying to measure sustainable reform. In addition, there are real differences as to what is regarded as a success in the governance sector (for example, whether creating statutory authorities in PNG for immigration and taxation is a positive governance outcome or not). A third issue in the 'tyranny of the measurable' is that even when there is information on "measurable wins", it often cannot be released in public. Some of the best contributions from advisers working in the governance sector cannot be revealed as they could break the secrecy provisions of another sovereign country (this would be the same issue for any foreign adviser working in Australia on issues that went to the Australian Cabinet)."

More specifically, when doing a cost benefit analysis of an activity which was more "quantifiable" involving advisors in the PNG Treasury, the net benefits exceeded in present value terms the entire Australian aid program to PNG for a single year. So the rate of return from simply one part of one institutional linkages program exceeded the entire amount of bilateral aid that year. This was clearly a good news story and one that is relevant for Australian taxpayers knowing that their scarce dollars were being spent effectively. However, when asked for details, I indicated that I could not provide them due to secrecy provisions around the work that had been done. Additionally, most outcomes from institutional activities involve a team involving advisors, and it is difficult to apportion outcomes. If Australian advisors claimed credit for specific outcomes, this would undermine the team approach essential for much policy work, and thereby undermine the objectives of the actual assistance. For institutional linkages activities, there is no simple solution to the "tyranny of the measurable".

4. Australia can also contribute to building institutions through high level policy dialogue, sharing lessons from its own past, especially in the area of supporting the private sector.

This Committee's focus is on Australia's bilateral aid program. Of course, Australia's relationship with PNG is much more diverse, and there can be significant synergies between elements of the relationship (as recognised by the new treaty). In building support for PNG's sustainable economic growth, with strong support for the private sector including aid-trade elements, Australia will

inevitably have to take a holistic approach. This also includes using various mechanisms to support appropriate macro-economic settings vital for development, including of the private sector. In an earlier submission to the JCFADT inquiry on "The role of the private sector in promoting economic growth and reducing poverty in the Indo-Pacific region" (submission 153 included at Appendix 2 for ease of reference), four support options were suggested:

1. Utilise multi-lateral opportunities for peer based reviews of macro-economic policies such as provided by the IMF and their annual Article IV discussions. This should also include other multilateral and regional opportunities, including regional trade negotiations as well as meetings such as the Forum.
2. On a bilateral policy dialogue level, we should ensure that such macro-economic issues feature in high level policy dialogues and relationships, including Ministerial discussions.
3. At a more indirect level, we should strengthen PNG's capacity to analyse its own economic performance, formulate good policies and implement actions. This includes building future capacities for more rigorous analysis.
4. On occasions, and these would be in more unusual circumstances, the appropriate utilisation of Australian laws could be a useful adjunct to other actions (examples were provided on use of anti-money laundering rules and foreign investment rules).

The third component is the one that dovetails most closely with the bilateral aid program, and the suggested approach towards support for institutional linkage activities. The institutional linkages programs either in place or commencing, such as an expanded SGP and the new Governance Precinct at the UPNG, would be effective ways to take forward this indirect type of support for good macro-economic policies. There are many options worthy of consideration, including linkages with the RBA, Productivity Commission and the Grants Commission. However, the other three elements are important, and should be supported through bilateral aid where there are possible connections.

Appendix 1

**DETERIORATION OF PUBLIC
ADMINISTRATION
IN PAPUA NEW GUINEA -
VIEWS OF EMINENT PUBLIC SERVANTS**

July 2004

**Report prepared for AusAID
By Lynn Pieper**

DISCLAIMER: The views expressed in this paper are those of the author and should not be attributed to AusAID, the Australian Government, or any other organisation with which the author is affiliated.

Appendix 1

TABLE OF CONTENTS

Introduction	1
The good years – what made them so?	1
Changing dynamics	2
Some pivotal decisions	3
Early opportunities to arrest the decline?	5
The role of donors	6
Public administration in PNG today	6
Where to now?	6
The future focus of aid	10
Views on PNG's outlook	10

Appendix 1

INTRODUCTION

This paper presents the personal views of eminent former or long-standing Papua New Guinean senior public servants on the deterioration of public administration in Papua New Guinea (PNG). Whilst there is a wealth of reports on this topic produced by academics or consultants, there is limited information documented on the views of Papua New Guinea's own experts in this area. Yet it is now well recognised that, without a high degree of sustained local commitment and ownership, most externally-driven initiatives to reform public administration in PNG have limited impact. This paper is an initial step in helping Australia develop a deeper understanding of what Papua New Guineans themselves consider to be the key issues influencing public sector performance and the priority areas needing reform.

In-depth, one-on-one interviews were held with a number of eminent former or long-standing PNG senior public servants during March 2004, which allowed for free-ranging discussion of issues they themselves believed to be of most importance. Interview questions were deliberately broad, focused on obtaining their views on the *quality* of public administration in PNG through the years since independence, the *degree* of deterioration and *prospects* for redressing current problems, main *causes* of deterioration of public administration, key *decisions* or *actions* needed to restore effective public administration, and the role of *donors* (either in contributing to the problems or assisting with solutions). This report attempts to synthesise the views and ideas of those interviewed, without interpretive comment.

THE GOOD YEARS – WHAT MADE THEM SO?

There was consensus amongst all those interviewed that public administration in PNG was excellent until the early 1980s.

Everyone shared a common agenda. People were energised, prepared, and completely focused on doing what was right for the country. There was a strong nationalistic drive in PNG to be independent of colonial powers and to run its own affairs as a country.

There was robust and frequent debate amongst and between senior public servants, Politicians, political advisers and senior public servants disagreed on many things, but shared the common goal of building a strong country, so there was openness to debate, and debate was frequent, robust and constructive. Also, because politicians and bureaucrats worked closely together, Ministers and departmental heads always presented a consensus view publicly, so there was no confusion in the community.

There was strong, centralised control of monetary and fiscal policy. Sector budgets were closely coordinated, and institutional, budgeting and public administrative systems all functioned well.

Senior public servants were generally better educated than politicians. This meant politicians, most of whom were young, relied on the advice of public servants, and did not interfere in decision-making relating to public sector management. The onus on public servants to brief their ministers well was strong.

Appendix 1

“Teamwork was the name of the game” amongst senior public servants, within and across departments, and through to provincial administrations. This strengthened the ability of the public service to process policies through to implementation. It also established institutional knowledge amongst senior managers, not only of their own organisation but of the entire system of government administration through to the community level. The benefits of consultation for cohesive policy were visible.

The public service was independent and professional. Public servants had job security and personnel were unaffected by politics. ***There were proper checks and balances*** in the system, and they were adhered to. In relation to performance management, for instance, the challenge of trying to be better than or equal to work colleagues meant people worked hard and strove to improve. Promotions were merit-based. On the flip side, penalties such as demotion, pay cuts, or dismissal were applied when staff did not meet expectations. ***The Public Services Commission (PSC) was powerful*** (the commissioners were known as “the three gods”), independent of politics, and fundamental to the charter of the public service.

Public servants were well trained, dedicated and closely in touch with basic service needs in provinces. Although transport facilities were far more limited than today, public servants got out of Port Moresby far more frequently, and worked closely with counterparts in provincial and local level government departments. At a central level too, departments worked much more closely with each other.⁷ Public servants had a strong sense of community service obligation which generally promoted community participation in development activities in local communities (as opposed to the handout mentality that is prevalent these days).

There was a dynamic team of young and committed expatriates, who were not in PNG for financial reasons, but for the challenge of helping an emerging nation.

Sir John Crawford at the time (1977) commented that PNG was running the country so well on all fronts that he could see nowhere it could go except down.

CHANGING DYNAMICS

Even during the early post-independence period, interviewees point to certain dynamics which, over time, contributed to increasing politicisation and gradual weakening of both the management and operations of the public sector in PNG. From the mid-1980s, the dynamics in favour of poor administration took much stronger hold.

There was a move away from traditional bureaucratic procedures. The move, post-independence, to “de-neutralise” public servants was an attempt to hasten change, as required by the independent constitutional review. The ethos and modus operandi of the Australian model for public administration were thought to be too heavily rules and procedures driven and not commensurate with PNG’s needs for public administration at the time.

⁷ One example given was the practice during the late 1970s of joint teams (Department of Finance, National Planning Office and Department of Provincial Affairs) visiting every province to conduct training programs in budgetary planning and financial management. This training was followed up with quarterly visits, again by joint teams, to work through any problems with provincial staff. Over time, those that were competent were given autonomy, or “full financial responsibility”. Others continued to receive quarterly on-the-job training and support from national level teams.

Appendix 1

A cadre of political advisers was put in place to provide alternative advice to that being given by the “old guard” of Australian-trained public servants. At the time, there were many highly competent people around, and this was seen as a desirable move - both to strengthen the competency of political leaders and to promote contestability. But over time it led to “all sorts of pseudo advisers coming out of the woodwork to influence Ministers” – one interviewee referred to these as “UFOs”.

The lines between politics and administration began to blur. There was an increasing feeling amongst politicians that the bureaucracy was too powerful and independent, and not astute to political needs. Although most politicians had little or no experience in public policy or organisation management, by the mid-1980s they were generally much better educated, and a belief grew that they “knew it all” and did not need to rely on the advice of public servants. Public resources increasingly became controlled by politics rather than public policy, and politicians began involving themselves in administration, project management, and senior appointments.

Within the public service itself, *professionalism and ethics were eroded* over time. Young and highly qualified graduates also felt they “knew it all”, wanting to be at the top without learning about the procedures and systems. The localisation program allowed this; it was easy to be promoted without sufficient skill levels during the 1980s. Later in senior management positions these people were ill-equipped to guide professional practices. Today, many public servants have had no exposure at all to “the old work ethic”, and believe current flawed practices - be they corrupt, inefficient, or unprofessional - to be the norm. Some are playing politics for personal gain; some for survival; and others because they know no different.

“Why do people criss-cross? *Self interest* drives much of it.” When combined with the continuing long-standing pressures of PNG’s wantok system, the trends toward cronyism and political interference in public administration meant newer breeds of politician or public servant were quickly absorbed into a “Me first, country second” approach to their roles, a trend which has yet to be arrested.

Expatriate personnel were in contracted, line positions, subject to normal lines of command, discipline, and public service ethics. *The shift to off-line, advisory support* during the 1980s, whilst a well-intentioned part of the localisation process, “was a step backwards” in the opinion of interviewees. Apart from being much more expensive, it has created a feeling of condescension between ‘advisers’ and their ‘counterparts’; reduced sustainability prospects by separating the work done by advisers from the ‘normal’ work of departments; created a dependency by Departmental Heads on using advisers to fix problems rather than training nationals to learn the job by doing it; destroyed the collegiate sense that previously existed (“we used to work and socialise together”); and eroded any sense of pride in achievements – counterparts do not have any sense of ownership of results, and advisers today “are not long term stayers”.

SOME PIVOTAL DECISIONS

There were also certain key policy decisions, taken in good faith at the time, which eroded the checks and balances in PNG’s public administration system and opened the door to corruption. Interestingly, all those interviewed point to the same decisions and events as having been pivotal.

Appendix 1

Control of sectoral budgets. By the early 1980s, certain line agencies (eg: education) were very well managed and obviously competent to control their own budgets. A sense of resentment over the tight central control and coordination of financial matters was developing in these agencies, a view with which the central controllers - the “Gang of Four”⁸ - had some sympathy. Plans were underway to give a greater degree of control to those agencies able to manage their sectoral budgets, and “sector funds” were being trialled. At this time, the Deputy Prime Minister and Minister for Transport argued that the transport sector budget was his to control. He axed the National Public Expenditure Plan, and took over decision making on allocations within the infrastructure budget. Agriculture then followed. This was the first real move to political control of public sector management, and to using public funds as slush funds. It was also the first step towards bad public administration.

Control of senior public service positions. By the mid-late 1980s, it became fashionable to introduce private sector culture into public services. In PNG, this trend coincided with the growing desire of politicians to control public resources. The powers of the PSC were reduced dramatically, senior public service positions became contract rather than permanent appointments, and departmental head appointments were made by Cabinet, rather than the PSC. In theory, the intention was to strengthen the role of departmental heads. In practice, the result has been that Secretaries (and often other senior personnel) change whenever a new Minister is appointed. This has seriously undermined the professionalism of the public service, causing departmental heads to focus only on the short-term, and to play political games in their own attempts at survival. It has also enabled politicians to get too close to operational areas within the public service.

Decentralisation – the 1995 Organic Law. Interviewees consider PNG’s three-tier system of government is not functioning as intended. Although intended to clarify the system, the 1995 revisions to the Organic Law added to the problems.⁹ PNG is now “over-governed”, and the system itself is hampering effective service delivery. All layers - of government, public sector institutions, and decision-making - are disaggregated and unfocused. Provincial governments have been unable to meet the expectations of them, and local governments have not been empowered. The end result is that significant funds are tied up in administration rather than development, services are not being delivered, and the gap between government and people is widening, not closing. Further, priority setting differs at national and provincial levels, so priorities cannot be reflected in a unitary way.

Adding to these complexities, resource needs calculated for provincial and local level governments in 1998 were never honoured by the national government. According to interviewees, the major problem was that the funding formula under the Organic Law reflected political expediency rather than economic reality. Grants were calculated on the basis on population and land mass; provinces had not been paid the full grants since 1995 when the Organic law was passed.

⁸ Sir Mekere Morauta (Treasury/Finance), Sir Rabbie Namaliu (Foreign Affairs), Sir Anthony Siaguru (Public Services Commission), and Mr Charles Lepani (Planning).

⁹ As an example, over 100 pieces of enabling legislation were needed to implement the 1995 Organic Law, which were not in place when the Law came into effect. These were still being worked through at the time of writing. In the meantime, confusion over the roles of agencies at different levels of government means service delivery is declining rather than improving. For example, the national government pays for the staff of provincial radio stations, but allocates nothing for goods and services funding on the assumption that provincial governments will fund these.

Appendix 1

Demand for government services increased and the public service machinery could not effectively deliver. Politicians, being concerned with survival, had to devise other delivery systems by taking greater control of the funding allocation to provinces. Thereafter, development grants were added to the funds of members of parliament, who now determine what funding goes where, and this may or may not match district priorities. In any case, interviewees argue that PNG's systems cannot support this many layers and institutions. PNG is now "over-democratised" and its problems have become multi-faceted.

The pace of localisation removed the foundation that had underpinned effective public administration in PNG. Significant expertise was lost from critical positions and, over time, as less experienced people took over key positions, productivity declined, inefficiencies took root, and the demand for service delivery forced the public service to grow in size - more people were needed to do the same jobs that had previously been done by a few. Nobody looked at the affordability of rapid recruitment at the time. Five to ten years later, it became clear that the rate of growth of the public service had outstripped PNG's economic capacity.

Embracing globalisation added to the pressures confronting PNG at about this time. PNG had to adhere to international commitments on various global issues such as the environment, trade, commerce, and economic performance, which not only placed additional pressure on the Government and the public service to meet those obligations, but at times also diverted attention from core domestic problems.

EARLY OPPORTUNITIES TO ARREST THE DECLINE?

One interviewee suggested it is wrong for critics to be too severe in their indictment of PNG's performance. At the time (through the 1980s), nobody said "hold on, we are heading in the wrong direction". Whilst there had been some clear examples of deliberate mismanagement or poor decision making, he felt much of the country's current situation could be attributed to missed opportunities, unforeseen disasters, and voluminous resource flows.

The *Leadership Code II* was an attempt to focus political leaders on sound management of the country. Prior to this, politicians had been required to declare any personal business interests; the new code required them to sell off those interests. It was disagreement over this new Code that led to the first major break in the Somare/Chan coalition in the early 1980s.

The degree of *instability in tenure* since the early 1990s (for both politicians and senior public servants) has made finding solutions to PNG's problems more difficult, even where they were recognised early. Although leaders under the Leadership Code II must forfeit any business interests, the likelihood that they will last more than 18 months (if elected at all given the proliferation of parties) makes many potential leaders reluctant to leave the private sector. Likewise, the shift to politically-controlled, contract appointment of departmental heads from the late 1980s has seriously limited the capacity to arrest deterioration of public administration. Since then, Secretaries have reportedly served on average only 12-18 months before losing their positions. Since they must be the champions of change within the public service, and cultural/attitudinal change takes time, even the best of them have been able to achieve little. According to one interviewee, this degree of instability now means PNG will never attract good public servants back from the private sector, even though such mobility may be desirable.

Appendix 1

THE ROLE OF DONORS

According to interviewees, the demise of public administration in PNG was largely self-inflicted. On the justifiable assumption that the sovereign government did concern itself with development, donors supported government priorities, whether rightly or wrongly. In PNG however, one can see with hindsight that, whilst government concerned itself with development in social sectors to some extent, little attention was paid to managing economic growth. At the time Australian budget support ceased, despite the fact that it was phased out over several years, PNG was not adequately prepared to be able to finance the gap, and lost the flexibility to fund priority programs. Budget support had allowed PNG to adopt a sense of complacency about the affordability of public sector salaries and programs and, by the time it ceased, the problem was already too large.

PNG did not reprioritise development expenditures, continuing to spend as it always had, and introducing “band-aid solutions” whenever problems emerged. Strategic development planning was never considered as a critical vehicle to guide long-term development and, as a consequence, the main focus was on annual planning, because this provided the means for political expediency. Then, from 1998, in response to World Bank reluctance to approve a second structural adjustment loan to finance PNG’s budget shortfall unless certain conflicts of interest were first addressed, PNG instead sought to find commercial loans and tried to launch an international bond float. “Forced” to borrow from the Central Bank, PNG further increased its excessive debt burden.

PUBLIC ADMINISTRATION IN PNG TODAY

As one interviewee put it, the failure to arrest deterioration of public administration has been “a matter of momentum”. The public service today is characterised by “muted frustration”. Its *independence and professionalism have been eroded*. Politics has usurped and devalued the fundamental role of public administrators - providing good technical advice to Ministers. The blurring of roles between politics and bureaucracy has derailed national and sectoral policies, led to gross inefficiencies, and left a demoralised and insecure public service. People do not see it being in their interest to change the nature of PNG politics, and the bureaucracy feels powerless. As one interviewee put it, “being a departmental head in this country is a nightmare”.

Within departments, *lines of authority and discipline have collapsed*, due to frequent changes in leadership, lack of direction on priorities, and an increasing lack of accountability and transparency in the public administration system. As these systems have broken down, service delivery has been adversely affected, and qualities such as honesty, trust, dedication, and the spirit of working together industriously have disappeared. The ethics of public service are no longer upheld. Another consequence has been a breaking down of nationalistic commitment within the public service. Personnel tend to be consider their province first, and region second.

WHERE TO NOW?

Although “*the constitution needs a major overhaul*” to address both political and policy dilemmas, most interviewees believe the failure to address these seriously to date is to some extent a resource problem rather than a lack of will. In their view, government

Appendix 1

interventions/initiatives introduced by the 2002 Somare Government and preceding Morauta Government are starting to have impact, but it is too early to see visible results as yet. The emphasis on fire-fighting means there are pockets of impact, but there is still no integrated focus to the reform efforts. The key for PNG lies in assuring the integrity of key institutions, maintaining consistency, and working to approved plans. Most of the legislation, policies and systems already in place are good. But they are only as good as the people who work the systems. PNG's problems are more to do with implementation than with policy. At the same time, before more effective approaches can be put in place and implemented, decision-makers need to reach consensus on what they want to achieve. In essence, the decision to be made is whether they want what is best for the country in the long term or what is best for individuals in the short term. Following are the issues that interviewees feel are of highest priority for PNG looking forward.

Reform PNG's political system to reduce the constant political changes. "PNG is a funny place and will always have coalition governments". Nevertheless, some greater degree of stability could be achieved, for instance by reducing the frequency of allowable no-confidence motions in parliament and by supporting political parties to maintain some degree of coherence.

Re-establish clear and independent roles of politics and the public service. To a large extent, this simply involves abiding by existing legal and constitutional requirements. But inappropriate practices are now so deeply ingrained that the issue is far from simple. First and foremost, strong direction is needed from Executive Government that the role of politicians is as legislated. Thereafter, administrative bodies must enforce rules, procedures and discipline, requiring compliance and not allowing or tolerating shortcuts. Whilst at first glance this may sound somewhat rigid, the increased role clarity and administrative efficiency would be expected to help instil a more positive work ethic throughout the public administration system in PNG. For instance, if people were assured of being paid, they may see some point to turning up at work. If they knew promotions were truly merit-based, they may have an incentive to perform. There is no short-term solution, because much depends on changing peoples' attitudes and, in PNG now, the "smorgasbord of cultural, work, and political values" makes it difficult to get back to a clear focus on service delivery. **The solution lies in strong leadership.** Leaders must not only give clear directions, but must drive the process to ensure action follows – and they must resource the administration appropriately to ensure it can.

In the first instance, PNG needs to "go back to the old PSC model". **Management of the entire public service should be housed with the PSC**, including appointments, transfers, dismissals, selection and performance criteria, and discipline. Departmental heads should revert to being permanent appointments, ideally with no selections referred to Cabinet for approval. If this is unrealistic, then providing a transparent shortlist of three candidates to Cabinet may be adequate. Recent changes aimed at empowering the PSC are a good step, but further reform is needed before true independence can be re-established. For instance, the PSC and DPM should be combined as one, independent constitutional office, as in the past, so that all personnel management matters can be protected from political interference. Also, the tendency for political suspension of departmental heads needs to be addressed.

As part of its reform program, the government is undertaking a major public service reform program with the intention of **refocusing the government on its core functions and re-establishing accountable, transparent governance systems and processes.** The program is

Appendix 1

still fragile and, while this government has put its weight behind it, the test will be to back it with real sustained support. Donors can play an effective supporting role in re-establishing systems and processes.

Put communities first. Both government and donors need to pay more attention to ensuring their programs actually mesh with local community priorities and capacity. These will vary from one community to the next, and a one-size-fits-all approach leads to “big white elephants” with unforeseen ongoing costs within communities. Funding should only be provided for priorities identified in local community development plans. Programs must be tailored to local capacity, and accountability requirements must appreciate local conditions. A requirement for three quotes from local contractors for a small community project on an isolated island, for example, “is sheer madness”.

Seriously address decentralisation (aspirations and current flaws) in the context of affordability and responsible public expenditure management. As one interviewee pointed out, lack of resources is not the issue. PNG has enough money; it is simply not spending in the right areas. The policy may be about decentralisation, but the reality is that more and more is centralised. “Waigani has ballooned.” Similarly, the mismatch between district priorities and the priorities of the members of parliament who control development funding needs to be addressed. ***The solution depends on political reform as much as on financial and administrative reforms.*** Between 1975 and 1995, various working groups looked at the technical and administrative issues associated with decentralisation; reports were debated; and a bipartisan committee of the National Parliament was formed. Yet today, with funding tight, PNG again finds itself at a crossroad - it cannot resource provincial and local governments properly.

Strengthen PNG's accountability institutions (Attorney General, Auditor General, Ombudsman, Judiciary, etc) so that they can and do “investigate and charge leaders”. These institutions are well respected in the community, having by and large withstood political pressures over the years, but they need to be supported.

Address and resolve fiscal problems. According to one interviewee, this first requires examining the actual performance of political leaders, the administration, and other agencies of the State (where and why performance has deteriorated, and strategies for improving it), at all levels of government. This will determine how resources are being spent, identify the real cost of services, and indicate areas that could be cut. In other words, ***the question of affordability should be considered after performance has been addressed.***

Strengthen central agencies and the Central Agencies Coordinating Committee (CACC). “National coordinating agencies have become defunct.” Some are highly politicised now; others simply won't deal with each other, and do not feel compelled to. Political control of appointment and dismissal of senior public servants has devalued incentives related to effective public administration, instead rewarding individual political profile and competition amongst central agencies for political favour. “If you coordinate, your own effect is blunted; you can't score points with politicians as easily or as quickly. Making the choice to share power is a part of the ethics of good management and leadership”. The CACC, established during Morauta's term, was intended as a means of reactivating the old *Budget Priorities*

Appendix 1

*Committee*¹⁰, which had assured the integrity and coordination of departmental proposals. Most interviewees remain optimistic about the CACC's potential to coordinate (or force) a shift back to responsible public administration, but they all agree that this initiative is only half working at this point in time. The CACC at present must make a separate submission to Cabinet on departmental proposals, and it has too many sector interests represented, which influence and skew budget decisions. It is also under-resourced, with little time to "ponder big issues". Other central agencies, such as Treasury/Finance, DPM, PSC and the Auditor General's Office also need to be resourced adequately to allow them to monitor and strengthen public sector performance agreements, strategic plans, financial management, budget planning, and so forth. Weak coordinating agencies leave line agencies exposed to direct political interference.

Establish a clear working relationship with donors. Interviewees feel strongly that donors continue to have an important role to play in PNG's development, but that the ball is in PNG's court to give donors a clear mandate on *where* they can help. As they see it, "donors are not there to solve our problems. They are there to help *us* solve our problems. If we don't have our house in order, donors become hesitant to support us." There is "a culture of denial" amongst some in PNG politics. They do not believe there is a problem and, in any case, do not want foreigners involved at all. All those interviewed, however, feel it is critical for PNG to "take advice from anyone, treat donors as resources, and stop denying ourselves access to advice." They argue PNG does not have the capacity or the resources to fix the system themselves, and must accept help.

Reinstate a structured and targeted public service training program. Until the mid-1980s, a coherent program of training for public servants was provided by the Administrative College (ADCOL), later the Institute of Public Affairs (IPA). This coherence was lost over time, initially when IPA sought to reinvent itself as an academic institution and was opened up to offer training to the private as well as public sector ("its relevance fizzled"), and then when a user pays system was introduced¹¹ and departments were given the freedom to source training from anywhere. Today, there is no institutionalised or enforced system for induction courses, middle management or senior executive training programs, or other administrative skills training requirements which must be completed prior to obtaining promotions. As a result, public servants are no longer fitted into an organisational culture from the outset, they have little or no exposure to public service ethics, and they learn in an ad hoc way as they go.

Efforts to revitalise the public service through training in the past have focused on the wrong things, such as scholarships and IPA infrastructure. Future support must ***target skills development at a working level***, through on-the-job training and mentoring rather than expensive formal courses. The strategy of sending people to complete Masters degrees, for example, needs rethinking. There are many Masters degree-qualified public servants today, yet productivity, efficiency and management ability continue to decline. Even the best-qualified people cannot effect change in a system so broken. The focus now needs to be on

¹⁰ The Budget Priorities Committee was chaired by the Treasury Secretary, who sat in Cabinet during deliberations. The Committee included Secretaries of the PSC, Foreign Affairs and Planning and, on occasion, involved the Attorney General. No department could put any proposal to Cabinet without going through this Committee. This ensured proposals were not approved without first obtaining support from Treasury/Finance (that funds would be available) and the PSC (that personnel and other necessary resources would be available). When this committee was dissolved, both Planning and DPM suffered, losing their link with the budget.

¹¹ As departmental resources have become more constrained over the years, training budgets have been cut. As a result, many departments stopped using IPA to conduct training.

Appendix 1

developing strong leadership and management skills so that the system as a whole can be improved.

THE FUTURE FOCUS OF AID

Restructure donor support to focus on a few clear priorities. Australia in particular is at risk of trying to do too much, thus diluting the results it achieves.¹² When results are not tangible, claims of 'boomerang aid' can surface. According to interviewees, donors need to focus on building goodwill by delivering results. They encourage donor partners to maintain their focus on helping PNG improve **governance**, in particular rehabilitation of the public service, as this is fundamental to effective delivery of basic services. Interviewees argue that **structural adjustment** is necessary, but will only succeed if PNG itself controls the process, resources it, and manages any donor support. The volume of donor funding available to PNG in the past has meant people did not need to look within for solutions. Thus they have never had any imperative to prioritise effectively.

Donor assistance also needs to be restructured to **focus on really rebuilding the capacity of the public service**. At present, "There are pockets of brilliance but the engine is not humming." Key precursors for achieving impact from capacity building support need to be reinstated, notably:

- Clear definition of the *roles* of management; and
- Ensuring the whole public administration *system* is integrated.

Another commonly held view amongst interviewees is that donor programs should not be put in place on top of existing government programs. Initiatives such as the *Enhanced Cooperation Program* (ECP) for example, need to **integrate advisers** within existing systems, both psychologically and in terms of their work programs. Other consultant support too, needs rethinking. In most cases, the **areas of focus are correct, but implementation approaches are ineffective**. More often than not, consultants leave nothing behind, either because they have been unable to encourage local commitment to following through, or because there is no consistency in the models, plans and approaches introduced. All interviewees describe advisers from earlier years being much more closely integrated and collegiate in their approach.

VIEWS ON PNG'S OUTLOOK

All those interviewed remain positive about PNG's prospects for effective public administration over the long term. They believe that, if PNG starts now and really focuses on the key issues, it can achieve this over one generation. "Things are happening now that can set the foundation, but it needs constant shoulders to the wheel." In spite of its problems, they identify a number of strengths that they believe give PNG a firm foundation on which to build:

- Strength of constitutional offices;
- Flexibility of governments of the day to amend the constitution when necessary;

¹² One example given was the fact that school inspectors are not visiting schools, because they are too busy "looking at high tech things like the Virtual Colombo Plan". The advice to donors is – "focus on core issues and don't divert".

Appendix 1

- Rural-based nature of the population – which assures a basic standard of living (access to basic housing, food and other necessities);
- Resource base for economic growth;
- Traditional land system – which provides people with a certain level of security even if all else fails; and
- A new, increasing demand from communities for performance from government.

Interviewees all recognise that the community's tolerance of government's problems (to date) has been because it can sustain itself; but impatience with the failure of service delivery is growing.

As they see it, attitude is the crux of the issue. PNG needs to develop confidence and a positive attitude to building a nation. It must learn to appreciate its own huge potential, embrace its ability to harness that potential, build a sense of community, and recognise the need to do things for itself. People need to think as Papua New Guineans first and foremost, respecting all others regardless of tribal group.

“OUR COUNTRY NEEDS GOOD ROLE MODELS, ESPOUSING THE RIGHT PRINCIPLES OF SERVICE AND COMMUNITY CARE. THEY MUST BE PEOPLE OF INTEGRITY AND COURAGE ENOUGH TO STAND UP FOR WHAT THEY BELIEVE TO BE RIGHT WHEN CONFRONTED WITH A SEA OF SILENCE AND QUIET CONSENT.”

- SIR ANTHONY SIAGURU, 1 APRIL 2004

Appendix 2

**JCFADT Inquiry: The Role of the Private Sector in Promoting Economic Growth and Reducing Poverty in the Indo-Pacific Region
Submission 153**

Opening presentation notes for Mr Paul Flanagan, Visiting Fellow, Development Policy Centre, Crawford School of Public Policy, Australian National University 9 February 2015.

Thank you for the opportunity to appear today.

The subject matter of the inquiry is an important element of the re-orientation of the policy directions for Australia's overseas assistance. I welcome most of these changes in direction, such as an increased focus on the private sector as well as supporting governance programs. Experience indicates they are the fundamental ways to reduce poverty.

Looking through previous submissions, including the excellent submission by my ANU colleagues Robin Davies and Margaret Callan, there has been considerable focus on several levels of assistance for the private sector. These include: building partnerships between the private sector, the community (such as churches and NGOs) and government; direct forms of assistance to businesses (such as financial inclusion funding and enterprise funds); sectoral based assistance in areas such as agriculture or tourism and broader support for the business enabling environment such as lowering the costs of doing business or improving competition policy.

Tonight, I wish to emphasise the importance of appropriate macro-economic settings to support private sector development. The comments will focus on PNG as a key partner country and one where I have the strongest background experience extending back to 1978 and including over two years as the senior advisor to the PNG Treasury from 2011 to 2013. My opening is in two parts – first, the case for considering macro-economic settings as an essential element for supporting private sector development, and second, the type of policy actions that Australia can take to support this element of building the private sector in our partners.

First, good macro-economic policies are essential to private sector development and poverty reduction, including and arguably especially for women. Although the linkage may seem indirect, these macro-economic settings are arguably the most important element for building a thriving private sector and leveraging entrepreneurial abilities. The macro-economic settings encompass good exchange rate policy, good fiscal policy (including tax policy), good monetary policy, and good wages policy.

A few examples. How does a sound exchange rate policy assist the private sector? PNG moved to a market based exchange rate in the mid-1990s. This was an important element of its recovery from the fiscal crisis at that time, as well as supporting the high growth rates following the Asian financial crisis from the turn of the century. However, **on 4 June 2014, PNG moved away from a market based exchange rate. Indeed, it appreciated its currency by 15% at that time. What have been the consequences of this policy? First, PNG businesses are now finding it very difficult to get the foreign exchange required to pay for imports essential to their businesses. By moving the value of the Kina above the likely market rate, there is a significant exchange rate shortage. PNG businesses now need to tell their overseas suppliers that it may take many months, even more than a year, to pay their bills – not because the business doesn't have enough funds, but because they cannot convert their Kina in other currencies required to pay for their imports. This raises**

Appendix 2

business costs. It makes business harder and undermines links to overseas suppliers. It undermines PNG's integration with the wider global economy. Currently, the central bank has to decide which imports to give priority to – is it to Puma to pay for petrol imports, or is it to a retailer seeking to restock their shelves, or is it to an agricultural producer to import fertilizer. **A second impact of such a macro-economic policy is on exporters. The largest component of the private sector in PNG in terms of the number of people affected are the small-holder cash cropping activities of farmers. For example, it is estimated that there are 2.1 million people, over a quarter of PNG's population, that receive 40 to 60 per cent of their incomes from selling coffee. This is an absolutely core element of the private sector in PNG. And with the 15% appreciation of the Kina on 4 June, it means that every one of these farmers now receives 15% less for each kilo of coffee they now sell. This obviously changes incentives. Indeed, it is estimated that the change was enough to force 130,000 of these farmers below the poverty line. Women and children are most likely to have been adversely affected. Macroeconomic policies matter.**

A second example. Fiscal policy in PNG is no longer credible and this will affect the private sector. In the very short term, the major scale up in Government expenditure produces more opportunities for contracts. However, with deficits now approaching double digit levels (estimated to be around 8% this year and over 10% from 2016 onwards on realistic scenarios), and the government effectively printing money to finance those deficits, inflationary pressures are likely. During PNG's last major fiscal crisis flowing from the Asian financial crisis, inflation jumped to nearly 20 per cent as did interest rates. The uncertainty and cost of such an environment is very difficult for the private sector to operate in. Additionally, the private sector is dependent on other key policies such as appropriate levels of funding for key infrastructure roads so goods can get to markets, as well as building the education and health of a workforce. Current funding projections are that areas such as infrastructure, education and health funding will be cut by over 25% in real terms over the next two budgets. In this context of required fiscal constraint, there are serious questions about the judgement calls to prioritise new equity funding in areas such as Oil Search shares – the government can get higher rates of return by investing in areas such as education, law and order and infrastructure.

So what actions can the Australian government undertake to work to ensure macro-economic settings in partner countries are part of the supportive environment for encouraging private sector growth? This can be a sensitive area as these macro-economic issues go to the core of sovereignty.

At a high level, we should utilise multi-lateral opportunities for peer based reviews of macro-economic policies such as provided by the IMF and their annual Article IV discussions. It is disappointing that with the move away from market based exchange rates and the move towards effectively printing money that the Australian Executive Director at the IMF did not encourage an IMF Board discussion of the PNG annual report late last year.

On a bilateral policy dialogue level, we should ensure that such macro-economic issues feature in high level policy dialogues and relationships, including Ministerial discussions. The most effective of these often occur behind closed doors, so possibly this avenue is already being actively pursued. As part of our regional engagement, the importance of relationships is critical. Our Treasurer and Finance Minister should have good relationships with peers in countries such as PNG.

At a more indirect level, we should strengthen PNG's capacity to analyse its own economic performance, formulate good policies and implement actions. This can occur through initiatives such as the Governance Precinct recently announced by the Minister for Foreign Affairs in seeking to strengthen PNG's pool of public policy skills. This indirect support level should also be reflected in

Appendix 2

much more support for government to government institutional linkages programs. This should be a whole of government approach, and individual agencies should be obliged to provide this support with appropriate DFAT funding. Support can also be provided to various key relationships that interact with government in the formulation of policies, such as chambers of commerce, the PNG Australia Business Council and other forms of building civil society.

On occasions, and these would be in more unusual circumstances, the appropriate utilisation of Australian laws could be a useful adjunct to other actions. For example, poor macro-economic policies can also be a reflection of corruption. **We have Australian and international rules such as anti-money laundering rules and proceeds of crime legislation that arguably could be used to reduce the incentives for corruption.** Mr Sam Koim, the Chairman of the now unfunded PNG anti-corruption taskforce, "Taskforce Sweep" has expressed concerns that Australia has not done enough to utilise its laws to provide a deterrent to corrupt practices in PNG (see his 4 October 2012 speech to AUSTRAC as an example).

Another example is the possible use in very selective circumstances of powers under Australia's foreign investment rules to influence decisions that are not supportive of good macro-economic or good governance policies. For example, there are arguments that the Australian Treasurer should have used or should use the powers under the Foreign Acquisitions and Takeovers Act 1975 to limit the major concerns around a major share purchase by the PNG Government in March 2014. Dealings around the \$US1.3 billion purchase of Oil Search shares and its associated loan agreement from UBS led to the dismissal of the PNG Treasurer. PNG's Chief Justice, acting on recommendations from the PNG Ombudsman and PNG Public Prosecutor, has called for a leadership tribunal for the Prime Minister O'Neill to face allegations "that the Prime Minister failed to comply with administrative and financial processes including the normal borrowing process". This proposed share purchase should have been notified to the Australian Government and been approved prior the PNG Government buying the shares (it was notifiable under the act as it represented a foreign government taking a direct investment (10.01% at the time of the transaction) in a company with 100% owned Australian subsidiaries with land interests in Sydney and Brisbane secured by guarantees from the parent company and non-recurrent assets of over \$US44m). It is not clear if the notification was made. However, it was still up to the Australian Government, specifically the Australian Treasurer, to ensure a determination was made under Australian law on whether the transaction was in the national interest. Arguably, the Australian Treasurer, in taking a due diligence approach and a broad interpretation of the national interest, could either refuse approval for the transaction or add conditions to the share purchase (such as having the loan approved by the PNG Parliament before the share purchase was completed). Of course, this would be a very sensitive issue but the circumstances are very unusual and significant. At this stage, the Australian Treasurer is or could be implicated in approving this Oil Search share purchase which has led to the dismissal of the PNG Treasurer and is the subject of a referral of the PNG Prime Minister to a Leadership Tribunal (when this last occurred, the former PNG Prime Minister Somare stood down for the time of the hearings).

By focusing on these macro-economic issues, I wanted to encourage consideration of the importance of good macro-economic policy settings which are fundamental to fostering the role of the private sector in promoting economic growth and reducing poverty.

Thank you for your time this evening.

Appendix 2

Some macro-economic snapshots of PNG's emerging fiscal crisis which will hurt the private sector

GoPNG Revenue and Expenditure Shares of GDP

