The 1995 Organic Law in Papua New Guinea

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This paper is a preliminary evaluation of the reforms to the provincial government system introduced by the National Parliament on 27 June 1995 under the Organic Law on Provincial Governments and Local-Level Governments (OLPGLG), with specific reference to Central Province. The problems of local development—lack of financial resources, skills, access to banking and credit, and poor strategies—are unlikely to be improved by the reforms.

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Papua New Guinea is a unitary state with some decentralising features (Cheliah 1981; Axline 1986; Peasah 1994). Provincial governments and provincial powers are defined through the 1977 Organic Law on Provincial Government (OLPG) and the 1995 OLPGLG, respectively. In 1995 the OLPG was repealed and the Organic Law on Provincial Governments and Local-Level Governments was enacted, giving the National Parliament the powers to grant and to withhold (through legislation) the powers of the provinces and also of local-level governments.

Papua New Guinea is comprised of several hundred micro-societies with distinctive cultures and languages. The process of decentralisation aims to accommodate this vast diversity.

However, at independence in 1975 the pressure for decentralisation was not uniform. In fact, there was little support for early independence, let alone increased decentralisation, in the populous Highlands region, which was lagging in educational and health services and was dependent on Canberra and Waigani for transfer of expanding financial and skills resources. It was perceived that, as power was devolved to Waigani, Australian aid would begin to slow down, and so would the flow of resources to the lagging areas. Nevertheless, with pressure from Bougainville forcing the pace of change, and following the recommendations of the Constitutional Planning Commission and later of the McKinsey Report (McKinsey and Company Inc. 1977) 19 provincial governments, each with its own Premier, executive and legislature as well as taxing and revenue-raising powers, came into being. Not all the provinces had the capacity to take on full financial responsibility and this was only steadily devolved. In 1995, when the OLPGLG was introduced, only eight (excluding Bougainville) provinces had full financial responsibility.

The introduction of OLPGLG not only reflected the conflict of interest between MPs and provincial politicians—the latter were seen to undermine the former—but also the sentiment among the MPs that the system in place under OLPG had failed, because there was little expansion of services beyond the provincial headquarters. They also argued that the problem was a lack of cooperation between the provincial and national politicians and that OLPGLG, by abolishing separately elected assemblies, was aimed at creating cooperative decentralisation. There was also a view that inadequate resources were being transferred from the national to the provincial level and, in particular, to the village and local level.

Under the OLPGLG the national government is obliged to transfer roughly another K200 million to the provinces, districts and local-level governments. These transfers are more egalitarian and take into account cost disability, of population, land area and, in the case of maritime provinces, the sea area.

The introduction of OLPGLG is still in a transitional stage and there are a number of confusing areas which are likely to be clarified with time. More importantly, OLPGLG is being implemented in the midst of a continuing fiscal tightness, starting with the 1994 crisis, with implications in terms of the transfers of revenues and functions to the provinces. There are likely to be continued structural adjustments with the shedding of staff at the national level.

Apart from severe budgetary constraints at the national level, there is also the skills constraint, which will affect the implementation of the reforms at the provincial, district and local level. OLPGLG increases demand for skills, particularly at the district and local level. In addition, the withdrawal of banking facilities by the banks at the district and local level is likely to create further difficulties for decentralising activity.

In the past, provinces have been optimistic about their revenue-raising capacities, but in practice revenues have been constrained by the lack of economic activity and the inability of the provinces to mobilise resources. Without such mobilisation and increased economic activity, transfers of revenues from the national government to the provincial, district and local-level governments will have only a marginal impact. The transfers in 1996 are largely illusory and in real terms, in the case of the Central Province, are considerably below those of the 1993 level.

The problems bedevilling development at the district and local level in Papua New Guinea have been the lack of financial resources, lack of skills, lack of access to banking facilities and credit, and the lack of a strategy to mobilise resources. These problems are not going to go away with the introduction and implementation of OLPGLG.

Implications of OLPGLG

According to the 1996 Budget Speech,

> [t]he principal goal of the reforms is to improve the delivery of services right down to the village level and in doing so improve the lifestyles, standard of living and opportunities for all Papua New Guineans (Haiveta 1996:14).

Improving the delivery of services and lifestyles of villagers could then be seen as a vision for Papua New Guinea. But will the OLPGLG and the structures deliver the outcomes envisaged?

It is not yet clear if the outcome of OLPGLG will be decentralising or centralising. By clearly specifying the separate revenue-raising powers of the local-level governments, it is decentralising. But the emerging financial and planning structure is centralising. Although the OLPGLG has defined separate revenue-raising powers for local-level governments, it only specifies administrative and financial structures for the provincial and district level. The financial and administrative structures for the local level are not defined. The district and the provincial treasurers are responsible to the Secretary of Finance. These treasurers will control outlays. The functioning and efficiency of these treasuries will be problematic, given the accounting skills constraint. Skills constraint has impaired the efficient operations of a number of provincial governments and will need to be stretched further to meet the requirements of 267 local-level governments, which are expected to come into being following the 1997 elections expected to be held in the third quarter of that year. OLPGLG requires provincial and local-level governments to submit a financial statement every year—the penalty for non-compliance could be the withholding of 50 per cent of their funds. It is unlikely that most local-level governments will be able to meet this requirement, causing tension between the national government and local-level governments and, in some cases, provincial governments. Even in the past, such tensions existed. For instance, the Central Provincial government was suspended just before the OLPGLG was introduced into the National Parliament in 1995—an implicit reason for its suspension was the opposition of the Premier to the decentralisation system reforms, which were being proposed by the Constitutional Review Committee. Financial mismanagement was another reason.

A structure for planning similar to the financial structure is expected to be set up with the recently recreated National Planning Office and its Director at its apex and the provincial, district and, perhaps, local-level planners below. Again the skills constraint will apply and the transition period in the establishment of this structure may stretch into the next century—although 19 Provincial Governments had been created by 1980, only nine of these had full financial responsibility in 1995, when the 1977 Organic Law was repealed. OLPGLG gives full financial responsibility to the provinces; there is no discussion of planning responsibility. But the National Planning Office expects to combine both the top-down and bottom-up approaches to project planning and programming. This requires not only planning skills at the three tiers of government, but also skills implementation.

Central Province is a province beset by severe skills constraint. This is evidenced by the lack of cash officers in two of the districts and the inability of the Provincial Administrator to attract qualified personnel to work at the district level. Given the high levels of financial and administrative skills of people of Central Province origin in the National Capital District and elsewhere in the country, this is at first puzzling. But poor infrastructure in the districts and the relatively low remuneration for skilled personnel, as well as the availability of employment opportunities elsewhere—particularly in National Capital District—explains this paradox.

In the face of worsening law and order problems the commercial banks in Papua New Guinea have cut back on their branches in the provinces. This will create

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particular problems for the operation of the district treasuries and more so of the proposed local-level treasuries. Without the banks, it is difficult, if not impossible, to operate cash offices, let alone treasuries. In the case of Central Province, at least two cash offices had to close as the commercial banks closed their operations in the 1990s.

Implementing the OLPGLG—some confusions and concerns

A number of confusions around the implementation of the OLPGLG were evident in early 1996.

The most significant related to the extent to which resources were being transferred to the provinces under the 1996 Budget. Under the OLPGLG formulas (together with mining provinces' additional entitlements under the mining agreements and special support grants), although the provinces were entitled to just over K516 million, only K466.3 was made available, due to the phasing-in of 'development grants' (the combination of Provincial Infrastructure Development Grants, Town & Urban Services Grants and Local Level Government & Village Services Grant) over the 1996–98 period. Only 75 per cent of these grants were being paid in 1996; it was planned to pay 90 per cent of them in 1997 and 100 per cent in 1998.

Although the national government (Haiveta 1995:16) argued that this phasing-in had been discussed and agreed to with the Governors of the Provinces, not all Governors appear to be in agreement. Moreover, the government had not invoked the 'serious downturn in the national economy', which it could have under Schedule 1.2 of OLPGLG, to reduce the amount being transferred. In addition, while the national government was saying that it was transferring in 1996 an additional K200 million over the 1995 amount paid to provincial governments (Haiveta 1995:15), only K133 million was budgeted (Papua New Guinea 1995a:Tables 4.2A and 4.2B). In 1998, when the full amount of development grants is paid to the provinces, it will be K183 million (and not K200 million) more than they received in 1995; unless there are cost of living adjustments. Given the budgetary constraints, it is unlikely that such cost of living adjustments will appear over the next few years. Consequently, although funds were being redirected from the national government to the provinces and local-level administrations, the figures released by the national government were different, creating some confusion as to the actual amounts to be disbursed.

In addition, as part of the provincial budget, an amount of K59.95 million of 'Rural Action Plan' funding was budgeted to be spent on the basis of a committee comprised of the local Member of Parliament as chair and at least one representative of a non-government organisation.

Whereas the Department of Finance plans to have control, through the provincial and district treasurers, over the spending of the Rural Action Plan, national MPs are likely to have different views. Around K33 million of this was previously part of the Electoral Development Fund or slush fund, which was spent at the discretion of national MPs in the past. It is probable that the national MPs will insist that they have total discretion over this K33 million. Once this K33 million is removed from transfers to the provinces, only K100 million of additional funds remains for transfer.

Not only was the amount being transferred much smaller than K200 million, but the provincial governments found themselves suddenly responsible for a number of additional functions. The provinces became responsible for Education Subsidies (in lieu of 'free education'), expansion of Grades 7 and 8 (top-up of community schools), payment of village courts, church health services and maintenance of health services. Some provinces, such as Central Province, found themselves (after the removal of amounts for the additional responsibility), with net appropriated amounts in money terms slightly smaller than they had been appropriated for 1995 and considerably smaller than the actual amount in 1993 (Table 1).

That the financial resources being made available by the national government to the Central Province in 1996 are considerably less than in 1993 is not surprising because of severe budgetary constraints faced by the national government. Under the current World Bank structural adjustment program the national government is limited to a budget deficit of not more than 1 per cent of GDP. Tight macroeconomic policies (fiscal, monetary and wages) must be kept in place in order to bring down the inflation rate, which in the third quarter of 1995 had hit 23 per cent. The 1996 Budget gives overall outlays as K1,924.3 million—K70 million more than 1995 and K173.3 million more than 1993. But once the public debt service component (which has risen since 1993 quite sharply because of high domestic interest rates and kina depreciation and therefore through the valuation effect) is removed from the total expenditure figures then the 1996 planned outlays (in money terms) are somewhat smaller than those in 1993 (Table 2). In real terms the 1996 outlays are likely to be 75 per cent of those in 1993 (actual). In relative terms, Central Province has become more disadvantaged than the other provinces since 1993 (Table 1 and Table 2)—the new grant formulas for Administration, Infrastructure and Local Level and Village Services are based on population, land area and, in the case of maritime provinces, on sea area as well. Provinces with a larger urban population gain from the population-based formula for a fourth Town and Urban Services Grant. Only the staffing and teaching services grants take account of existing (1995) staffing costs and responsibilities.

Central Province's population is about 75 per cent of the mean of Papua New Guinea's 20 provinces. Though its land area (29,500 km) is larger than the average for the other provinces (23,112 km), this does not substantially change the outcome of

Table 1 **Central provincial government funding from national government, 1993–96** (K'000)

	1993 Actual	1994 Appropriation	1995 Appropriation	1996 Appropriation
Funding to Central Province	16,089.8	16,113.3	14,151.0	17,034.8[a]
Less cost of additional functions in 1996				3,030.4[b]
Total				14,004.4

[a] Includes K2.75 million of Rural Action Program funds.
[b] Does not include K500, 000 which Central Province is required to pay for the use of Port Moresby General Hospital as a part of cost-sharing arrangement with the National Capital District.
Source: Calculated by the authors from: Papua New Guinea, 1995b. *1996 Estimates of Revenue and Expenditure*, Government Printer, Port Moresby; Papua New Guinea, 1994. *1995 Estimates of Revenue and Expenditure*, Government Printer, Port Moresby; information supplied by the Provincial Administrator, Vari Fore.

Table 2 National government: overall budget constraints, 1993–1999 (million kina)

	1993 Actual	1994 Actual	1995 Prel.	1996 Budget	1997[P]	1998[P]	1999[P]
Total expenditure	1751.0	1722.4	1854.5	1924.3	1972.3	2092.4	2207.6
Public debt service	297.7	383.6	429.4	478.0			
Total	1453.3	1338.8	1425.1	1446.3	1435.4	1516.6	1563.8

[P] projected
Source: Papua New Guinea, 1995a. *1996 Budget, Vol. 1, Economic and Development Policies*, Government Printer, Port Moresby:Table 4.3(a).

the grants for Central Province, if they were only based on the per capita population formula. With a total urban population of only 4,517, its urban population is only 4.8 per cent of the total for the Province, compared to 15.4 per cent of the total for the whole of Papua New Guinea (Papua New Guinea, National Statistical Office, 1994a:43); only Enga, Southern Highlands and Chimbu had lower shares of urban population in 1990 and these shares are likely to have changed in the 1990s for both Enga and Southern Highlands with the onset of mining activity. Consequently, Central Province's Town and Urban Services Grant is much smaller than that for most other provinces.

Though population-based per capita grants are much more equalising than the minimum unconditional grants based on the now-repealed 1977 Organic Law (which catered for the staffing requirements of the services in the provinces as they existed in 1976/77) these population-based grants will create future problems. One of these will be the reliability of the population data which, under the OLPGLG, is required to be collected every 5 years—one year before the general elections. Since grants are population-based there will be a temptation for local areas, districts and provinces to raise their population count.

The National Government's tight budgetary situation in 1996 will apparently continue to exist for the rest of this century (Table 2), so part of the confusion exists because of raised expectations in the provinces which are divorced from the reality of the fiscal situation. The national government has also had difficulties in 1995 in making voluntary redundancies; the public service in 1996 has around 2,000 more employees than planned at the end of 1994.

Apart from the problem of unrealistic expectations created by some national government statements, there is an added reason for the confusion in the way development grants have been set out for the different provinces in the estimates of revenues and expenditures. While they are not separately specified for the Central Province (and three to four other provinces), they are clearly separately specified for the rest, leading to speculation that some Provinces (including Central) may have missed out on some of the grants. The budget papers have structured the revenue transfers from the national to the provincial governments differently. For example, there are some provinces which receive grants for Arts Schools, when there are no Arts Schools in these provinces. Because of the confusion, some Provincial Governors have threatened to sue the national government for being in breach of the OLPGLG in the allocation of funds to the provinces.

Further confusion has been created because of the contradictory statements of the Minister for Village Services and Local Level Government and the Minister for Finance as to who is responsible for the approval of the provincial budgets. Whereas the OLPGLG makes the Minister for Village Services and Local-Level Government responsible for approving the provincial budgets, the Minister of Finance (and especially the Department of Finance) argue that the former is expected to be a rubber stamp for such budgets, after they have been scrutinised by the Department of Finance and passed by the provincial assemblies. As a result of this only a few provincial budgets had been approved by the national government by April 1996, almost five months after the 1996 Budget had been approved by the National Parliament.

In addition, the National Economic and Fiscal Commission, which has been made responsible for the calculation of the equitable factor in the four grants (Provincial Government and Local Level Government Administration Grant and the three Development Grants), had not, at the time of writing, explained how it will determine such an equitable factor. Its predecessor, the National Fiscal Commission, failed to increase resources to the lagging provinces (Axline 1986), due to inadequate funds, some of which went towards maintenance grants, and others were spread too thinly in per capita terms. After 1986, it effectively ceased to function, because no funds were made available by the Department of Finance for it to disburse.

The manner in which the National Economic and Fiscal Commission calculates the equitable factor will make a difference to the final amount paid out to the provinces—some provinces will get an additional amount, while the grants of others will be reduced. The grant formulas also include a provision for payment of a conditional complimentary support grant, which is also based on the recommendations of the Commission. The most difficult task will be the creation of a database comprised of social and economic indicators, revenues and expenditures, physical infrastructure and geographical information for each province and for each local-level government area. Such a database, properly resourced and serviced, is essential for the National Economic and Fiscal Commission to conduct its functions properly. Given the experience of the National Fiscal Commission, the National Economic and Fiscal Commission should avoid calculating the equitable factor, because it will not have the resources to do a satisfactory job. Instead, it should use the imperfect information on regional and intra-regional inequalities to recommend a conditional complimentary support grant, which would be aimed at stimulating economic activity in a lagging province or district. The objective should be to stimulate economic activity, to improve the economic and revenue base of such areas. Spreading resources thinly, as the National Fiscal Commission did, would achieve little.

Since the creation of the provincial governments in 1977, all the provinces have been entitled to a 'Derivation Grant', which was 1.5 per cent of the export value of goods, excluding natural resource exports, such as minerals and timber, on which the provinces exporting such products have received royalties. OLPGLG continues this grant but raises it to 5 per cent —an additional transfer of K12–K13 million of funds from the national government to the provinces. The problem in the past has been that export values have not been available to the Department of Finance for the calculation of the Derivation Grant. For instance, despite enormous fluctuations in the value of rubber, which is a major export from the Central Province, it continues to receive a Derivation Grant of K49,700. Unless the National Statistical Office and each province create such export data in collaboration, the Derivation Grant will, at least in the case of some provinces, be below their entitlement under OLPGLG. The National Statistical Office needs additional resources for this exercise as well as for the increased workload associated with conducting a population census every 5 years.

Further issues for Central Province

The 1996 Central Provincial Government budgeted the total estimated revenue at K22,239,600. Of this, K17,034,000 are grants from the national government; the balance of K5,204,800 is internal revenue. The latter represents around 23 per cent of total estimated revenue. In relation to the historical experience of the province (Table 3), this appears to be too large; in 1993, which was a good year for Central Province, internal revenue was around 9.5 per cent of total revenue. In 1996 around 50 per cent of the internal revenue is expected to be raised from general sales tax and vehicle registration and licensing fees. The general sales tax component is dependent upon the National Capital District sharing its sales tax revenue with Central Province. Given that the Governors of both these provinces belong to the same political party, the Governor of National Capital District in 1996 budgeted to provide K2 million to Central Province as a part of revenue and cost-sharing arrangement; Central Province is to pay K500,000 for the use of Port Moresby General Hospital. If these revenue and cost-sharing arrangements can be formalised as an agreement, then it will certainly improve the financial situation of Central Province. Though the province was promised K1 million in 1995 as its sales tax due by the National Capital District government, this amount was not paid. The money from vehicle registration and licensing fees (budgeted at K848,000) is dependent on the provincial government reopening its registration office in Port Moresby, closed because of funding constraints in 1995. In mid-February 1996 it had not been reopened. Given the large revenue gains, it is in the interest of Central Province to reopen it urgently.

K800,000 is expected to be raised through a Bookmakers Turnover Tax. This was previously being collected by the national government on behalf of Central Province. Whereas the national government

Table 3 **Central Province internal revenue as a proportion of total revenue, 1982–96** (per cent)

	1982 Actual	1984 Actual	1989 Actual	1993 Actual	1996 Budget (internal)
Revenue (per cent)	1.8	0.5	5.0	9.5	23.4

Source: Axline, W.A., 1986. *Decentralisation and Development Policy: Provincial Government and the Planning Process in Papua New Guinea*, Papua New Guinea Institute of Applied Social and Economic Research Monograph 26, Boroko. Calculated by the authors from Papua New Guinea (various). *Budget Papers*, Government Printer, Port Moresby; Papua New Guinea, Central Provincial Government (various). *Budget Papers*, Government Printer, Port Moresby.

budget papers do not have any mining and timber royalties plus Special Support Grant, Central Province's budget papers expect to raise a total of K430,000 as internal revenue from these sources. Since these are transfers from the national government (and the national government apparently does not have additional funds) rather than internal revenues, these amounts are unlikely to be available to Central Province.

The internal revenue base of Central Province in 1996 is not likely to be different from that of 1993, except for the improved prospects of receiving its share of the Sales Tax from National Capital District. Urban population data suggests that, with the exception of Bereina and to some extent Tapini, economic activity as reflected in changes in urban population declined. In one sense this is not serious, because the population of Central Province is able to find employment in National Capital District. But the close proximity of Port Moresby also drains Central Province of economic activity and inhibits expansion of its economic base.

A strategy for Central Province

It is clear that Central Province needs to improve its revenue and production base. The Provincial Government has focused on cost and revenue-sharing arrangements with National Capital District, which are likely to net Central Province K1.5 million. These arrangements should be formalised, so that a change of government in National Capital District does not mean a loss of revenue for Central Province. In addition, the Transport Registry office should be reopened for the registration of motor vehicles from Port Moresby and surrounds —there are substantial net revenue gains to be made from its operation. The province needs to ensure that it receives its dues from Tolukuma Gold Mine from the national government in 1996 and up to the life of the mine. It should conduct an inventory of its production and export base and use the data to claim its appropriate Derivation Grant, which has to be larger than K49,700; at 5 per cent (instead of 1.5 per cent) of the export value, it should at the minimum be K165,000.

Central Province should seek in the 1997 Budget a conditional complimentary grant from the national government to help it build a new Provincial capital within the bounds of the Central Province. If Central Province locates its Provincial capital at a natural harbour some distance from Port Moresby, but connected to the capital by a good quality and regularly maintained network, this could set into motion agglomeration forces, which could see the growth of an urban centre to cater for its needs. It would also draw urban activity away from National Capital District and would, through the improvement of infrastructure, encourage some highly skilled people of Central Province to return to work in the province. As the revenue base is lifted, this would enable improvements in transport infrastructure, which would further stimulate economic activity, expanding the revenue base. The ability of the national government budget to provide real expansion in transfers is limited for the foreseeable future (see Table 2).

Unless Central Province, through tax and cost sharing arrangements with the National Capital District, and through stimulating economic activity, increases its revenue base it will continue to remain a backwater of the National Capital District.

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