Note

Fiscal responsibility legislation and its relevance to Papua New Guinea

Brian Brogan, Michael Woods and Carla Schmidt

Visiting Fellow, Australia Asia Management Centre, The Australian National University
Commissioner, Australian Productivity Commission
Associate, Australia Asia Management Centre, The Australian National University

The 1997 *World Development Report* begins

> Around the world, the State is in the spotlight. Far-ranging developments in the global economy have us revisiting basic questions about government. What its role should be, what it can and cannot do and how best to do it (World Bank 1997:1).

Some countries have been more energetic and creative than others in responding to these questions. For some it has been an academic exercise entered into with little enthusiasm. For others, it has been a matter of great urgency spurred by political or economic collapse.

For the OECD countries the focus was on identifying what government alone can do, leaving the rest to the private sector and devising better ways of doing what was to remain in the public sector. English-speaking countries have been in the vanguard of these reforms. New Zealand is probably the most often cited as a shining example—the United Kingdom and Australia are not far behind. Surprisingly the United States has lagged.

For developing countries the task has been broader and more difficult—redefining the role of government is not easy in societies with limited business and commercial sectors. The centrally planned economies have even greater problems. At times they have no commercial sector at all, have poorly developed financial systems and lack the market mechanisms so vital to economic efficiency.

An extensive literature now exists on public sector reform. Common themes are emerging but solutions must be tailored to a country's needs and capacities, not simply follow international fashion. Balancing the need to achieve global competitiveness against the restraints of local resources and history is at the heart of any practical reform program. No one model of reform is uniquely relevant to all countries. Nevertheless important lessons can be learned by detailed study of the endeavours of other countries—unsuccessful as well as successful.

Papua New Guinea can learn by investigating both world best-practise and the history of reform scenarios such as the New Zealand model. Ultimately local characteristics have to be grafted before workable solutions to local problems are found.

The following elements can be found in all successfully reforming countries

- policy is developed and managed in a framework of open, transparent and accountable institutions and procedures

- public financial flows are fully documented in timely, periodic and independently prepared reports made available to the public
- a public culture of policy and management evaluation and debate is encouraged by fostering appropriate institutions such as elected parliaments, a free press, academic research facilities and institutionalised opportunities for business and community groups to involve in dialogue with government on the basis of such reports and evaluations
- a move away from budgeting simply for financial inputs to specifying required outputs and to evaluate performance by recognising both financial probity and achievement of specified output goals
- a gradual move to accrual from cash accounting—moving from traditional recording of cash flows to a system where the government-wide and long-term expenditure and revenue implications of present decisions are noted at the time the decisions are made
- commercial forms and practises being adopted in arranging and managing government activities by corporatising, possibly privatising and contracting out or outsourcing the supply of required public goods or services.

Fiscal responsibility legislation

Fiscal responsibility legislation is one element in a reform program. It can take various forms but usually comprises

- legislated fiscal outcomes—a specified state of budget balance or maximum rates of change in designated fiscal flows (this presumably compels fiscal responsibility)
- legislated requirements on governments to report fully to the parliament on the state of fiscal affairs at designated times, for example at budget time, prior to elections (presumably inducing governments to act honestly and fairly through public exposure of its financial dealings and their impact).

Few analysts support the first option—legislated fiscal targets. Even where they have been adopted (United States) they have been largely ignored as there are no penalties for non-compliance. In most countries adoption of fiscal responsibility legislation mandating procedures is the preferred option.

Fiscal responsibility legislation usually comes at a late stage in the reform process, after accrual accounting is fully implemented, introduced against a settled background of regular reporting, parliamentary scrutiny of government fiscal performance and entrenched attitudes to evaluation and review of policy and performance.

Australia, with considerable achievements in public sector financial management reform over the past decade, legislated a 'Charter of Budget Honesty' only in 1998 (Australia 1998).

An approach to fiscal responsibility legislation for Papua New Guinea

Papua New Guinea public sector reforms are not sufficiently advanced at this stage to accommodate dedicated fiscal responsibility legislation. We follow suggestions made in a 1995 Report of the Public Accounts Committee of the Australian Parliament (Recommendations 12–20, 136–141) that Australia was not then ready for full-scale fiscal responsibility legislation. A recommendation for acceleration of the existing reform of financial procedures and

Note

reporting mechanisms and procedures and fiscal responsibility legislation was to be a medium term goal.

We suggest that Papua New Guinea persist with its ongoing reforms of public sector structures and procedures at National and Provincial levels. As part of these ongoing reforms, we advise strengthening of the obligation on public agencies for timely and objective financial reports, improved inputs to the reporting process from the Finance Department and the Bank of Papua New Guinea, and enhanced mechanisms and opportunities for the Parliament to review and debate government performance on the basis of such reports. We also recommend more frequent opportunities for business and community groups to engage in dialogue with government on economic management and future policy options.

The mechanism for this already exists in the *Public Finances Management Act*. Minor amendments would suffice as an introduction to fiscal responsibility legislation strengthening

- reporting obligations, setting up a unit in the Finance Department to monitor compliance
- increasing penalties for non-compliance and enhancing the role and prestige and increasing the resources of the Parliamentary Public Accounts Committee.

For these suggestions to work, other more widespread changes would be necessary.

Parliamentarians would need to take more seriously their responsibility through the Public Accounts Committee to monitor, evaluate and scrutinise government financial management. Public servants would need to take their reporting and evaluating obligations more seriously and adopt more professional attitudes than previously to the correct and punctual compliance with recording and reporting public sector financial transactions. The public generally, especially the media, the business and commercial sector, educators and researchers would have to play an active role in promoting rational debate on the basis of these more transparent and accountable public processes.

The recommendations for Papua New Guinea in our report, if implemented, would assist in the development of sounder policies and enhance the efficiency of government activities. They would also assist the public in making realistic judgments about the limits of government largess—in the long run this would be good for politicians.

An unintended side effect of transparency would be that the harsh light thus focused on public financial flows would deter public officials from the temptation to improve their own well-being at the public expense.

References

Australia, Parliament of the Commonwealth of Australia, 1998. *Financial Reporting for the Commonwealth: towards greater transparency and accountability*, Report 341, Joint Committee of Public Accounts, Australian Government Publishing Service, Canberra.

World Bank, 1997. *World Development Report*, World Bank, Washington, DC.

Note

This Note is based on *Legislating for Fiscal Responsibility: the prospects for enhancing public management through transparency and accountability in Papua New Guinea,* 1998, prepared for the Institute of National Affairs, Papua New Guinea.