

## Financial Management Assessment of the Climate Change and Development Authority

### A Public Financial Management

1. Papua New Guinea (PNG) has experienced sustained economic growth in the past ten years lead by high commodity prices. Despite a rich resource base, the country's social indicators (child and maternal mortality, prevalence of HIV/AIDS and education) lie below those of countries with similar per capita gross domestic product (GDP) levels.

2. The Government of Papua New Guinea (GoPNG) plays a critical role in the economy as the private sector is not well developed. Since independence in 1975, infrastructure assets have not been properly maintained and large scale development projects not launched, despite gains from its resource based economy. The largest project with private sector participation in recent years is the liquid natural gas (LNG) project. The LNG Project, a joint venture led by Exxon Mobil, is expected to begin production in 2015. This is the largest project undertaken in PNG at an estimated cost of \$15 billion<sup>1</sup>, and involves gas production and processing facilities in the Southern Highlands and Western Provinces and liquefaction and storage facilities with a capacity of 6.6 million tons per year. The impact of the LNG Project on the economy will be significant in the production phase as all value addition will take place in PNG<sup>2</sup> and is estimated to add 20-25 percent of GDP.

3. GoPNG has struggled to deliver basic services in the form of health, education and infrastructure to its people as a result of institutional weaknesses, serious capacity issues, geographic challenges, serious issues of law and order and misappropriation of public resources. In the area of public financial management (PFM), although the legal and other guidelines are available for good governance, the continuation of these practices remaining a major challenge. Under the Constitution, public finances are required to be dealt with and accounted for in accordance with the Public Management Finances Act 1995. The Act prescribes basic components of PMF including planning, budgeting, raising and spending public resources and accounting, controls including audit. Planning and budgeting starts from the local level governments (LLG) which are separate and independent budgeting units. The Minister of Finance is responsible for supervision of finances of the GoPNG and District Treasury Offices provide accounting, financial management and support services to LLGs. Detailed procedures for commitment of expenditure and payment of such expenditure are laid down under the Act. However, donor agencies have commented on poor governance in financial management despite the existence of sound systems.<sup>3</sup>

4. PNG's policy framework for public sector management is strong, as expressed through its Medium Term Development Strategy, Medium Term Fiscal Strategy, Medium Term Debt Strategy and the Medium Term Financial Management Strategy. Furthermore, GoPNG has made efforts to strengthen PFM through two Public Expenditure and Financial Accountability Assessments (PEFA) in 2005 and 2008/9. The 2009 PEFA has reported some improvement over 2005 but has commented on the need to improve budget execution and efficiency of service delivery. As a result, in 2009 and 2010, together with its major partners in public financial management reforms, the World Bank, Asian Development Bank, Australian Government (DFAT) and the GoPNG agreed on a new way forward through a Framework for Fiscal Management Enhancement in Papua New Guinea. The Framework provided for strategic initiatives in three broad areas, i.e., managing volatility, strengthening service delivery and integrity of budgeting systems and processes. Whilst it is evident that there is commitment of

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<sup>1</sup> Treasury Department, PNG.

<sup>2</sup> During the construction phase most investment occurred offshore.

<sup>3</sup> Public Expenditure Review & Rationalization (PERR) Program, World Bank, ADB and AusAid.

GoPNG in PFM reform, it is the human resource and institutional capacity to ensure the implementation of systems and legislation that is lacking.

5. Public procurement remains an area of concern despite the strengthening of regulations and the creation of the current structure where the Central Supply and Tenders Board oversees the Specialized and Provincial Tender Boards. Yet, pressures on senior officials and provincial Supply and Tender Boards remain and the risk of contract award manipulation is high.

6. The Office of the Auditor General has made progress in dealing with audit backlog but would benefit from greater resources and specialized skills in dealing with the challenges it faces. The effectiveness of the Public Accounts Committee can be improved so that audit reports are tabled in a more timely manner.

## **B. Financial Management Assessment of CCDA**

7. **Description of CCDA.** OCCD was established as a self-accounting government entity on 1 August 2011, by order of the National Executive Council<sup>4</sup> (NEC) under the Public Finances Management Act of 1995. As a government entity, with its own budgetary identity, OCCD is funded through the Consolidated Fund, and therefore governed not only under the provisions of the Public Finances Management Act of 1995 (the law that governs public finances), but also the Audit Act of 1989. On 27 July 2015, Parliament approved the Climate Change Management Bill making OCCD an authority and renamed as Climate Change and Development Authority (CCDA). The Public Finances Management Act specifies the manner in which public finances should be authorized, accounted for and reported. The Audit Act specifies the institutions that come under its regulation and also the documents that need to be submitted for audit.

8. Under the Climate Change Management Bill, CCDA will be entitled to collect revenues from sources such as excise duty on sale of fuel, import of motor vehicles and any others to be determined.<sup>5</sup>

9. CCDA<sup>6</sup> is headed by an Executive Director who is appointed by the NEC on the recommendation of the Minister of Forests and Climate Change. The four Divisional Directors for (i) Reducing Emissions from Deforestation and Forest Degradation and Mitigation, (ii) Adaptation, (iii) Measurement, Reporting and Verification and National Communications, and (iv) Corporate Services (human resources, finance and information technology) report directly to the Executive Director. The Director Corporate Services is a human resources specialist and therefore the daily operations of the finance division have been entrusted to the Accountant. The position of Finance Manager is vacant and has been advertised. Once recruited, this position will assume responsibility for all accounting matters. The Organization Chart of the Corporate Services Division is presented in Figure 1.

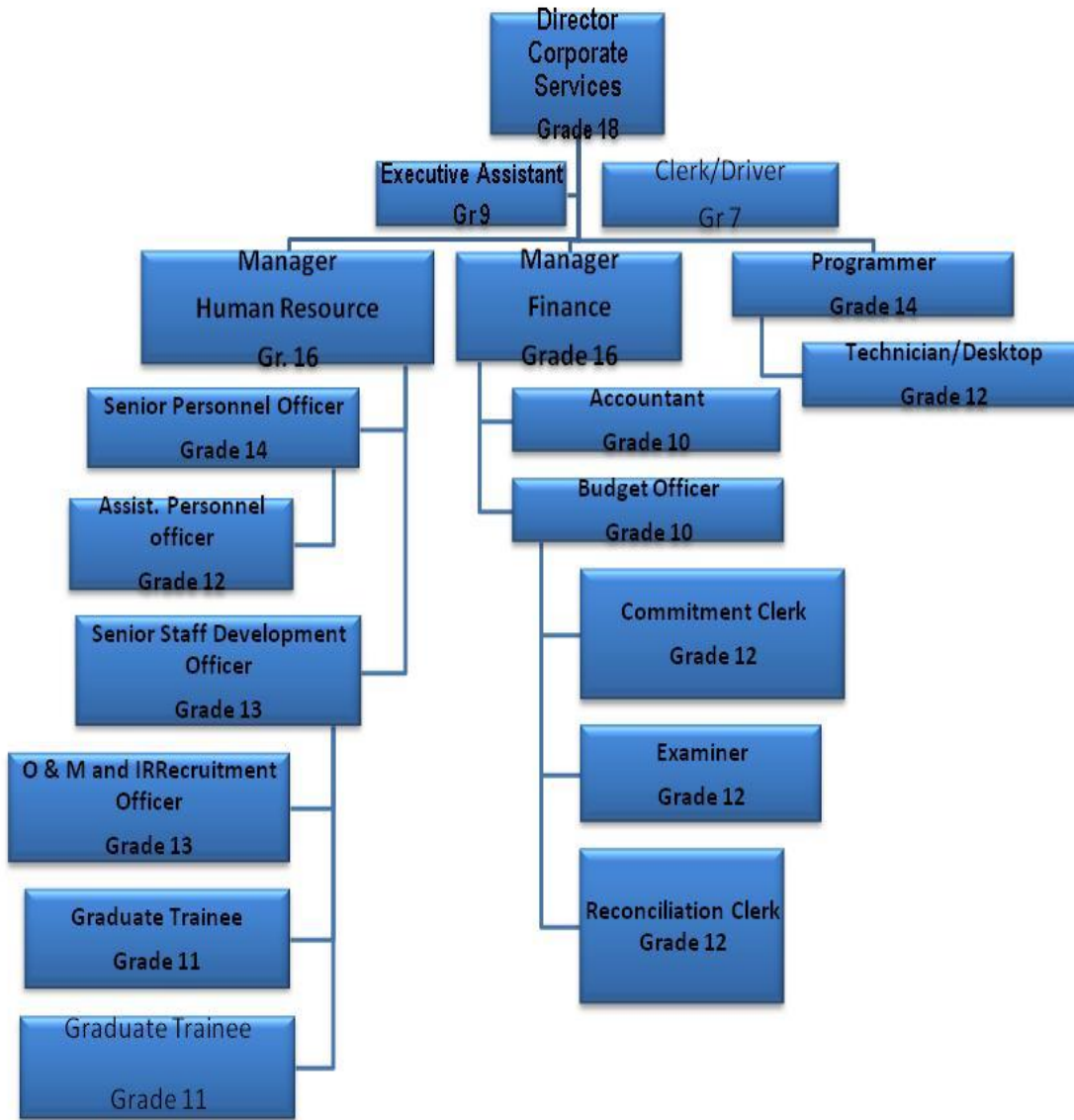
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<sup>4</sup> Government decision making body, i.e. the Cabinet

<sup>5</sup> S.61 titled Funding Levy and Equalization Arrangement proposes an excise levy on sales of diesel 2 toea per litre and on gasoline of 3 toea per litre

<sup>6</sup> Organization structure as given by OCCD

**Figure 1 : Organization Chart - Corporate Services Division**



Source : OCCD

10. The finance division currently comprises of the Accountant, Commitment Clerk and the Examiner. There is anticipated to be a significant expansion of the work of CCDA with the inflow on donor funds, and therefore CCDA submitted a proposal to increase staff from the current 22 to 73. This proposal has been submitted to the Department of Personnel Management and has been approved by the Salaries and Condition Monitoring Committee and the positions advertised. Meanwhile, given the acute shortage of experienced staff in finance and accounting, CACD has contracted the services of a Governance and Statutory Compliance Consultant until March 2014. The feedback from the recruitment process is that it is difficult to attract high quality applicants at the government salary scales being offered. As seen from Table 1 below, the Finance Manager, who will be the officer-in-charge of the finance function is being recruited at Grade 16 for which the annual salary is K44,263 (\$15,500). Requirements for the position are a university degree in accounting, finance or commerce and/or a Certified Public Accountant with

at least three years' experience in accounting and finance in the public or private sector.<sup>7</sup> An equivalent role in the private sector will command an annual salary of approximately K70,000.

**Table 1: CCDA List of Positions advertised for Corporate Services Division**

<b>Corporate Services</b>			
CCDA CS 01	Director	Grade 17	51,251
CCDA CS 02	Executive Assistant	Grade 9	21,079
CCDA CS 03	Driver/Clerk	Grade 7	16,498
CCDA HRM 01	Manager, HRM	Grade 16	44,263
CCDA HRM 02	Senior Pers. Officer	Grade 14	36,167
CCDA HRM 03	Assist Pers. Officer	Grade 12	30,731
CCDA HRM 04	Senior Training and Development Officer	Grade 13	33,262
CCDA HRM 05	Org Design Officer	Grade 13	33,262
CCDA HRM 06	Graduate Trainee	Grade 10	23,974
CCDA HRM 07	Graduate Trainee	Grade 10	23,974
CCDA FIN 01	Manager, Finance	Grade 16	44,263
CCDA FIN 02	Accountant	Grade 14	36,167
CCDA FIN 03	Commit Clerk	Grade 12	30,731
CCDA FIN 04	Examiner Clerk	Grade 12	30,731
CCDA FIN 05	Reconciliation Clerk	Grade 12	30,731
CCDA CIT 01	Director, CIT	Grade 16	44,263
CCDA CIT 02	Systems Analyst	Grade 14	36,167
CCDA CIT 03	Programmer	Grade 14	36,167
CCDA CIT 04	Technical/Desk Off	Grade 12	30,731

Source : OCCD

11. **Funds Managed by CCDA.** The CCDA has an Adaptation Fund amounting to \$6.4 million, financed by the UNDP and also a similar fund for the Reducing Emissions from Deforestation and Forest Degradation and Mitigation division. However, CCDA does not manage the fund and only authorizes UNDP in PNG to make payments on its behalf. Discussions with UNDP resident office concluded that funds could be transferred to a PMU with a proven record.

12. The accounting system is computerized on the PNG Government Accounting System (PGAS). The system operates as a single entry accounting system with information on budget appropriation as approved by Parliament, warrant authorizations, payments against those warrant authorizations and funds available. The approved budget appropriations are sent to CCDA bank account on a monthly basis, on the second week of each month.

13. **Financial Reporting.** The PGAS produces information required by the Department of Treasury. This involves submission of a summary of expenditure allocations setting out the

<sup>7</sup> OCCD Job descriptions, qualifications and duties

appropriation, warrant authority, payments and funds available on a quarterly basis. However, there is no analysis and dissemination of financial information to CCDA and its various divisions.

14. Under Section 8 of the Audit Act, the Auditor General is required to report to the relevant minister on all financial statements furnished to him under the Public Finance Management Act. These financial statements have been defined under the Audit Act as (i) the financial operations for the period and (ii) the state of affairs at the end of that period. Therefore, an Income and Expenditure Account as well as a Balance Sheet must be submitted by CCDA to comply with the Audit Act. The PGAS system cannot produce such statements, therefore CCDA have not been subject to audit since its inception. They are now in the process of preparing these financial statements using *Manage Your Own Business* (MYOB)<sup>8</sup> accounting software and submitting for audit with the assistance of the Governance and Compliance Consultant who is a professional accountant. This is a tedious task as each transaction has to be entered into MYOB based on the PGAS output. The accounting division needs to be properly staffed if these statements are to be prepared and the Audit Act complied with.

15. **Budgeting and Management Accounting.** The annual budget is prepared by the Consultant at CCDA based on work-plans of each division within CCDA. The 2014 Budget Submission contains detailed description of work-plans/activities for each division for which cost estimates are prepared. Therefore, it is a bottom-up approach which can be substantiated. Generally, the finance division would be in charge of sending out the budget formats / templates to the operational departments, obtaining the feedback and preparing the annual budget of the department. However, as it stands there is no staff capable of carrying this out and therefore the services of the Consultant were required. This is then submitted to the Department of Treasury for incorporation into the country's annual budget for approval in the Parliament.

16. **Internal Auditing and External Auditing.** CCDA does not have an internal auditor at present although the position has been advertised. This is an important position since the primary duty of the Internal Auditor is to ensure that proper internal controls have been designed and are in operation. Under the Public Finance Management Act, an internal auditor is required. The position of Internal Auditor has been advertised with the other positions at Grade 15 with an annual compensation of K39,882 (\$14,000).

17. The external auditor is the Auditor General of PNG. However an audit has not been carried out since the inception of CCDA due to non-availability of financial statements in suitable form for submission.

18. **Results of the Financial Management Assessment.** Overall the current status of financial management at CCDA is not of a suitable standard to implement the proposed project. The following support this conclusion;

- CCDA does not produced financial statements in a form suitable for submission to the Auditor General for the purpose of audit. Under Section 8 of the Audit Act, the Auditor General is required to report to the Minister of Finance and the relevant Minister on all financial statements furnished to him under the Public Finance Management Act. These financial statements have been defined under the Audit Act as (i) the financial operations for the period and (ii) the state of affairs at the end of that period. Therefore, an Income and Expenditure Account as well as a Balance Sheet must be submitted **by law** to the Auditor General. Since the accounting staff at CCDA do not have the capacity to produce these financial statements, the CCDA

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<sup>8</sup> MYOB is an off-the-shelf accounting package generally used for small organizations. Used widely in the PNG. Other suitable software are Quickbooks and Accpac.

Consultant has been tasked with this and the 2011 financial statements are expected to be submitted for audit when completed;

- The finance division is grossly under-staffed and under-skilled. The three staff who are in the division have no formal accounting qualifications and have been hired on a casual basis. The Accountant has been recently relieved of his duties due to incompetence. There appears to be a complete lack of financial discipline and work ethic, from basic attributes such as maintenance of a proper filing system and long absences during work hours to technical issues as elaborated below;
- The actual accounting procedures adopted contravene with the law. Under Section 24 of the Public Finance Management Act, re-allocation of expenditure within budget items is not permitted unless with the permission of the Minister of Finance. This practice is adopted on a routine basis with Journal Entries used to transfer expenditure from a budget line that has been over-committed to another budget line. Over-commitment of funds by itself attracts penalties under this Act and is also liable for disciplinary action under the Public Service General Orders for improper discharge of responsibility;
- There are several internal control weaknesses due to the lack of staff and staff without the necessary skills. Segregation of duties is a major internal control risk when operating in such an environment. In addition, (i) no bank reconciliations have been carried out since its inception (ii) payment vouchers not stamped as paid when they are paid, leading to the possibility of paying more than once (iii) payments are posted to incorrect budget items, for instance under code 121 allocated for travel and subsistence there are postings for internet expenses, under code 124 for operational materials and supplies there are payments for hire of vehicles, under code 138 allocated for training there are payments for vehicle hire, vehicle hire also appears under code 141 allotted for retirement, pensions, gratuity and many other instances. (iv) no asset management system or verification of assets;
- CCDA finance staff has no experience of handling an ADB project along with Statements of Expenditure (SOE) supporting Withdrawal Applications and managing an Imprest Account or managing procurements.

19. There have been many instances where the warrant authorization (as the draw-down of monthly appropriation is named), has been fully committed resulting in CCDA having to postpone its work plan pending the next warrant. One reason for this is that with CCDA's expanding work-plan, the budget has been understated and secondly that the Ministry's request for funds which should have been budgeted within the Ministry in the first place.

20. **Recommendations Arising from CCDA Financial Management Assessment.** There are two options to manage the proposed project. The first is to strengthen the finance division of CCDA to enable them to manage the project. The second is to create a Project Management Unit (PMU) to manage the proposed project and eventually future climate change projects. CCDA is currently experiencing difficulty in recruiting qualified and experienced staff under the existing government remuneration package. This has resulted in very weak financial management as there is no one who is capable of taking responsibility for the work of the finance division. Internal controls are also very weak and this may result in the mis-management of funds under the proposed project. Furthermore, CCDA financial information is prepared on the cash accounting basis which is entirely different to reporting requirements of the project, where a full suite of financial statements including Income and Expenditure, Balance Sheet and Cash-flow need to be prepared on the accruals accounting basis and regularly submitted for audit.

21. It is recommended that a separate Project Management Unit (PMU) is established for the purpose of the proposed project. In fact, it has been agreed with CCDA, Department of Planning and UNDP that a separate PMU be established to initially manage the funds of the proposed project fund and once proven to be a success will evolve into an operational unit of CCDA with responsibility to manage all climate change projects. These staff should ideally be recruited prior to implementation of the project to enable them to be properly trained in ADB procedures, by recruitment of a suitable Consultant and by under-studying successful ADB projects currently being implemented in PNG.