Report Number: ICRR0022783

1. Operation Information

Operation ID	Operation Name
P165717	PNG Development Policy Operation
Country	**Practice Area (Lead)**
Papua New Guinea	Macroeconomics, Trade and Investment

Non-Programmatic DPF

L/C/TF Number(s)	Closing Date (Original)	Total Financing (USD)
IDA-63110	31-Mar-2020	147,989,555.65
Bank Approval Date	**Closing Date (Actual)**	
25-Oct-2018	31-Mar-2020	

	IBRD/IDA (USD)	Co-financing (USD)
Original Commitment	150,000,000.00	0.00
Revised Commitment	150,000,000.00	0.00
Actual	147,989,555.65	0.00

Prepared by	Reviewed by	ICR Review Coordinator	Group
Shahrzad Mobasher Fard	Paul Holden	Jennifer L. Keller	IEGEC

2. Program Objectives and Pillars/Policy Areas

a. Objectives

The program objectives of the stand-alone First Economic and Fiscal Resilience Development Policy Operation were to support the Government of Papua New Guinea strengthen its fiscal management and revenue performance, and strengthen key building blocks for public financial management and financial inclusion. The project development objectives (PDOs) are identical to the program's pillars:

Objective One: Strengthen fiscal management through improvements in revenue performance.

Objective Two: Strengthen key building blocks for public financial management and financial inclusion.

b. Pillars/Policy Areas

The operation was structured around two pillars: (i) strengthening fiscal management and revenue performance; and (ii) strengthening key building blocks for public financial management and financial inclusion.

Pillar I had 4 Prior Actions (PAs) [PD, p. 8-9]

- PA1: In order to establish a medium-term fiscal anchor: (i) the Recipient's Parliament has amended its Fiscal Responsibility Act to require the fiscal strategy to target a zero average annual non-resource primary fiscal balance over the medium term; (ii) the Recipient's National Executive Council has approved a Medium Term Fiscal Strategy (MTFS) for 2018-2022 that is consistent with a zero average annual non-resource primary fiscal balance over the medium term; and (iii) the 2018 Budget presented to the Recipient's Parliament is consistent with the MTFS for 2018-2022.
- PA2: To improve revenue administration and enhance compliance: (i) the Recipient's Parliament has voted its approval of the Tax Administration Bill; (ii) the Recipient's Parliament has amended the Income Tax Act to make Taxpayer Identification Numbers mandatory; and (iii) the Recipient's Internal Revenue Commission has approved the establishment of a new Large Taxpayer Office.
- PA3: The Recipient, through the Department of Treasury and the Internal Revenue Commission, has prepared a tax expenditure statement and made it publicly available as part of the 2018 Budget.
- PA4: The Recipient has increased the excise tax on diesel in the 2018 Budget, in order to raise revenue, reduce the distortion between diesel and petroleum taxes, and reduce environmental pollution.

Pillar II had 2 PAs [PD, p. 9-10]

- PA5: The Recipient's Department of Finance has implemented the Integrated Financial Management System in national government departments, such that it is being used to record all expenditures other than trust fund expenditures.
- PA6: To support the increase in financial inclusion, the Recipient's National Executive Council has (i) approved the Financial Sector Development Strategy and the National Financial Inclusion Policy; and (ii) to increase women's financial inclusion, the Recipient, through the Bank of Papua New Guinea, has launched the Gender Equity and Social Inclusion (GESI) Policy for Microfinance Institutions

c. Comments on Program Cost, Financing and Dates

The Papua New Guinea Development Policy Operation received funding of USD 150 million from IDA. This was increased from the original amount at project approval of USD 100 million as a result of the February 2018 earthquake which led to a significant deterioration in the fiscal outlook for the country.

The program was initially designed to be a programmatic series of two operations, each of USD 100 million. The second operation was dropped due to the government's inability to lead the fiscal adjustment program that was sought under Pillar I.

The first operation was approved on October 25, 2018 and became effective on December 10, 2018. The financing was allocated in a single tranche, disbursed on December 19, 2018. The actual amount disbursed was USD 147.99 million. The difference was due to exchange rate fluctuations.

3. Relevance of Design

a. Relevance of Objectives

At the time of approval, Papua New Guinea (PNG) was navigating a period of sluggish economic growth. Annual real gross domestic product (GDP) growth had fallen from 15.4 percent in 2014 to -0.8 percent in 2018. This came largely as a result of the end of the liquefied natural gas (LNG) boom in 2014 (with large investment projects in the extractive sector ending in 2017), as well as the deterioration in the extractive sector's terms-of-trade due to softer international commodity prices. This led to a widening of the fiscal deficit and a shortage of foreign exchange. To restore fiscal balance and address current spending slippages, cuts in capital spending were initiated by the government, and the government introduced import compression policies to address the shortage in foreign exchange. This led to reduced investment and growth in the non-resource sector.
PNG's economic performance was further derailed by natural disasters. The severe drought caused by El Niño in 2015-16 led to a significant reduction in agricultural output. Later, in February 2018, Papua New Guinea was struck by a 7.5 magnitude earthquake which disrupted production and exports of the oil, gas and mining industries.

The fiscal deficits recorded in the years that preceded the operation brought PNG's debt-to-GDP ratio to exceed its medium-term target. Furthermore, the government was accumulating large expenditure arrears and payment delays, which were not reflected in the fiscal accounts and which was also cited by the private sector as one of the most important factors dampening non-resource business activity. This induced the government to introduce a supplementary budget to collect additional revenue and to reduce unproductive expenditures. While revenue collection was higher and expenditure lower than budgeted in the 2017 Supplementary Budget through measures such as the commencement of the payroll audit, the freeze on new recruitments, cessation of use of the parallel payroll system, and the migration of all government employees onto the centralized government payroll, spending controls remained weak, leading to the buildup of substantial budget arrears. By end October 2018, the government estimated that budget arrears were equivalent to 1.3 percent of GDP.

Alignment of PDOs with the Government's reform agenda. Following the 2017 elections, the government announced a 100-Day Economic Stimulus Plan, which included measures to enhance the medium-term sustainability of public finances and ensure inclusive economic growth. It also published a Medium-Term Fiscal Strategy (MTFS) and a Medium-Term Revenue Strategy (MTRS) covering the 2018-2022 period. The MTFS aimed to improve fiscal resilience by adhering to fiscal anchors to mitigate the impact of commodity price volatility on the budget. The MTRS outlined measures to modernize revenue policy and legislation and strengthen revenue administration, with the aim of reducing compliance costs and increasing tax collections. Pillar I of this operation was well aligned with Government of PNG's reform agenda.

Alignment of PDOs with the FY2019-23 CPF. The first pillar of the CPF consists of "improving macro and fiscal resilience", which features "strengthening fiscal management", including both macroeconomic management and public finance management, as its first objective. Both pillars of the DPO were closely aligned with this CPF objective. The third focus area of the CPF is "encouraging private sector growth and job creation in the non-resource sectors", under which the first objective is improving micro and SME competitiveness and access to financial services, and the third objective is deepening economic participation of women and youth. PA6 under the second pillar of the DPO was closely aligned with this CPF objective which aimed at improving the institutional environment for microfinance providers and women's access to finance.

b. Relevance of Prior Actions

Rationale

There were six PAs, with PAs 1-4 supporting Pillar 1 (strengthening fiscal management and revenue performance) and PAs 5-6 supporting Pillar 2 (strengthening key building blocks for public financial management and financial inclusion). Most of the PAs consisted of compound prior actions.

Prior Action #1 established a medium-term fiscal anchor through a zero average annual non-resource primary fiscal balance to insulate fiscal policy from resource revenue volatility. This was a relevant policy given that PNG was dependent on highly volatile resource revenues and was consistently incurring deficits in the non-resource primary fiscal balance, which led the country's public sector’s debt-to-GDP ratio to exceed the medium-term target. (Relevance of PA1=S)

Prior Action #2 on improving revenue administration and enhancing tax compliance was intended to help raise public revenues through lower tax evasion. Tax evasion was found to be prevalent in the formal sector of the economy, as well as in the informal sector of the economy which is estimated at roughly 30 percent of PNG's GDP. Moreover, the ICR notes that the 2020 Budget raised concerns about persistent weaknesses in tax administration, which have led to a compliance gap possibly worth up to PGK 3 billion, despite the significant increase of the Internal Revenue Commission (IRC) resources. The first part of the PA (Recipient's Parliament voting approval of the Tax Administration Bill) is intended to modernize, simplify and harmonize legislation relating to tax administration, allowing the reform of IRC’s systems, procedures, forms, filing, and payment mechanisms, with the simplification of tax administration ultimately leading to a reduction of taxpayer compliance costs, reducing the size of the informal economy and boosting tax revenue collection. The second part of the PA consisted in in amending the Income Tax Act to make Taxpayer Identification Numbers mandatory such that banking data and income tax records are linked, allowing the IRC to more effectively address tax evasion and reduce the informal economy by relying on third-party information, especially from banks. The third sub action under this PA on the establishment of a new Large Taxpayer Office was targeting tax compliance for large taxpayers through improved engagement, which would significant help raise public revenues given that 20 percent of taxpayers contribute 80 percent of tax revenue in PNG. . Since there is a credible causal chain linking PA2 to the overarching objective of strengthening fiscal management and revenue performance, the relevance of this PA is rated satisfactory. (Relevance of PA2=S)

Prior Action #3 on preparing a Tax Expenditure Statement (TES) and making it publicly available as part of the 2018 Budget was intended to reduce tax expenditures by enhancing transparency about their size and allocation. With regard to the magnitude of foregone revenues captured in the TES, the ICR indicates that the estimated total tax exemptions in 2018 were equivalent to 3.8 percent of total tax revenue. Table 1 presents a breakdown of foregone tax revenue in 2018 by tax measure. The ICR indicates that the 2019 Budget expanded the coverage of the TES by capturing additional tax incentives provided in the Income Tax Act, GST Act and the Customs Tariff Act. While the preparation of a TES is an important step in drawing attention to the magnitude of exemptions granted and does contribute to an improvement in fiscal management, it does not itself reduce tax expenditures, and does not therefore directly enhance revenue performance. Indicative trigger 3 under the program consisted in the Recipient's Department of Treasury completing a review of tax incentives, with recommendations following the review being tabled at the Recipient's National Executive Council, which would have constituted the next step toward reducing tax expenditures. PA3 is therefore rated moderately satisfactory (Relevance of PA3=MS)

Table 1: PNG's Tax Expenditure by Tax Measure, 2018

	Income tax	GST	Excise and customs taxes	Total revenue foregone
In % of revenue collected from each tax	1.9	4.2	17.0	n.a.
In % of total tax revenue	1.1	1.4	1.3	3.8

Source: ICR.

Prior Action #4 on the increase in the excise tariff on diesel in the 2018 Budget was intended to raise revenue, reduce the distortion between diesel and petroleum taxes, and reduce environmental pollution. The program allowed the diesel excise tariff to be increased from PGK 0.10/lt to PGK 0.23/lt on January 1, 2018.There were no indicative triggers for subsequent increases, with the ICR noting that authorities had committed to raising the diesel tax every two years. Since the ICR document does not provide estimates of the anticipated increase in revenues from the excise tariff on diesel and the program did not include indicative triggers on subsequent tariff increase, PA4 is rated as moderately unsatisfactory. (relevance of PA4=MU)

Prior Action #5 on implementing an Integrated Financial Management System (IFMS) in national government departments to record all expenditures other than trust fund expenditures is an important step to ensure the transparency and accountability of public spending as it includes a comprehensive range of control mechanisms in the payment process module of IFMS, with access being restricted and changes being recorded, which would result in an audit trail. . This PA is anchored on the findings of the Public Expenditure and Financial Accountability (PEFA) 2015 report, which framed the PEFA Roadmap 2015-2018. Only three government departments (i.e., Treasury, Finance, and National Planning and Monitoring) were connected to the IFMS in 2014. With PA5, all 37 national departments would be connected to the IFMS. Moreover, the ICR indicates that this has been rolled out in seven out of nine Statutory Authorities of the first phase (i.e., IRC, Ombudsman Commission, National Museum and Arts, Customs, Immigration and Citizenship Services, Auditor General Office, Science and Technology Commission). The ICR reports that a The relevance of this PA is rated as satisfactory. (relevance of PA5=S)

Prior Action #6 drew on the PNG's Financial Development Strategy prepared by the World Bank in 2014. Approving the Financial Sector Development Strategy and the National Financial Inclusion Policy consisted in: (i) expansion of digital financial services as a key to promoting financial inclusion in remote communities; (ii) provision of inclusive insurance for the protection of low-income people; (iii) financial consumer protection to level the playing field between suppliers and consumers of financial products and services; (iv) promoting access to finance for informal and agricultural enterprises; and (v) promoting financing of SMEs. The second measure on launching the Gender Equity and Social Inclusion Policy for Microfinance Institutions included measures to: (i) remove barriers to the employment and promotion of women within microfinance institutions; (ii) design products and services to fit the needs of women customers; and (iii) change the way microfinance institutions engage with women customers. While the policies featured under PA6 are highly relevant to greater financial inclusion, the interventions are too broadly defined and it is not clear as to how the government would engage with the banking and insurance sectors in order to allow these policies to be accomplished . (relevance of PA6=HU)

Rating

Moderately Satisfactory

4. Relevance of Results Indicators

Rationale

Pillar 1 (Strengthening fiscal management and revenue performance) had two results indicators (RIs), with RI linked to PA1 and R2 linked to PA2, PA3 and PA4. Pillar 2 (Strengthening key building blocks for public financial management and financial inclusion) had three RIs, with RI3 associated with PA5, and RI4 and RI5 linked to PA6. (Table 2)

Table 2: Association of Result Indicators to Prior Actions, and Baseline, Targeted and Actual Values of Results Indicators

RIs	Associated PA(s)	Baseline (including date)	Target (including date)	Value as of target date	Most recent value available
Pillar 1: Strengthening fiscal management and revenue performance					
RI1: The non-resource primary fiscal balance as a percentage of non-resource GDP improves	PA1, PA2, PA4	-4.7 percent (2016)	-0.9 percent (2020)	Actual (2020): -9.4 percent	
RI2: Tax buoyancy (i.e., tax revenue as a share of GDP) increases	PA2, PA3, PA4	14.2 percent of GDP (12.9 percent—revised) (2016)	14.6 percent of GDP (13.3 percent—revised) (2020)	Actual (2020): 12 percent	
Pillar 2: Strengthening key building blocks for public financial management and financial inclusion					
RI3: Accountability and	PA5	Statements	Statements	Actual (June	

transparency in the use of public funds is improved through the timely submission of the annual financial statements to the Auditor General's Office		submitted at least 12 months after the end of each fiscal year (2014-2016)	submitted within three months of the end of each fiscal year (2018-2020)	2021): Statements for 2019 and 2020 not yet submitted to the Auditor General's Office	
RI4: Financial inclusion increases, as indicated by the percentage of adults with an account at a formal financial institution	PA6	36.96 percent (June 2016)	≥ 50 percent (June 2020)	Actual (2020-Q2): 63.8 percent	
RI5: The gender gap in new bank account establishment declines	PA6	26 percent of the new bank accounts established in 2013-2016 were by women (2016)	≥ 35 percent of the new bank accounts established in 2016-2020 are by women (2020)	No publicly available data for 2020	32 percent (2019)

RI1 is reflecting the outcome of PA1, PA2 and PA4 by establishing a target for the non-resource primary fiscal balance expressed as a percentage of non-resource GDP. PA1 amended the Fiscal Responsibility Act to require the country's fiscal strategy to target a zero average non-resource primary fiscal balance over the medium-term, which would be approved by the Recipient's National Executive Council and which would be reflected in the 2018 Budget presented to Parliament. PA2 allowed for a reduction in tax evasion and of the informal economy in order to boost public revenues by modernizing and simplifying tax administration, the introduction of Taxpayer Identification Numbers linking taxpayer and banking information for third-party verification, and a closer engagement with large taxpayers through the establishment of the Large Taxpayer Office. RI1 was envisaging a decline of this ratio from a baseline of -4.7 percent in 2016 to a target of -0.9 percent in 2020. It would have been, however, appropriate to adopt a more disaggregated approach to assessing the impact of each of the three PAs for this RI, by considering, for example, the revenue collected by the Large Taxpayer Office. (relevance of RI1=S)

RI2 (associated to PA2, PA4 and PA4) is targeting an improvement in tax buoyancy (i.e., tax revenue as a share of GDP) from a baseline of 14.2 percent of GDP in 2016 (revised to 12.9 percent of GDP) to 14.6 percent of GDP (revised to 13.3 percent of GDP), which would be an effective increase of 0.4 percent of GDP. Based on the PAs featured in the program, increased tax buoyancy is expected to be achieved through a reduction in tax evasion avoidance from Taxpayer Identification Numbers, the creation of the Large Taxpayer Office, the increase on the excise on diesel and potentially, a reduction in tax expenditures. While RI2 would measure progress toward the achievement of the objective along the results chain, it is not a well targeted measure for PA3 and PA4. A better targeted RI for PA4, for example, could focus on revenues from fuel taxes specifically. The ICR does not specify how the target was established. The ICR also notes numerous factors for why the target for RI2 was not achieved which, by itself, suggests that this indicator was not the appropriate measure for assessing the outcome of PA2 to which it was linked. (relevance of RI2=MS)

RI1 and RI2 were well aligned with the RIs featured in the CPF of improving non-resource primary balance as a share of non-resource GDP and increasing non-resource tax revenue as a share of GDP.

RI3 relates to the timely submission of annual financial statements to the Auditor General's Office, from statements submitted with a delay of at least 12 months after the end of each fiscal year under the 2014-2016 baseline, to statements submitted within three months of the end of each fiscal year as the target in 2018-2020. Although the timely submission of annual financial statements to the Auditor General's Office is important, an alternative indicator, such as, for example, the share of expenditures covered by IFMS would have been much better and closer along the results chain which would help satisfy the overarching objective of strengthening public financial management. RI3 is well aligned with the RI featured in the CPF of improving accountability and transparency in the use of public funds through the timely submission of annual financial statements to the Auditor General's Office. (relevance of RI3=U)

RI4 and RI5 are associated with PA6 to increase financial inclusion. RI4 targets the share of the adult population with an account at a formal financial institution, from a baseline of 36.96 percent in June 2016 to more than 50 percent in June 2020. RI5 relates to the share of new bank accounts for the female adult population, with the baseline at 26 percent over the 2013-2016 period and the target at more than 35 percent over the 2016-2020 period. Since RI4 and RI5 do not isolate the effect of PA6 on promoting financial inclusion and are solely limited to the creation of bank accounts rather than access, usage and the quality of services offered to those who are under-represented, they remain imperfect. There are a number of factors beyond the scope of this program which may have contributed to financial inclusiveness and as such, the RIs do not allow us to delineate the impact of PA6 relative to other factors. (relevance of RI4=U, relevance of RI5=U)

Rating

Moderately Unsatisfactory

5. Achievement of Objectives (Efficacy)

OBJECTIVE 1

Objective

Strengthen fiscal management through improvements in revenue performance.
Supported by PAs 1-4
Progress measured by RIs 1-2

Rationale

Outcomes. The program did not meet two of three targets which were established. RI1 on achieving a non-resource primary fiscal balance as a percentage of non-resource GDP of 0 was not at all met and is rated as Negligible. Similarly, RI2 on increasing tax buoyancy was not met, with the target being also assessed as being inadequate to measure performance, and is rated as Negligible.

The actual outcome on RI1 suggests a significant deteriorating performance in the non-resource primary balance at -9.4 percent in 2020. PA1 triggered a huge imbalance in spending, with a very large increase in the public sector wage bill being offset by an enormous decline in capital spending. Indeed, much of the fiscal adjustment came in the form of reduced capital spending, which fell by 75 percent, while current spending, notably, the public sector wage bill and interest payments rose by 116 percent and 63 percent, respectively, between 2014 and 2017. As reported in the ICR, “the significant increase in the public sector wage bill reflected the limited effectiveness of payroll monitoring and control” and “interest payments rose because of the increasing level and servicing cost of domestic debt”. And while the budget deficit improved from -4.6 percent of GDP in 2014 to -2.5 percent of GDP in 2017, it was in part achieved through the accumulation of budget arrears in 2017 (which continued during the 2018 fiscal year).

The ICR also documents a series of unexpected factors that led to this outcome. First, there was an unbudgeted annual increase in the public sector wage bill by 3 percent increase in 2017 and 2018. Second, the change in administration in 2019 revealed substantial revenue shortfalls (PGK 1 billion in 2019), budget arrears accumulated by the previous administration (PGK 120 million to public servants and of PGK 521 million to other service providers), and arrears in public service exit payments (PGK 2 billion). The payment of budget arrears in 2019 and 2020 led to a widening in the fiscal deficits and higher debt-to-GDP ratios. While the government introduced revenue-enhancing measures in the 2020 budget to improve the unfavorable fiscal and debt performance, including, through higher excises on alcohol and cigarettes and higher levies in the telecommunication and banking sectors, the non-resource primary balance was still projected, at -5.9 percent in 2020 before the pandemic, or -4.3 percent excluding budget arrears, well below the -0.9 percent result indicator target associated with PA1. The COVID-19 pandemic, which significantly weakened external and domestic demand for goods and services, led to a real GDP contraction of 3.9 percent in 2020, and widened the fiscal deficit. Against this backdrop, the non-resource primary balance deteriorated to -9.4 percent of non-resource GDP in 2020.

PA2 sought to improve revenue administration and enhance compliance in order to reduce the size of the informal economy and raise tax revenues.. While the Tax Administration Act (TAA) was expected to go into effect on January 1, 2020, to modernize, simplify and harmonize legislation relating to tax administration and ensure efficient collection, a number of the provisions of the Act needed to be amended. Furthermore, awareness needed to be raised and IRC’s systems needed to be updated to reflect provisions of the TAA, which were facilitated by the establishment of the TAA working group. To this date, the TAA has not become effective as there were significant delays in rewriting certain provisions of it, which in turn, have delayed the updating of the IRC’s systems.

With regard to the second measure on making Taxpayer Identification Numbers (TIN) mandatory, the ICR indicated that the TIN was rolled out, with a unique TIN being automatically generated by the Standards Integrated Tax Administration System following registration, and that taxpayers can be registered for various accounts based on tax type, often based on IRC's recommendation, with each account holding a distinct number. Moreover, it pointed to the fact that all accounts were linked to the taxpayers' registration information and that third-party information was used in IRC risk assessments mainly based on banking sources. Finally, the ICR indicated that the TIN was required for opening business bank accounts. The ICR also pointed to a number of weaknesses with the design of the TIN, in particular as it relates to the integrity of the information held in the registration database. A review through the Tax Administration Diagnostic Assessment Tool (TADAT), revealed key IT system design weaknesses that affect compliance management and the security of the taxpayer register. These included: (i) the absence of an audit trail of user access and changes in taxpayer registration information; (ii) no online access for taxpayers; (iii) no connection between the accounts of associated entities; (iv) the absence of a self-validating mechanism in the TIN; (v) no classification of sole traders by sector; and (vi) no interface with other IT systems to support the registration process. According to the assessment, critical taxpayer background information, such as contact details, is missing or outdated. A March 2019 Internal Revenue Commission internal audit report highlighted significant concerns about the accuracy of the registration database, including incorrect registrations and opening of accounts, multiple accounts, duplicates and inactive taxpayers. The TADAT score on the indicator of "Knowledge of the potential taxpayer base" was C, indicating "weak performance relative to international good practice".

The ICR reports that the Large Taxpayers Office (LTO) has been operational since October 2018, with 19 account managers and 11 audit officers auditing 170 large taxpayers by the end of 2019 across sectors, such as finance/banking, construction and extractives. The ICR reports that the TADAT assessment revealed that the LTO audits are generally limited to the verification of supporting documents and that indirect audit methods to verify amounts being reported are rarely used. The low efficacy for this measure is assessed to be linked to the PA itself which established the LTO, but did not create the mandate for audit officers to rely on indirect audit methods to verify amounts being reported. The results chain was well thought of with two of the three measures under Indicative trigger 2 on completing the first phase of the compliance strategy for data matching between banking data and income tax records to identify business accounts with and without

TINs, and developing and implementing the Standard Operational Procedural Manual for the IRC's new risk-based audit referral tool being met.

RI2 on raising tax revenue to 13.3 percent of GDP was not met, with the ratio falling to 12 percent of GDP in 2020 from a baseline of 12.9 percent of GDP at end of 2016. Much of the improvement in tax buoyancy was expected to be made through increased tax compliance. The ICR indicates that despite the disruptions caused by the COVID-19 pandemic, 16 internal audits were completed and 27 fraud and corruption investigations were completed. The ICR does not provide a comparison on the number of internal audits, and fraud and corruption investigations, prior to the implementation of PA2 which would be critical in order to assess the impact of these measures. Moreover, the ICR does not provide any information on the additional number of taxpayers reporting revenue to the Internal Revenue Commission, nor does it report any figures on the average additional taxes paid by taxpayer by level of revenue reported. In order to appropriately assess efficacy, it would have been advisable for the task team to consider result indicators such as the number of taxpayers, average taxes paid per taxpayer by level of revenue, and the percentage increase in taxes collected following audits prior and after the implementation of PA2.

PA3 on preparing tax expenditure statements and making them public was achieved on time. However, it has not led to a reduction in tax expenditures by the time of project completion. Indicative Trigger 3 was intended to complete a review of tax incentives, with the recommendations of the review being tabled at the Recipient's National Executive Council. Although RI2 was associated to the achievement of PA3, it was not a well targeted measure for the progress toward the achievement of the objective along the results chain.

PA4 sought to increase the excise tax on diesel consumption in order to raise revenue. The ICR indicates that tax revenue from inland excise taxes increased from 1 percent of GDP in 2017 to 1.3 percent of GDP in 2019 mainly as a result of this measure. Although RI2 was associated to the achievement of PA4, it was not a well targeted measure for the progress toward the achievement of the objective along the results chain. In order to assess the impact of this PA, it would have been critical to include a result indicator, with a target which would allow to assess the magnitude of the increase in revenue from fuel taxes relative to the baseline figure. The ICR also indicates that while the government was initially committed to increasing the excise tariff for diesel incrementally by PGK 0.13/lt every two years over the medium-term until the distortion between petroleum and diesel excise tariffs was eliminated, additional increases have so far failed to materialize. Incremental increases on the excise tax on diesel consumption could have been supported by the inclusion of triggers, which the task team failed to incorporate in the program. Since the PA, which was intended to contribute to improved revenue performance by reducing the distortion between diesel and petroleum taxes, was only partially met with only one incremental increase of what was intended to be a series of excise tariff hikes, the achievement of this objective was not met.

In all, the non-resource primary balance deficit ballooned, the Tax Administration Act did not become effective and raising taxes in proportion to GDP did not happen.

The achievement of the first objective is judged to be Highly Unsatisfactory.

Rating

Highly Unsatisfactory

OBJECTIVE 2

Objective

Strengthen key building blocks for public financial management and financial inclusion.
Supported by PAs 5-6
Progress measured by RIs 3-5

Rationale

Outcomes. R3 on the timely submission of financial statements to the Auditor General's Office in order to raise transparency and accountability was not met and its achievement is rated as Negligible. While RI4 on the percentage of adults with an account at a formal financial institution was met, the indicator did not isolate the impact that can be directly attributed to PA6 and as such, is rated as Modest. RI5 not only did not isolate the impact that can be directly attributed to PA6, but also lacked data provision to measure the outcome achieved in 2020, and is therefore rated as Negligible.

The achievement of the second objective is judged to be Highly Unsatisfactory.

Rating

Highly Unsatisfactory

Overall Achievement of Objectives (Efficacy)

Rationale

The first objective is judged to be achieved at a level that is Highly Unsatisfactory. The second objective is judged to be achieved at a Highly Unsatisfactory level. Overall efficacy is judged to be Highly Unsatisfactory.

Overall Efficacy Rating

Highly Unsatisfactory

6. Outcome

Rationale

The relevance of prior actions (design) was rated Moderately Satisfactory, and the achievement of objectives was rated Highly Unsatisfactory. This leads to an overall outcome rating of Highly Unsatisfactory. Many of the prior actions were necessary conditions to meeting the objectives of the program, but they were either not well defined or complementary conditions to meet these objectives were not addressed. RIs only partially measured the impact of the PAs on progress toward the achievement of the targeted outcomes and their links to the program objectives were unclear in some instances. PA3 and P4 did not have RIs associated with them which did not allow to measure progress toward the achievement of the objectives. RI5 had no publicly available data available at the completion of the program.

a. Rating

Highly Unsatisfactory

7. Risk to Development Outcome

The ICRR concurs with the risks identified in the ICR:

1. **Political and governance risks are high.** Successful motions of no confidence in the government are relatively frequent, and governing coalitions do not tend to be based on clear programmatic policy platforms, so the policy environment can be quite unpredictable. The upcoming national elections in 2022 will be another test of this. As a result, there is a high risk that the policy reforms supported by the DPO may not be maintained sufficiently to yield the expected outcomes. In particular, government plans for implementing fiscal consolidation measures may be undermined by the volatile political environment, which may not be conducive to implementing revenue reforms and restraining unproductive expenditure.
2. **Macroeconomic risks are high.** PNG faces a number of significant risks to the macroeconomic outlook—i.e., weak economic growth and large public finance imbalance, which could lead to an overshooting of public debt above its medium-term target—that, if realized, would constrain fiscal space and place pressure on containing the fiscal deficit and keeping public debt on a sustainable trajectory. These risks include a larger and persistent adverse COVID-19 impact on the economy than currently projected, lack of progress on major resource projects under the expected timetable, or deterioration in global commodity prices. The eventual impact of COVID-19 is still unknown, but it may adversely affect medium-term growth prospects of the economy. Macroeconomic risks are mitigated by ongoing IMF dialogue and monitoring under the Staff-Monitored Program and associated macroeconomic policy dialogue with all development partners, including the World Bank's own policy dialogue and monitoring under the Sustainable Development Finance Policy.
3. **Institutional capacity for implementation poses a substantial risk to the sustainability of results.** While there are segments of strong capacity in particular institutions within the government, capacity is relatively thin across the board, which poses a specific risk to the achievement of the sustainability of results from policy reforms that depend on institutional capacity, particularly in tax administration and PFM. The ICRR finds, however, that the technical assistance provided by the World Bank, along with the lack of coordinated efforts with other development partners, pose a significant risk to the ultimate achievement of the objectives sought by this program.

8. Assessment of Bank Performance

a. Bank Performance – Design

Rationale

While the project's objectives were clear and focused, the PAs were not focused enough and the RIs were poorly defined. PA1 was relevant in order to decouple fiscal policy from resource revenue volatility. PAs 2, 3, 5 and 6's analytical underpinnings were based on the World Bank's 2017 Systematic Country Diagnostic, the PNG Economic Update, PEFA 2015, and the PNG Financial Development Strategy prepared by the World Bank in 2014, but the PAs did not articulate the specific conditions required in order to allow for a credible causal chain between prior actions and objectives.

The result indicators did not adequately capture the achievement of the objectives and some were too high level to accurately reflect the impact of PAs.

The program design also failed to take into account the capacity of the government to implement reforms given the challenging political environment and low technical capacity it was confronted with. The PAD concluded that “despite risks to the outlook, the macroeconomic policy framework is deemed adequate for this operation, based on the policy commitments provided by the authorities”.

The PAD also indicated that "the IMF is providing technical assistance to GoPNG in several areas of relevance to the Bank’s DPO, particularly in support of monetary and exchange rate policy reforms and improved revenue performance. Australia’s Department of Foreign Affairs and Trade (DFAT), through the PNG Governance Facility (PGF), also provides technical assistance to GoPNG in areas of relevance to the World Bank’s DPO, particularly in support of the implementation of the PEFA Road Map 2015-2018”. There was a lack of coordination between the World Bank and these other development partners given that the technical assistance did not result in the achievement of the objectives sought by the program under PA1, PA2, PA3, PA5 and PA6. It appears that the technical requirements of some of the reforms were not well understood at the outset.

There was also a lack of provision to collect data on some RIs.

Rating

Unsatisfactory

b. Bank Performance – Implementation

Rationale

The ICR states that "the implementation of the program was supposed to benefit from the Asian Development Bank's (ADB) policy-based lending operation on strengthening procurement, planning, budgeting, funds flows, accounting and reporting. The World Bank also collaborated closely with the IMF, which provided technical assistance in areas such as revenue performance. The World Bank also coordinated with Australia's Department of Foreign Affairs and Trade, through the PNG Governance Facility, which provided technical assistance to the implementation of the PEFA Road Map 2015-2018.".

The ICR states that "during program implementation, starting from the PNG Economic Update of June 2019, the World Bank pointed to the widening of the NRPB and the associated deviation from the fiscal-consolidation path. The task team notably highlighted the difficulties in controlling the wage bill and the need to improve the realism of the budget. The January 2020 PNG Economic Update pointed to the lack of ambition of the new fiscal consolidation strategy. The Implementation Status and Results Report (ISR) of the DPO released on February 2020 acknowledged that the expected improvement in the NRPB and tax buoyancy did not look on track to occur in 2020."

The Bank continued to provide technical assistance in important areas of domestic revenue mobilization, specifically as it pertained to the adoption of a methodology for improving the comprehensiveness of tax expenditure statements over time. This technical assistance was, however, insufficient to meet the overarching objective of strengthening fiscal management and revenue performance without any measure to effectively reduce these tax expenditures.

It is clear from the ICR document that the team brought issues with regard to the implementation of the program to the authorities' attention on numerous occasions, but that the government was not in position to initiate the measures required to achieve the targets which were established prior to the program's approval. Given the challenging political environment, which were out of the task team's control, the Bank's performance with regard to implementation is rated as Moderately Satisfactory.

Rating

Moderately Satisfactory

c. Overall Bank Performance

Rationale

The overall rating for Bank performance is judged to be Moderately Unsatisfactory. There were shortcomings in the design of the operation. The PAs did not consider the technical requirements of the measures within the context of the relatively low implementation capacity of the government. The RIs were not well formulated in order to be able to assess the impact of the measures featured under the PAs, and there was a lack of provision for gathering data. The assessment of risks and complementary interventions, such as technical assistance, to ensure the full impact of PAs on the objective were not properly considered. Meanwhile, the challenging political environment constituted a critical constraint to the achievement of the objectives which were laid out in this program.

Overall Bank Performance Rating

Moderately Unsatisfactory

9. Other Impacts

a. Social and Poverty

The ICR does not identify any social and poverty impact linked to the PAs.

b. Environmental

The report does not identify any environmental impact from the PAs.

c. Gender

The report does not identify any gender impacts from the PAs.

d. Other

None identified.

10. Quality of ICR

Rationale

The ICR is candid about the program's shortcomings in achieving the development objectives. It lays out well the country context prior to the approval of the program. It fails to provide a clear and credible explanation of the causal chain between the design of prior actions and actual outcomes, however. The discussion on prior actions and their rationale is at times incomplete in the details provided. The presentation on the achievement and results framework does not provide a clear linkage between prior actions and the development objectives which are sought. The reassessment of risks to development outcomes is candid. The quality of the ICR is rated Modest.

a. Rating

Modest

11. Ratings

Ratings	ICR	IEG	Reason for Disagreement/Comments

Outcome	Unsatisfactory	Highly Unsatisfactory	The difference in outcome rating stems from the difference in the assessed efficacy rating, which was judged to be HU by IEG while the ICR task team rated it as U. IEG's HU rating stems from the fact that the achievement of RI1 and RI2 under Pillar 1 are rated as Negligible, leading to a HU rating, while RI3, RI4 and RI5 under Pillar 2 are rated as Negligible, Modest and Negligible, respectively, leading to a HU rating.
Bank Performance	Moderately Satisfactory	Moderately Unsatisfactory	The Bank's performance on design is rated as Unsatisfactory as he PAs were not focused enough and the RIs were poorly defined, and the Bank failed to consider the government's capacity to implement reforms against a low technical capacity backdrop. The Bank's performance on implementation is rated as Moderately Satisfactory in recognition of the challenging political environment the country was confronted with for implementing reforms.
Relevance of Results Indicators	---	Moderately Unsatisfactory	
Quality of ICR	---	Modest	

12. Lessons

The review concurs with one of the lessons drawn from the ICR (pp. 29-30), with some adaptation. Other lessons are excessively general and do not lend themselves to a behavioral response on the part of Bank staff to improve outcomes going forward.

1. The implementation experience suggests that policy actions must be combined with adequate capacity building in order to achieve the intended outcome, and that an assessment of implementation capacity is required to gauge the scope of reforms prior to engaging in an ambitious program. In the case of PNG, there was inadequate understanding of or attention to the many obstacles that would be faced in pursuing the reforms supported by the operation.

The review judges that the program was overly ambitious relative to the capacity of the government to initiate these reforms, and that there was a lack of clarity on the results chain that would need to occur to have lasting impact. These shortcomings constituted the main impediments to the achievement of the PDOs which were sought.

13. Project Performance Assessment Report (PPAR) Recommended?

No