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PAPUA NEW GUINEA'S DRIVE TO  
PROMOTE MICRO, SMALL AND  
MEDIUM ENTERPRISES:  
CORRUPTION IN THE PUBLIC  
SECTOR MUST BE TACKLED

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## Key Points

- Micro, Small and Medium Enterprises (MSMEs) have the potential to contribute significantly to Papua New Guinea's economy.
- Corruption in the public sector of Papua New Guinea (PNG) restricts the ease of doing business in MSMEs.
- Corruption in the public sector contributes to the loss of government revenue that would have accrued to it from taxes paid by MSMEs.
- Medium-sized enterprises benefit from corruption, whereas micro and small enterprises are disadvantaged.
- Corruption can be tackled by improving the quality of governance in PNG and by increasing the penalty associated with corrupt practices.
- Corruption can also be tackled by increasing the capacity of anti-corruption agencies and by providing public awareness on the negative effects of corruption on PNG's economy.

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## PAPUA NEW GUINEA'S DRIVE TO PROMOTE MICRO, SMALL AND MEDIUM ENTERPRISES: CORRUPTION IN THE PUBLIC SECTOR MUST BE TACKLED

By Eugene E. Ezebilo and Francis Odhuno

Micro, Small and Medium Enterprises (MSMEs) provide jobs for many people and contribute significantly to Papua New Guinea's economy. However, corruption in the public sector is believed to be one of the major barriers to doing business in the country. This paper focuses on one of the findings from a recent article by Kavan et al. (2019) concerning the impact of public sector corruption on MSMEs in Papua New Guinea (PNG). The study was based on MSMEs managers' and owners' perceived impact of corruption on employment growth in their firms, using data from a nation-wide survey of SMEs conducted by Tebbutt Research (2014). It was reported that only medium-size firms appear to benefit from corruption in the public sector. This is likely because they have more money to give corrupt public servants who demand bribes whereas micro and small firms do not have money to bribe them. This often restricts micro and small firms from doing business. In this paper, emphasis is placed on the potential strategies that could be used to tackle corruption in the public sector. If the intention of the State is to tackle corruption, it should improve the quality of governance, reduce bureaucracy in the public sector, increase the penalty for engaging in corrupt practices, provide rewards to people who discourage corrupt practices and expand the capacity of government agencies that are responsible for tackling corrupt practices.

### What are Micro, Small and Medium Enterprises (MSMEs)?

The term MSMEs describes the size of firms in relation to the size of business they do in terms of their number of employees, gross turnover and the value of assets owned by the firms. According to the Department of Trade, Commerce and Industry (2016) classification, the number of employees in relation to MSMEs is the following:

- Micro enterprises are firms that have fewer than five employees.

- Small enterprises are firms that have five to 19 employees. However, for firms in labour intensive sectors such as agriculture, forestry and fisheries, it ranges from five to 39 employees.
- Medium enterprises in the manufacturing, engineering and construction sector should have 20 to 99 employees, and in the agriculture, forestry and fisheries sector, 40 to 99 employees.

### Types of corruption

According to Gupta and Abed (2002), corruption is the abuse of public office for private gain. It is primarily an issue associated with governance, which is linked to a failure of institutions and a lack of capacity to manage society by means of a framework of social, judicial, political and economic checks and balances. Corruption arises from the summation of myriads of interactions at micro and macro levels. The costs and benefits associated with corruption emanate from the interactions between different economic agents such as a company's manager and government officials. In PNG, some people perceive corruption as being connected to the State and others are worried about corruption that involves non-State actors as well as cultural decay (Walton, 2015). Corruption can be classified into three main types as the following:

*Rule-bending.* This involves the abuse of public office for private gain within the limits of the existing regulations. It results in providing the briber with preferential treatment or the interpretation of certain regulations without the corrupt party operating outside its legal boundaries.

*Rule-breaking/administrative corruption.* This entails the violation of legal rules, which might include fraud and extortion of money from unsuspecting people. It is the most common type of corruption.

*State-capture.* This involves the changing of existing rules and regulations to favour the corruptor's interests. For example, managers of a rich multinational company could bribe public sector officials to develop and implement policy that favours the activities of the company.

### Is corruption bad or good for businesses?

There has been a perception from different parts of the world that corruption in the public sector is either good or bad for businesses. There has been a general consensus that corruption serves as grease to make public sector systems work well in countries that have poor governance and strong institutional barriers. It has the potential of functioning as “speed money” by enabling investors to avoid bureaucratic delay. For example, a company manager who receives a licence quickly because of corruption might see it as positive. On the other hand, corruption is perceived as a barrier for businesses in countries that have good governance and effective government institutions. This has resulted in two classes of the perceptions of the impact of corruption to businesses namely: (i) Corruption in the public sector is a barrier to businesses; and (ii) Corruption in the public sector is beneficial to businesses.

### Corruption in the public sector is a barrier to businesses

Some of the potential reasons that make corruption serve as a barrier to doing business are the following:

*Corruption is often an impediment to economic growth.* Corruption restricts economic development, reduces investors’ willingness to invest and restricts foreign direct investment. Firms that engage in payments to corrupt public officials often find that it results in a stunted growth in their businesses, which has adverse effects on the firm’s investment. Bribery also places huge burdens on firms because it weakens their ability to grow, which discourages them to do business.

*Corruption results in the loss of government revenue.* The revenue that would have accrued to the government through tax is diverted by corrupt government officials, which makes it difficult for the government to be able to provide adequate infrastructure and services needed for businesses to thrive.

*Payment of bribes to corrupt government officials diminishes profit from businesses.* Bribery contributes to the cost of doing business, which reduces the profit margin made from investment. As profit margin continues to contract as a result of bribery, business owners might be discouraged from doing business in that country.

*Corruption has adverse effects on the performance of businesses.* An environment characterised by corruption has an adverse effect on firm efficiency and lowers their performance. This is because the money that business owners would have used for research and to acquire more efficient technologies is depleted by the payment of bribes to corrupt

government officials. For this reason, less productive firms are likely to engage in bribery.

*Corruption results in the production of poor quality goods and services.* Since government officials whose responsibility it is to see that minimum quality standards are met are more interested in collecting bribes than carrying out their primary responsibilities, enterprise owners might not have the incentive to provide quality goods and services. This is one of the reasons that corruption in the construction industry often results in the construction of poor quality infrastructure.

### Corruption in the public sector is beneficial to businesses

Some potential reasons that corruption in public sector appears to be beneficial to businesses are the following:

*Corruption assists business managers to avoid bureaucratic delays in the public sector.* The bureaucracy in the public sector often results in delay in the delivery of services. Therefore, to reduce costs associated with delays, some business managers pay some public officials to enable them access services quickly. Thus, the money paid to corrupt public officials is seen as “speed money”; that is, money paid to avoid delay in provision of services to the corrupter. For this reason, a company manager that receives a licence quickly by bribing public officials might see corruption as a positive practice.

*Corrupt practices might result in an increase in profit from businesses because tax is either not paid at all or only a small portion of it is paid.* Corruption in the public sector provides firm managers with an incentive to make payments to corrupt public officials that allow the managers to either not pay tax at all or pay far less than the appropriate tax. Paying less or no tax leaves big profit margins for the firms, which could be used to expand businesses and thus result in an increase in growth of businesses.

*Corruption in the public sector provides corrupt firms with the opportunity to win government contracts.* This has the potential to assist corrupt firms to win tenders for government contracts, which increases their revenue compared to non-corrupt firms.

*Corruption provides corrupt firms with the incentive to deliver poor quality goods and services while making huge profits.* Public officers who take bribes are not likely to assess the quality of goods and services delivered by corrupt firms. This could be one of the reasons that some construction firms provide poor quality paved roads without being held responsible by government officials.

## Potential policy interventions to tackle corruption

Corrupt practices in the public sector are strongly linked to the loss of revenue that would have accrued to the government from tax. The loss of government revenue as a result of corruption restricts the government's ability to provide the infrastructure and services required to ease doing business in PNG. This could be one of the reasons that the country has often performed poorly in 'ease of doing business index'. For example, PNG ranked 141 out of 190 countries in 2014 and ranked 108 in 2018 (Trading Economics, 2018). This indicates that there are several impediments such as bureaucracy, inadequate capacity and poor government institutions that restrict proper functioning of the public sector in the country.

In order to tackle corruption in the public sector, the government could consider the following:

- *Support programs that promote public awareness on the cost of corruption to PNG's economy.* This could be achieved by raising public awareness through advertisement campaigns associated with the costs of corruption. This has the potential of promoting the correction of the imperfections in public institutions by correcting the information asymmetry between formal and informal institutions that generate corruption.
- *Improve the quality of governance in the country.* This could be achieved by promoting impartiality in implementing the rule of law in all cases, so that offenders are prosecuted without fear or favour.
- *Increase the capacity of government agencies for effective and efficient service delivery.* Increase capacity of formal institutions by employing competent personnel and training of the existing ones.
- *Increase the risks of being caught and the penalty associated with the engagement in corrupt practices.* This has the potential of restricting people from engaging in the practices.
- *Provide reward mechanisms for people and corporate bodies that engage in anti-corruption practices.* Incentives could be introduced to enhance the benefits of not engaging in corrupt practices. Identities of whistle-blowers should be held in confidence and protected.
- *Expand the capacity of government agencies whose responsibilities are to tackle corruption.* The Ombudsman Commission is one such agency.

They should be adequately funded and their staff well remunerated.

## Concluding remarks

The general perception of owners and managers of MSMEs in PNG is that corruption in the public sector is a significant constraint to the performance of their businesses. However, our research revealed that micro and small enterprises are likely to be disadvantaged by endemic corruption in the public sector, whereas medium-size firms could be benefiting from it. Generally, corrupt practices in the public sector often result in loss of revenue that government would have used to provide the enabling environment such as infrastructure and services for businesses of all sizes to thrive. So, corruption in public sector must be tackled in order to provide a level-playing field for firms of all sizes to do business in PNG.

To promote ease of doing business and economic growth, this paper suggests the following measures that should assist policy makers in making informed decisions aimed at minimising the loss of government revenue through corruption in the public sector. First, the government should consider removing excessive bureaucracy in the public sector by reducing hierarchy of organisational structure. Second, it should promote customer-orientated strategies among public sector employees and protect and reward whistle-blowers. Third, the quality of governance should be improved by allowing the rule of law to prevail under all circumstances regardless of the gender, ethnicity, age, educational background, political affiliation and wealth of the people involved. Fourth, it is necessary to implement a public awareness program that focuses primarily on the cost of corrupt practices to PNG. Fifth, the public should be informed where suspected incidents of corruption can be reported and stiffer penalties for corrupt practices should be imposed. Finally, government agencies mandated to curb corruption should be empowered with adequate funding, manpower and legal provisions.

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