

## **GOVERNMENT OF NAURU POLICY FRAMEWORK**

### **COMMUNITY SERVICE OBLIGATIONS**

This paper outlines the framework for Community Service Obligations (CSOs) that may be required of State Owned Enterprises (SOEs) pursuant to sections 25 and 26 of the *Public Enterprises Act 2019* (PEA).

The framework outlines the purpose of CSOs, and the terms upon which they may be agreed between the Government and a State Owned Enterprise.

- Implementing the CSO framework will enable SOEs to achieve the PEA primary objective of profitability, whilst enabling the Government to be transparent about the pursuit of social objectives and their cost, improving allocative efficiency of government expenditure.

#### **Background**

CSO's are a mechanism used by other jurisdictions to be transparent about government's directives to SOEs to pursue the delivery of social obligations that undermine the ability of SOEs to operate commercially. The SOEs receive the CSO in acknowledgement of the cost of the non-commercial activity, so that overall the SOE's are able to earn sufficient revenue to be commercial.

- Governments generally accept the principle that the costs of CSOs need to be made transparent for reasons of public accountability and scrutiny and in order to better assess the financial performance of SOEs.

A CSO arises when a government specifically requires a public enterprise to carry out activities relating to outputs or inputs which it would not elect to do on a commercial basis, and which the government does not require other businesses in the public or private sectors to generally undertake, or which it would only do commercially at higher prices.

To be considered a CSO, the following conditions must be in place:

- There must be a specific request from Government to the SOE that the activity should be pursued – the CSO must be negotiated between Government and the SOE
- The outcome would not be pursued if the SOE was operating on a purely commercial basis
- There is a specified social objective
- The CSO is costed at 'avoidable cost' (ie marginal cost of service)
- Funding is from the budget

#### **Issues**

The PEA requires all SOEs to fulfil the primary objective to be commercial. However, Government often imposes non-commercial obligations on SOEs.

This has a number of impacts, including that most SOEs are non-compliant with their legislative obligations, and Government has to provide ad hoc subsidies to enable them to at least meet their financial obligations. This results in in-efficient cross-subsidies within the business, where one group of customers has to pay more for a service than another group, leading to allocative inefficiency and dead weight losses that reduce national wealth.

A CSO framework resolves some of these issues, and enables a more efficient allocation of resources. It also enhances accountability for the expenditure of public funds, making it clear how the Government supports social outcomes, and the cost of that support.

It is important to note that not all SOEs will have scope to pursue legitimate social objectives. CSOs usually relate to the provision of essential services at affordable cost.

## **Policy**

To reflect the expectation that government will continue to require social obligations of SOEs, and that it is appropriate that Government meet the marginal cost of meeting these obligations, the Government has implemented a framework for acknowledging and agreeing to CSO commitments.

To be considered a CSO, the following principles must be met:

- Only the Government can request that an SOE pursue a social objective funded through a CSO – the request must come from Government
- The CSO agreement would be negotiated with the SOE at the Government's request with details agreed between the SOE and Minister for Finance and approved by Cabinet
- The CSO objective is to be clearly specified, and conditions for the CSO, including key performance indicators are to be documented.
- The objective would not be pursued if the SOE was operating on a purely commercial basis
- The CSO is costed at 'avoidable cost' (ie marginal cost of service), and this costing is based in evidence
- Agreements are to be annual, and funded in the budget
- Agreements are to be periodically reviewed to ensure that the social objective remains relevant, and that the CSO remains appropriate, efficient and effective in achieving the objective.

Given the financial implications of proposals, the Ministry of Finance (Treasury) is responsible for implementing any CSOs through Head 16.

In the first instance, the option to implement a CSO is limited to the following:

- a) provision of essential services
- b) mitigation of the risks to food and supply security
- c) alleviating cost of living pressures or price rises for all residents.

## **Implementation**

Where the need for a CSO has been identified, the Ministry of Finance (Treasury) will develop the proposal with the relevant SOE, and seek Cabinet and Minister of Finance approval.

The Form at Attachment A is to be used to inform all applications.

The final agreement, and performance indicators, is to be finalised between the Minister for Finance and SOE, once Cabinet has agreed in principle to the terms of the CSO.

Treasury  
17 May 2020

## ATTACHMENT A

### COMMUNITY SERVICE OBLIGATION PROPOSAL FORM

Please note that the requirements on this form will need to be mutually agreed between the Government and SOE, and must reflect the underlying policy principles for CSOs

Item	Proposal	
	Name of CSO	
1	Specify the policy objective to be achieved	
2	Specify the benefit – what does success look like? For example how will the lives of all Nauruans be improved by achieving the objective?	
3	Specify goods or services to be provided (ie the activity to achieve the policy objective)	
4	Specify the agency best placed to undertake the activity	
5	Quantify value of goods or services to be provided: estimate total cost and/or revenue	Estimate of revenue foregone
6	Specify how delivery and performance will be monitored and assessed: <ul style="list-style-type: none"> <li>• service levels,</li> <li>• key performance indicators</li> <li>• reporting framework</li> </ul>	
7	Specify the duration of the agreement	12 months from 1 July 202x to 30 June 202x
8	Identify source, amount and frequency of funding	Direct budget support from Head 16  SOE to invoice Treasury monthly based on the actual cost incurred and revenue foregone.
9	Any other conditions or performance expectations	
10	Review – what are the arrangements to review the effectiveness of the CSO in achieving the benefits	Review operation prior to any successor CSO or renewal of agreement
11	Value for money assessment	
	(a) Appropriate	
	(b) Efficient	.
	(c) Effective	

Date: 17 May 2020