

# Cook Islands – Private Sector Assessment

## DRAFT Summary of Key issues and Recommendations

### Introduction

The Cook Islands is among the best performing of the Pacific Island economies. An economic crisis in the mid-1990s re-oriented the economy away from one dominated by government to one encouraging private sector led growth, which has led to significant prosperity relative to other countries in the region. The economy is closely aligned with New Zealand's and is primarily based on tourism. It uses the New Zealand dollar as currency, and New Zealand is the source for the majority of its goods imports and tourists. Currently, movements in the New Zealand dollar appear to have limited impact on the private sector. The country has limited potential for developing non-tourist based activities.

The Cook Islands requires continued economic growth to support improvements to social programs, and help address emigration pressures resulting from Cook Islanders' open access to New Zealand and Australia. Economies grow and create jobs as a result of productive investment. Private sector investment in the country, however, has been sluggish since 2009.

The Asian Development Bank (ADB) is undertaking a Private Sector Assessment (PSA) to assist the Government of Cook Islands develop a deeper understanding of key issues that should be addressed in order to develop a more conducive environment for broad-based private sector investment and sustainable growth.

PSA's are prepared based on a review of government planning documents, available economic reports and discussions with stakeholders. Work on the Cook Islands' PSA commenced in early December 2014 with an in-country visit and discussions with government officials, donors and representatives of the private sector. A draft PSA report is expected to be ready for circulation to stakeholders in late February 2015. This note provides an advance summary of key issues and recommendations likely to flow from that report.

### Key issues and recommendations

Area	Key Issues	Recommendations
General	<ul style="list-style-type: none"><li>• <b>Transparency</b> – Written policies are lacking for many areas related to investment, or are not up-to-date. Cook Islands' laws in many cases are also not readily accessible, and there is a lack of written information clearly explaining many regulatory requirements.</li><li>• <b>Public sector</b> – While public service personnel expenditures as a percentage of total government revenue remain within the target level, the size of the public service has steadily increased since 1999 and risks crowding out private sector employment, particularly outside of Rarotonga. There is also a need to continue to improve public sector performance efficiency. Currently, economic development efforts are fragmented and spread across seven government agencies.</li></ul>	<ul style="list-style-type: none"><li>• Prepare clear written policies addressing all investment related areas. Consideration should be given to doing this in the form of a National Investment Policy Statement.</li><li>• Make all legislation available electronically, free of charge, preferably through one website.</li><li>• Develop a written plain-language guide(s) identifying and describing requirements for complying with key business regulatory processes.</li><li>• Refrain from increasing the size of the public sector further, and continue to streamline public sector organizational structures and systems to improve performance efficiency. With respect to the latter, consideration should be given to revisiting recommendations from the 2011 Functional Review.</li></ul>

Business entry	<ul style="list-style-type: none"> <li>• <b>Company registration</b> – Paper-based system reliant on outdated legislation.</li> <li>• <b>Foreign investment approval</b> – Foreign investment is a sensitive issue but its current level and importance in the economy is unclear. While it provides a source of long-term investment capital and contributes to raising productivity and income growth in host countries, the process used to regulate its entry in the Cook Islands is unwelcoming because it is discretionary and time consuming to comply with.</li> <li>• <b>Foreign workers</b> – The local labor pool is insufficient to meet the economy’s current demand for workers. Despite this it is difficult for employers to hire foreign workers. The process regulating the issue of work permits lacks transparency, is time consuming to comply with and includes the same requirements regardless of the type of position being applied for. There are also concerns over the treatment of foreign workers while they are in the country.</li> </ul>	<ul style="list-style-type: none"> <li>• Undertake the planned comprehensive review of the Companies Act to bring it fully in line with modern companies legislation. Once new company legislation has been agreed on, develop an electronic registry allowing online filing and external searches via the internet.</li> <li>• Compile information clarifying foreign investment participation in the economy. Consider including foreign investment registration as a component of the electronic, online company registry once it is established.</li> <li>• Review the foreign investment approval process to enhance its transparency and align it more strategically with potential growth sectors where new investment is needed.</li> <li>• Adopt a more strategic, transparent and streamlined system for issuing work permits that provides employers easier access to foreign workers to address shortages in the citizen labor pool.</li> <li>• Introduce regulations to the Employment Relations Act that establish clear expectations about what constitutes a safe and appropriate work environment. Options for establishing an independent labor dispute tribunal that workers (citizen and foreign) and employers can access at a reasonable cost should also be explored.</li> </ul>
Land	<ul style="list-style-type: none"> <li>• <b>Land tenure system</b> – While providing business with access to land for development, the current system suffers from a number of weaknesses including fragmented ownership, an ineffective land registry and cumbersome leasing procedures.</li> <li>• <b>Land use planning</b> – No land use planning is being done. As a result, consideration is not being given to the most appropriate uses of available land, and development is occurring in environmental sensitive areas.</li> <li>• <b>Environmental impact assessment (EIA)</b> – EIA decision-makers are political appointments, and there are concerns that decision-making is insufficiently science-based.</li> </ul>	<ul style="list-style-type: none"> <li>• Examine existing land policies and processes to determine how they can be best adapted to improve the functioning of the land market. This requires: <ul style="list-style-type: none"> <li>– Building on existing efforts of the Ministry of Justice to create an accurate and comprehensive electronic land register that includes information on land titles, as well as other instruments that affect title such as leases, mortgages and occupation rights;</li> <li>– Reviewing the process for dealing with leases, subleases and assignments with the aim of simplifying it, and reducing transaction costs;</li> <li>– Holding discussions with landowners to identify feasible options for addressing land fragmentation and absentee ownership.</li> </ul> </li> <li>• Engage with landowners to identify a strategy to enable the gradual introduction of orderly land use planning and zoning.</li> <li>• Strengthen the EIA process by selecting members to sit on Island Environment Authorities (IEAs) based on technical expertise, and introducing a mechanism to enable IEAs readily access technical advice if it is deemed necessary.</li> </ul>
Finance	<ul style="list-style-type: none"> <li>• <b>Financial intermediation</b> – While the financial sector performs relatively well given the small size of the domestic market, commercial bank lending has been on a downward trend since 2009. This is due in part to an unresolved non-performing loan problem resulting from weaknesses in the collateral framework, and difficulties assessing borrower risk.</li> <li>• <b>Payment system</b> – The existing system is</li> </ul>	<ul style="list-style-type: none"> <li>• Establish a taskforce to gain a clear understanding of the reasons behind the recent fall in domestic credit to the private sector, and develop practical strategies to address the situation. The taskforce’s terms of reference should include: <ul style="list-style-type: none"> <li>– Defining the extent of the outstanding non-performing loan problem and its causes;</li> <li>– Identifying gaps in existing bankruptcy provisions;</li> <li>– Reviewing the legal framework for using</li> </ul> </li> </ul>

	<p>highly inefficient, with little by way of platforms enabling banks to interconnect as a system.</p> <ul style="list-style-type: none"> <li>• <b>Cook Islands National Superannuation Fund (CINSF)</b> – The Fund is increasing the country’s savings rate and has the potential to participate in the domestic financial market, but all funds are currently invested offshore.</li> </ul>	<p>moveable property as collateral for loans, and assessing whether reforms in this area would support increased lending to business;</p> <ul style="list-style-type: none"> <li>– Investigating the feasibility of establishing a credit bureau linked to one based in New Zealand.</li> <li>• Investigate options for improving domestic interbank clearing and settlement, including the feasibility of integrating the Cook Islands payment system into the New Zealand payment system.</li> <li>• Undertake an assessment of the potential the Fund could play in the domestic economy. This should include public consultations to determine CINSF members’ openness to having the Fund play such a role, and if the Superannuation Supervisory Bill provides a suitable prudential framework for this to occur.</li> </ul>
Other	<ul style="list-style-type: none"> <li>• <b>Infrastructure</b> – While there are weaknesses in all areas, services with respect to water, sanitation and solid waste are of particular concern given how important a quality natural environment is to sustainable growth of the tourism industry. The National Infrastructure Investment Plan (NIIP) and Capital Plan are aimed at addressing weaknesses in the infrastructure provision. However, it is essential planned investments are efficiently and effectively implemented, and assets sustainably maintained. This is currently hindered by a high degree of fragmentation in how services are delivered, and limited service provider regulation and oversight.</li> <li>• <b>State-Owned Enterprises (SOEs)</b> – The Cook Islands SOE portfolio generates a return on equity that is considerably below the cost of capital, and what comparable firms in the private sector would be expected to achieve. Aspects of the current governance and legislative framework make it difficult to achieve performance improvements. The SOE purpose is insufficiently defined and the rules around Community Service Obligations (CSOs) are confused. There is also a lack of a transparent skills based director selection process, and a clear contracting and Public-Private Partnership framework.</li> <li>• <b>Competition framework</b> – The Cook faces a number of competition related issues including single suppliers in key markets, regulatory practices that discriminate against small enterprises and concerns over high prices and anti-competitive business practices. The country, however, lacks a competition policy articulating its objectives with respect to competition, or what measures will be used to achieve them.</li> </ul>	<ul style="list-style-type: none"> <li>• Improve the quality and sustainability of core infrastructure services. This requires: <ul style="list-style-type: none"> <li>– Addressing priorities identified in the NIIP, in particular infrastructure services (water, sanitation and solid waste) that are deteriorating the quality of the country’s natural environment;</li> <li>– Integrating the NIIP into government planning and budgeting processes, and ensuring it is monitored and updated over time;</li> <li>– Exploring opportunities to improve efficiency by consolidating service delivery into fewer institutions, particularly with respect to energy, water, sanitation and solid waste;</li> <li>– Strengthening asset management systems, including the development of comprehensive and up-to-date infrastructure asset registers;</li> <li>– Ensuring effective cost recovery systems are in place to help manage demand and encourage conservation, and provide funds for investment and maintenance;</li> <li>– Separating the infrastructure regulation function from service delivery, and consider combining these regulatory functions into a single multi-sector regulator.</li> </ul> </li> <li>• Strengthen the policy and legislative framework for SOEs. This requires: <ul style="list-style-type: none"> <li>– Clearly defining the principal objective of an SOE as maximizing the net worth of the public investment;</li> <li>– Establishing clear rules for identifying and funding Community Service Obligations (CSOs);</li> <li>– Establishing transparent, skills based criteria for the selection and appointment of SOE directors;</li> <li>– Introducing a formal requirement for SOEs to always investigate options to contract out activities and services they provide and look for opportunities to work with the private sector through joint arrangements.</li> </ul> </li> <li>• Develop a coherent competition framework for the Cook Islands.</li> </ul>