

COMMISSION OF INQUIRY INTO
ASPECTS OF THE FORESTRY INDUSTRY

FINAL REPORT

Volume 1

July 1989

10 APR 90



COMMISSION OF INQUIRY INTO ASPECTS OF THE FOREST INDUSTRY

P.O BOX 2554

TELEX NE. 23290

PAPUA NEW GUINEA

4 July 1989

The Rt Hon Rabbie Namaliu
Department of Prime Minister
P O Box 6605
WAIGANI

DATE:

OUR REF:

YOUR REF.

TELEPHONE. 25 7099

My dear Prime Minister,

I have the honour to present you with the final report of the Commission of Inquiry into Aspects of the Forest Industry. The report is in two volumes and should be read in conjunction with the seven interim reports which have previously been presented. The full report therefore consists of:

Interim Report No 1

Interim Report NO 2 "The Gadaisu Timber Permit
Angus (PNG) Pty Ltd"

Interim Report No 3 "The Forest Industries Council as
The State Marketing Authority"

Interim Report No 4 "Timber Exploitation in New Ireland"

Interim Report No 5 "Comparison of various Timber Areas

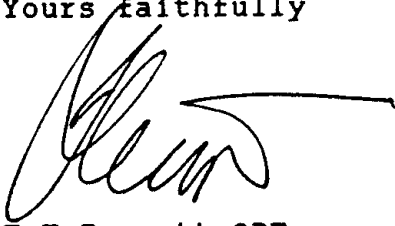
Interim Report No 6 "Log Marketing"

Interim Report No 7 "Current Events"

The Final Report

With the presentation of this report I have discharged my
Commission.

Yours faithfully

A handwritten signature in black ink, appearing to read 'T E Barnett', with a long horizontal flourish extending to the right.

T E Barnett OBE
.....
Commissioner

COMMISSION OF INQUIRY INTO
ASPECTS OF THE FORESTRY INDUSTRY

FINAL REPORT

Volume 1

COMMISSION OF INQUIRY INTO
ASPECTS OF THE FORESTRY INDUSTRY

FINAL REPORT

CONTENTS

VOLUME 1

<u>1. INTRODUCTION</u>	1
Introduction and Terms of Reference	1
Administrative Arrangements	4
Finances	5
<u>2. COURSE OF THE INVESTIGATION</u>	6
Expanded Terms of Reference and Extensions of Time	6
Angus Inquiry	6
New Ireland	8
Interim Reports	9
Marketing	10
Forest Industries Council	11
Policy	12
Current Events	13
Summary of Interim Reports:	14
Interim Report No.1	14
Interim Report No.2	14
<i>"The Gadaisu Timber Permit - Angus PNG Pty Ltd"</i>	

Interim Report No.3	16
<i>"The Forest Industries Council as the State Marketing Authority"</i>	
Interim Report No.4	17
<i>"Timber Exploitation in New Ireland"</i>	
<i>Uncontrolled damage</i>	
<i>Corruption</i>	
<i>Transfer Pricing</i>	
<i>Destruction of resource</i>	
<i>Inadequate monitoring</i>	
Interim Report No.5	20
<i>"Comparison of Various Timber Areas"</i>	
Allocation	
Interference with functions	
Compliance with Conditions	
Marketing	
Logging Practices and Monitoring	
National and Provincial Government Relations	
Benefits for the people	
Protection of the Forest Resource	
Interim Report No 6	32
<i>"Log Marketing"</i>	
Interim Report No.7	33
<i>"Current Events"</i>	
Introduction	
Jaha LFA - Manus Island	
Sebulon Watt - Tabar Island	
Sir Hugo Berghuser - Superior Tropical Timbers	
Michael Somare - Lower Sepik LFA	
Santa Investments - West Gadaisu	
Long Term Trading Co - Turama TRP	
Arawe Timber Area	
Francis Sia (MDI) and E. Tomon	
Santa Investments Hearing	
Gasmata Resources Hearing	
PHOTOGRAPHIC EVIDENCE	37
REPORT ON TERMS OF REFERENCE	40

3. <u>DEFINITION OF POLICY</u>	41
Introduction	41
The Carson Report	42
National Forestry Policy 1974	43
The Forest Estate	43
Working Plans	44
Reafforestation	45
Forest Industries	46
Forest Technology	48
Training	48
Finance	49
Independence and Provincial Government	50
Revised National Forestry Policy 1979	51
Post 1979 Scene	53
Broad Policy Postulates	57
Assessment of Policy Performance	59
Postulate 1 Customary ownership and National Control	59
Postulate 2 Orderly exploitation and protection of forests for future generations	59
Customary ownership	60
National control and orderly exploitation	62
Policy aims	62
Knowledge of resource	62
Proper plans	63
Project planning	68
Appropriate laws	71
Honest independent leadership	75
Monitoring and enforcement of conditions	77
Protection and Expansion of the Forest for Future Generations	83
Natural regeneration	84
Reafforestation	

Summary	87
Postulate 3 (Decentralisation)	90
(a) Analysis of government functions	91
(b) Consultation	94
(c) Reallocation of staff	94
(d) Substantive authority	95
(e) Funds	95
Performance of Decentralisation Policy	
(a) Analysis of government functions	95
(b) Consultation	96
(c) Staff	96
(d) Substantive authority	98
(e) Funds	99
(f) Legislative powers	102
(g) Joint ventures	103
Provincial Forestry Offices	104
Central	104
Oro	106
West New Britain	107
New Ireland	107
Western	108
West Sepik	108
Summary	109
Postulate 4 (Fair share for PNG citizens)	110
(A) Timber Rights Purchase and Royalties	111
(B) Ownership of Permit	111
(C) Premium arrangement	114
(D) Promotion of Business and Economic Development	115
(E) Local Processing Benefits	117
(F) Employment opportunities	118
Summary	119
Postulate 5 ("Papua New Guinea Ways")	120

Summary	122
Postulate 6 (Control of Foreign Investment)	122
Strict Controls	123
(a) Pre registration with DOF	123
(b) 1979 Guidelines	124
(c) NIDA	125
(d) Central Bank	126
(e) Control over acquisition of goods and services	127
(f) Control over transfer pricing	127
(g) Monitoring and control of operations	128
(h) Leadership Code	129
(i) Criminal Law	134
Foreign Dominance	136
Compromising PNG's National Integrity	138
Investment in political parties	140
Summary	142
Postulate 7 (State participation)	144
i) Stettin Bay Lumber Co	145
ii) Kumusi Timber Co	146
iii) Open Bay Timber Co	146
iv) Wewak Timbers (Madang Timbers)	147
v) Ulabo Timber Co Ltd	148
vi) Woodlark Island Development Corporation and Bougainville Forest Enterprises	148
vii) Kei Besau Kampani	148
Summary	149
Postulate 8 (Fair return to landowners and National and Provincial Governments)	150
National Benefits	150
. Royalties	150
. Company Tax	151
. Import duties	152
. Export Duty	152
. Foreign revenue earnings	153
. Infrastructure	153

Provincial Government Benefits	154
Royalties	154
Derivation grant	154
Budget allocation	154
Landowner Benefits	155
Summary	155
Postulate 9 (Promote PNG owned medium and small scale processing)	157
Summary	159
Postulate 10 (Promotion of onshore processing)	159
A <u>Large scale integrated processing</u>	159
Jant	
Nam Yang	
Stettin Bay Lumber co	
Open Bay Timber Co	
Vanimo Forest Products	
Wawoi Guavi Timber co	
Policy Performance Evaluation - Onshore Processing	163
Recent Allocations	168
Ania Fullabourne	
Jant	
Manus	
Arawe	
Nam Yang	
Government Plantations	170
Bulolo Pine	
Brown River	
Kerevat	
B. <u>Small/Medium Onshore Processing with PNG ownership and participation</u>	173
(a) Landowner companies	
(b) Wokabout Somils	
(c) Small to medium sawmills	

Summary	176
Postulate 11 (Increase log exports)	176
Revised Forestry Policy 1979	177
Guidelines of general application	178
A Strict national government control	178
B National government control	179
C Fix total log export quotas	179
D State Marketing Agency	180
E Restrict foreign investment to capital intensive projects	181
F No log export entitlements if sole buying/finance agreement	182
G Forest management controls	183
H Market promotion	
I Enterprise to construct its own infrastructure requirements	183
J Government equity	183
K Local Business Development	184
L Enforce all conditions	184
M Training and Localisation	187
N Marketing Controls	188
O Export duty of 10 percent FOB	193
Summary	194
Guidelines for Specific Enterprises	194
1. PNG Log Exporting Enterprises (FDC's)	195
2. Enterprises involved in timber processing	196
3. Foreign Log Export Enterprises (not processing)	197
4. Foreign Log export/road construction enterprises	203
Summary	204
Postulate 12 (Training)	205
Postulate 13 (Research)	206
CURRENT NATIONAL FORESTRY POLICY	207
DE FACTO FORESTRY POLICY	214
1. Resource allocation	214
2. Conditions	216
3. Marketing and pricing practices	218
4. Foreign investment	220
5. Resource Survey	221

6.	Onshore processing	222
7.	Papua New Guinea Ways	223
8.	Landowner Benefits	224
9.	Decentralisation	225

VOLUME 2

4.	<u>FUNCTIONS</u>	226
	Term of Reference No 5	225
	Preliminary observations	226
A.	<u>Powers and Functions of National Executive Council</u>	227
	Constitutional Responsibilities	227
	Powers and Functions conferred by Acts of Parliament	228
B.	<u>Powers and Functions of the Minister for Forests</u>	229
	Constitutional Functions	229
	Minister's Responsibilities to NEC	231
	Powers Conferred by Acts of Parliament	233
C.	<u>Powers and Functions of the Department of Forests</u>	234
	Generally	234
	General Responsibilities of the Departmental Head	237
	Legislative Powers and Responsibilities	238
D.	<u>Powers and Functions of Forest Industries Council</u>	239
E.	<u>Powers and Functions of Provincial Governments</u>	240
	Concluding Remarks	243
	Schedule 1 - Powers and Functions of the Minister for Forests under the Forestry Act and Regulations	245

Schedule 2 - Powers and Functions of the Minister for Forests under the Forest (Private Dealings) Act	246
Schedule 3 - Powers and Functions of the Minister for Forests under the Forest Industries Council Act	247
Schedule 4 - Powers and Functions of the Departmental Head under the Forestry Regulation.	248
Schedule 5 - Powers and Functions of Forest Officers and Forest Inspectors.	249
Schedule 6 - Powers and Functions of Forest Industries Council under the FIC Act.	251

5 INTERFERENCE WITH FUNCTIONS 252

Term of Reference No 7	252
Payment of Improper Benefits	252
FIC and Michael Cowan	253
Allocation of Wawoi Guavi Timber Permit	254
Granting of Vudal TRP to Weco	255
Angus and Edward Diro	257
Kabil LFA and John Kasaipwalova	258
Political intervention	258

6 MARKETING 267

Outline of Marketing Investigation	267
General findings on marketing	270
Transfer Pricing and Related Abuses	273
Definition of transfer pricing	273
Overvaluing Imports	274
Stettin Bay Lumber Co	274
Vanimo Forest Products	274
Wawoi Guavi Timber Co	275
Shin Asahigawa	276

Santa Investments	276
Angus (PNG)	276
Malaysia Overseas Investment	276
Madang Timbers	276
Undervaluing Exports	276
Outline of investigations	277
Undermeasurement	276
Species misidentification	278
Undergrading	278
Estimate of Loss by Transfer Pricing Report on Particular Companies	279 280
Stettin Bay Lumber Co	282
Vanimo Forest Products	282
Wawoi Guavi Timber Co	282
Open Bay Timber Co	283
Tonolei Development Corp.	284
Bismark Industries	284
Gaisho Company (NG)	284
Lusco Enterprises	285
Shin Asahigawa	285
Sumitomo Forestry Co	286
United Timbers (PNG)	286
Santa Investments	287
Bruce Tsang	287
Malaysia Overseas Investment (PNG)	287
Angus (PNG)	287
Nam Yang Timbers	288
Madang (Wewak) Timbers	288
Dewai Resources	288
Superior Tropical Timbers	288
Woodchip	289
Sawn Timber	289
Rattan Cane	290
Sandalwood	290
Concluding Comments on Marketing	290

7. <u>FOREST INDUSTRIES COUNCIL AS</u>	294
<u>THE STATE MARKETING AGENCY</u>	
Term of Reference No. 1	295
(a) Decision to involve FIC in marketing	297
(b) Nature and extent of the operations	299
(c) Nature and extent of Ministerial involvement.	299
(d) Role played by Department of Forests	301
(e) Financial effect on funds of the FIC	302
Term of Reference No 2	303
Michael Cowan	303
Miskus Maraleu	303
Wawoi Guavi Timber Company	304
Francis Sia and MOI Pty Ltd	304
E.R Diro	304
Angus (PNG) Pty Ltd	305
Santa Investments	305
Stettin Bay Lumber Co	306
Laki Sawmills and Amazon Bay	306
Sawmilling and Lumber Co	306
National Forest Products	307
Term of Reference No 7	307
Interference with functions	307
Concluding Comments	309
8 GIVING, GAINING, RECEIVING AND REQUESTING	312
 IMPROPER BENEFITS	
Term of Reference No 8	312
1. National Ministers and their Staff	315
(a) Edward Ramu Diro	315
(b) Paul Torato and Lindsay Lailai	315
(c) Stephen Raka	317
2. Other National Politicians	318
(a) Roy Evara	318
(b) Noel Levi	319
(c) Gerard Sigulogo	319

3.	Provincial Politicians	319
	(a) Robert Seeto	320
	(b) Sampson Gila	321
	(c) Ope Oaeko	321
	(d) Other New Ireland Politicians	321
4.	Public Servants	321
	(a) Oscar Mamalai	322
	(b) Jack Masu	322
	(c) Dennis Hoivo	322
	(d) Other Public Servants	323
5.	Lawyers	323
	(a) Miscus Maraleu	323
	(b) Sebulon Watt	323
	(c) Gerard Kassman	324
6.	Advisors/Agents	326
	John Kasaipwalova	326
7.	Political Parties	327
	(a) Peoples Progress Party	327
	(b) United Party	328
	(c) Pangu Pati	328
	(d) Peoples Action Party	328
8.	Managers of Landowner Companies and Community Leaders	329
9.	Owner/Managers of Foreign Timber Companies	330
	(a) Angus (PNG) Pty Ltd	330
	(b) United Timbers Pty Ltd	330
	(c) Shin Asahigawa Pty Ltd	331
	(d) Santa Investments (PNG) Pty Ltd	332
	(e) Gaisho Co (NG) Pty Ltd	332
	(f) Lusco Enterprises Pty Ltd	333
	(g) Sumitomo	333
	(h) Bruce Tsang	334
	(i) Francis Sia and Malaysia Overseas Investments Pty Ltd	334
	(j) Stettin Bay Lumber Company Pty Ltd	334
	(k) Wawoi Guavi Timber Company Pty Ltd	334
	(l) Open Bay Timber Co	335
	(m) Tonolei Development Corp	335
	(n) Bismark Industries	335
	(o) Nam Yang Timbers	335

Conclusion	336
Santa Investment and Gasmata Resources	337
9. <u>CONCLUDING COMMENTS</u>	339
RECOMMENDATIONS	342
1. Commissions of Inquiry	342
2. Policy	349
3. Legislation	350
4. Administration of Forestry	351
5. Consultative Arrangements	353
6. National Forest Development Plan	354
7. National Forest Development Programme 1987-1991	356
8. Resource Survey	357
9. Existing Operations	357
10. Monitoring	358
11. Continous Review and Assessment	361
12. Controls on Foreign Investment	364
13. Price Controls	365
14. Form of Exports	367
15. Benefits to Landowners	369
16. Landowner Preparation	369
17. Leadership Code	370
18. Criminal Law	370
State Marketing Agency	370
Distribution of Report	372
CONCLUSION	375

LIST OF ABBREVIATIONS

1.	ANCC	All Nippon Checkers Corporations
2.	App.	Appendix
3.	DDC	Djaul Development Corporation
4.	DOF	Department of Forests
5.	DLAD	Danfu Logging and Agricultural Development Pty Ltd
6.	DTI	Department of Trade and Industry
7.	FAO	(United Nations) Food and Agricultural Organsiation
8.	FDC	Forest Development Corporation
9.	FIC	Forest Industries Council
10.	FOB	Free on Board
11.	FWP	Forest Working Plan
12.	GAISHO NG	Gaisho Company (New Guinea) Pty Ltd
13.	IR.No	Interim Report Number
14.	KBK	Kei Besau Kampani
15.	LC	Letters of Credit
16.	LFA	Local Forest Area
17.	MEP	Minimum Export Price
18.	MOI	Malaysia Overseas Investment (PNG) Pty Ltd
19.	MTD	Mussau Timber Development Pty Ltd
20.	M3	Cubic Metre
21.	NEC	National Executive Council
22.	NFDP	National Forests Development Programme
23.	NIDA	National Investment and Development Authority
24.	NTA	Native Timber Authority
26.	NIOD	New Ireland Otsuka Development Pty Ltd
27.	NYDF	National Youth Development Fund
28.	OBTC	Open Bay Timber Company Pty Ltd
29.	S\$	Singapore Dollar
30.	SBLC	Stettin Bay Lumber Company
31.	SGS	Societe De Surveillance
32.	SMA	State Marketing Authority
33.	STT	Superior Tropical Timber Pty Ltd Company
34.	TTDC	Tabar Timber Development Corporation Pty
35.	TRP	Timber Rights Purchase
36.	UNCTC	United Nations Centre on Transnational Co-operation
37.	USDS	United States Dollar
38.	VFP	Vanimo Forestry Products
39.	VOL.	Volume
40.	WGTC	Wavoi Guavi Timber Pty Ltd

COMMISSION OF INQUIRY INTO
ASPECTS OF FORESTRY INDUSTRY

FINAL REPORT

1. INTRODUCTION

The Commission of Inquiry was established on the 29 April 1987 primarily to inquire into allegations which had been made concerning the involvement of the Forest Industries Council (FIC) in marketing logs on behalf of the State. It had been alleged that members of the FIC executive had exceeded their functions and had interfered with the functions of the Minister for Forests and the Secretary and Department of Forests (DOF). It was also alleged that improper benefits may have been obtained by some of those involved with the FIC's marketing activities.

It was originally intended that the inquiry would be of this limited nature and that it should be completed in six months. The original terms of reference were Terms 1 to 6 and were concerned with defining policy and functions of the Minister, the Secretary and the Department to ascertain whether they had gone off course and whether there was interference between them. The whole question of the involvement of the FIC in marketing was to be canvassed and the benefits to the State of that involvement were to be assessed. There was also to be an inquiry into the question of improper benefits. During the first weeks three more terms of reference were added.

Presentation of Report:

The result of the Commission's inquiries and its findings have been reported upon already in seven interim reports consisting of eighteen volumes. Those volumes consist of text, schedules of tables and photocopies of key documents set out in appendices. The interim reports are an integral part of the Commission's report to the Prime Minister. In this Final Report an attempt has been made to draw together the main findings and to give a very brief overview of the course of inquiries and a summarised report on each term of reference.

To gain access to the Commission's findings on any topic however it will be necessary to refer to the relevant interim report and to at least read the appropriate passages of the text and refer to key tables - especially the schedules of marketing tables.

The final terms of reference were as listed below. (The section in the report where each term is dealt with is shown in brackets).

- "1. The process by which the Forest Industries Council became involved in the marketing of timber and -
 - (a) when, and by whom a decision was or decisions were made to involve the Council in marketing operations; and
 - (b) the nature and extent of the actual operations; and
 - (c) the nature and extent of any Ministerial involvement in marketing operations; and
 - (d) the role (if any) played by the Department of Forests in the actual marketing operations and resource allocation; and
 - (e) the financial effect of the marketing operations on the funds of the Council.
- (Sect.7 and IR No.3)

2. The benefit obtained by Papua New Guinea (if any), from the marketing operations of the Council.
(Sect.7 and IR No.3)
3. Whether any persons associated with the Council or its marketing operations received any direct or indirect benefits, whether financial or otherwise, as a result of the marketing operations of the Council and whether it was proper or improper for such benefits to be given or received.
(Sect.7 and 8 and IR No.3)
4. What is the existing Government policy relating to Forestry and in particular relating to resource allocation and conditions of operations, marketing and pricing of timber within the forestry industries in Papua New Guinea.
(Sect.3)
5. What are the functions of the Department of Forests, the Minister for Forests, and the Forest Industry Council within the Government policy for the forestry industry.
(Sect.4)
6. What effect, if any, the involvement of the Forests Industries Council in marketing operations has had on the Government policy and the functions exercised by the Minister for Forests and the Department of Forests.
(Sect.7 and IR No.3)
7. Ascertain whether and to what extent the functions of each of the Minister for Forests, the Department of Forests and the Forests Industries Council under the approved policy for the Forest Industry identified under Term 5 have been interfered with or encroached upon by another or others of such functionaries or any other person.
(Sect.5)
8. Establish whether any of, or any persons associated with, the Minister of Forests or any officer of the Department of Forests Industries Council or any other person has received or attempted or sought to receive any direct or indirect benefits whether financial or otherwise as a result of or in connection with the allocation or promised or prospective allocation of the right to participate in any way in the exploitation of timber resources and establish whether it was proper or improper for such benefits to be given attempted or offered or received attempted or sought.
(Sect.8 and all interim reports)

9. Ascertain whether any and if so which person or persons associated with the PNG timber industry have been frustrating government policy by misdescribing species, quantity, quality or value of log exports or by deliberately understating income or overstating costs or by manipulating shipping freight charges or by any other similar devices including the practices commonly referred to as transfer pricing.
(Sect.6, Sect.8 and IR No.6)

The formal instruments of appointment, statement of case and terms of reference are appended to Interim Report No 1.

The first few weeks were taken up with establishing the Commission's administrative arrangements.

Administrative Arrangements

The administrative arrangements for setting up the Commission were fully described in Interim Report No 1. It shows how the Commission was established with myself as sole Commissioner, assisted by Mr John Reeve as Counsel assisting the Commission, Mr Jack Nouairi as Secretary, Mr David Keta (my associate) as a professional assistant, Mrs Hebou Homoka (and later Mrs Sheila Robert) as Steno/Secretary and Messrs Tau Helai and Kerry Agua as drivers. Its office was set up in the National Parliament and the finances and major administrative arrangements were to be handled by the Department of the Prime Minister.

Those arrangements continued except that Mr Keta took on the task of office Manager after Mrs Robert resigned and Mrs Joyce Peter replaced Mrs Robert as Secretary. Mr Martin Yakopa replaced Mr Nouairi as Secretary. Late in 1988 the Commission relocated in the

National Court House. At the Courthouse the Commission had the advantage of using additional secretarial assistance and additional word processors.

During the last two months Mr Graham Powell joined the Commission's staff as an additional counsel assisting the Commission.

In the last month Mr Benedick Kilian replaced Mr Keta as my Associate and assistant.

Finances

The Commission was greatly assisted by the fact that all its accountancy, bookkeeping and financial arrangements were handled by the administrative section of the Department of the Prime Minister.

The total cost of the Commission for the two years, and two months, not including the cost of the Commissioner's personal staff and vehicle made available by the National Court is estimated at approximately K282,763 and made up as follows:

MAJOR EXPENSES OF COMMISSION OF INQUIRY

	1987	K
<u>ITEM</u>	<u>DESCRIPTION</u>	<u>AMOUNT</u>
2.	TRAVEL AND ACCOMMODATION	5,067
3.	UTILITIES (Telephone Post Office, Telex etc)	850
4.	MATERIALS AND SUPPLIES	7,012
5.	TRANSPORT HIRE (IN AND OUT OF PORT MORESBY	9,858
6.	SPECIAL SERVICES (including consultancy fees)	17,651
7.	CAPITAL ASSETS (Office equipment)	4,333
8.	NIL	
9.	OTHERS (AIR CHARTER)	519
10.	WAGES AND OVERTIME	<u>2,080</u>
	TOTAL	<u>K47,370</u>

1988		K
<u>ITEM</u>	<u>DESCRIPTION</u>	<u>AMOUNT</u>
2	TRAVEL AND ACCOMMODATION	4,881
3.	UTILITES: (i.e telephones, Telex, Post Offices etc)	676
4.	MATERIALS AND SUPPLIES	4,151
5.	TRANSPORT HIRE	3,718
6.	SPECIAL SERVICES (including consultancy fees)	117,876
	TOTAL	<u>131,302</u>

1989 (until June 16)

2.	TRAVEL AND ACCOMMODATION	392
3.	UTILITIES	-
4.	MATERIALS AND SUPPLIES	2,660
5.	TRANSPORT HIRE NIL	2,011
6.	SPECIAL SERVICES (Anticipated)	96,200
7.	CAPITAL ASSETS	-
8.		-
9.		-
10.	OVERTIME AND WAGES	2,828
	TOTAL	104,091
TOTAL OF ACTUAL COMMITMENTS FOR 1987 TO 1989		282,763
COST OF STAFF AND SERVICES PROVIDED BY NATIONAL COURT		188,101
		<u>K 470,863</u>

2. COURSE OF THE INVESTIGATION

Expanded terms of reference and extensions of time:

Immediately upon commencing the inquiry I took possession of all FIC files by subpoena. Shortly afterwards I subpoenaed all files of Angus PNG Pty Ltd. Even a preliminary look at the FIC files showed evidence of an improper relationship between its chairman Miskus Maraleu and Executive Director Michael Cowan with

Minister Diro and with members of the timber industry which went outside the Commission's limited terms of reference. Further studies disclosed evidence of improper benefits being received by politicians, public servants, landowner company directors and others outside the narrow range of people referred to in Term of Reference 3. I sought and was readily granted an amendment to the Terms of Reference to enable these matters to be investigated and terms 7 and 8 were added on the 14 May 1987.

Further inquiries disclosed that all trails led to transfer pricing. It was impossible to turn a blind eye to transfer pricing as it soon became apparent that it was a major preoccupation of the great majority of the companies being studied. It was the source of funds from which improper benefits were being sought and paid and was a major consideration when assessing the achievements of FIC State Marketing and the benefits flowing to the State from that involvement.

Reluctantly and with deep reservation I sought and was granted a further amendment to enable me to inquire into the far reaching question of transfer pricing. Term of Reference 9 was added on the 8 July 1987 and I embarked on a major investigation which has covered all aspects of the timber industry and has taken two years and two months to complete.

When seeking the first extension of time from the then Prime Minister, I pointed out that it was not then possible to make a realistic estimate of the time which would be required. The Commission would be searching in the dark; especially on the question of transfer pricing. This was because of the difficulty of obtaining firm evidence of the practice when, at that stage, I had no

idea how to even begin to seek it out. Although the extension was for a fixed period, the Prime Minister assured me that there would be no difficulty in obtaining further extensions if good results were being obtained.

On that assurance, I was able to plan the methodology of the inquiry and to set in motion several "probes of inquiry" simultaneously in the hope that it would all come together in the end. I directed Mr Reeve to concentrate on collecting evidence for the Angus Inquiry and set in motion an internal audit of FIC's books, to be followed by an investigation audit by the Auditor General. I myself inspected timber operations in New Ireland and, progressively, in other provinces to broaden my knowledge of the industry and the varying conditions under which it operated. My aim was to observe forestry policy "in action"

Angus Inquiry:

The Angus Inquiry centered around the involvement of former Forests Minister E R (Ted) Diro.

Owing to Mr Diro's non co-operative attitude, the Angus Inquiry took far longer than expected but I persevered because it was crucial to all other investigations. Eventually that inquiry introduced the Commission to one key group of prominent persons whose improper activities extended over the whole of the industry. These included the former Minister for Forests, the Secretary for Forests and the Chairman and Executive Director of the FIC. Following up the links from that central group to other persons, and to various "deals" and operations has been a major part of the Commission's subsequent work.

The Angus Inquiry also yielded detailed knowledge of more than one type of transfer pricing scheme and showed the immensity of the sums of money involved in that practice. It also enabled Counsel Assisting to experiment with, and to evolve, techniques for obtaining evidence of transfer pricing.

New Ireland

Having made a general examination of major timber operations in several provinces, having commissioned the study into FIC's records and accounts and having worked out the techniques for investigating transfer pricing, I then set about a detailed study of the industry in New Ireland. New Ireland was chosen as it had been subjected to heavy logging for a long time and because the smell of corruption and transfer pricing seemed to be coming most strongly from that province. That province was studied in detail because the allocations, the operations and the "behind-the-scenes" manipulations were all interrelated. I have presented key documents as schedules to the Commission's reports to enable successful "follow up" action to occur.

Interim Reports

As I knew that the task ahead was a long one and as the "follow up" action was immediately and urgently required, I have presented a series of detailed interim reports and held a series of policy conferences with Ministers and Officers as the work progressed and the results became available. As I had only one counsel assisting me the time consuming task of preparing these reports and handling the ongoing conferences added considerably to the length of the inquiry. It did however yield significant gains for the government. Many

of the loopholes and irregularities the Commission has uncovered have now already been rectified, timber companies have modified their practices and very significant revised taxation assessments have been negotiated with several timber companies as a result of the transfer pricing activities that the Commission has proved, documented and already reported upon.

There are seven interim reports in all totalling 18 volumes. They must be read in conjunction with this final report as, together, they constitute the Commission's Report to the Prime Minister.

Marketing

The techniques for uncovering transfer pricing were evolved during investigations into companies operating in New Ireland and then a major investigation into the marketing practices of all the major producers in other provinces was launched. The background work involved was very time consuming and involved shipment by shipment analysis of each company's activities locally and overseas. It involved gaining a detailed knowledge of transfer pricing intermediary companies in Hong Kong, Singapore and elsewhere; it involved tracing through the web of corporate interrelationships between companies operating in PNG and their overseas "parents" and affiliates; and it involved studying the details of log price variations over the last ten years or so on the international market.

Public hearings on "marketing" were then held over several months in Waigani and were attended daily by the taxation investigator who had previously been made available to work with the Commission. A great volume of evidence was taken and that has been painstakingly analysed over the many months since those hearings

finished. As the inquiry into each company was finished. the evidence collected by the Commission, and the results of its analysis, formed the basis of revised tax assessments which have already yielded well over K3 million to the government.

Forest Industries Council

When the Auditor General's report on FIC accounts was available in August 1988 it became possible to continue the investigations and hearings into FIC matters and then to begin the massive task of analysing the evidence for presentation as the Third Interim Report. This report was presented in November 1988 and was subsequently tabled in the National Parliament.

The next task was to re-examine the evidence and materials already collected on New Ireland. When this re-examination was carried out, new light was thrown on it from the completed FIC investigations and from the ongoing studies into transfer pricing. My knowledge of the interrelationships between New Ireland personalities such as Bruce Tsang, Francis Sia and Miskus Maraleu was greatly extended by being able to link them firmly to the characters involved in F.I.C affairs. The "innocent explanations" offered by some New Ireland companies about their marketing practices were no longer credible in the light of the wider understanding which the Commission then had about international marketing, transfer pricing and about the similar activities of other companies disclosed during the marketing hearings. The Commission's very detailed report on the New Ireland Timber Industry was presented to the Prime Minister in March 1989.

After completion of the New Ireland Report the Commission concentrated on completing its analysis and report on marketing, on reporting on some mainland timber companies and on conducting an investigation into some current events. The report on the mainland companies (and a report on Manus Province) were presented as Interim Report No 5 in April 1989.

Throughout this period the Commission has methodically continued its analysis of the evidence on the marketing practices of most companies involved in marketing PNG logs and sawn timber. This long and detailed task has been conducted on a shipment by shipment basis and Counsel Assisting the Commission has been assisted by Mr Roe of the Office of Taxation. As my findings on each company's marketing were completed, I presented them to the Prime Minister as volumes 2 to 4 of Interim Report No 6. At the same time the evidence was made available to the Chief Collector of Taxes and he has used it as the basis of reassessment of taxes in some instances. Volume 1 of Interim Report No 6 was completed just prior to the completion of this final report and it contains a complete overview of the findings I have made concerning log and sawn timber marketing in PNG together with comments and recommendations.

Policy

To define policy as required by Term of Reference 4 involved a full study of "policy in action" and a thorough study of documentary sources as there was no clear comprehensive statement of current policy. These studies disclosed that there was a huge gap between what was being done, and allowed to happen, and what had been formulated as policy in the scattered documents being studied.

For this reason, throughout the lifetime of this Commission and throughout, all its investigations, I have been observing all practices and occurrences, all government decisions and all instances of acquiescence by government with a view to assessing what I have described as "defacto policy". In this report I have followed the lead given by G L Carson in his 1974 Report when he said that;

"policy is a course of action adopted by government"

This difficult task of defining National Forestry Policy was required of me by Term of Reference No 4. My attempt to report on that question takes up the major part of this final report as it involved an extensive investigation into all aspects of timber operations from initial planning (where it occurred), allocation of the resource, logging operations, marketing of the product and, finally, financial disclosure to resource owners and to the PNG government. In the course of my inquiries into de facto policy I inspected timber operations in six provinces and conducted a series of "closed" seminars and public hearings into various aspects of current policy. My definition of National Forestry Policy is dealt with in Section 3.

Current Events

A number of occurrences and practices have occurred since I completed my formal investigations. At first I tried to turn a blind eye to them so as not to be distracted from the preparation of this final report and so, also, as not to become too deeply involved in current controversies.

As the time extended, however, I came to realise that some current events are directly relevant to my previous investigations and to ignore them would be to knowingly present only part of the picture. Also the fact that some malpractices have continued to occur despite the very wide public exposure of them in the Commission's public hearings and reports is worthy of reporting as it illustrates the urgent need for appointing an individual or a body to be a permanent or "stand by" watchdog over the timber industry. These current events are reported in Interim Report No 7.

SUMMARY OF INTERIM REPORTS

Interim Report No 1

This report details the establishment of the Commission and outlines its early inquiries. It focuses on the gap between policy statements and defacto "policy in action. On the basis that "policy is a course of action adopted by government "(Carson 1974) I have listed at pp 17-26 my preliminary observations on defacto policy. Nothing I have seen or heard since then has inclined me to change those general observations. They have in fact been thoroughly confirmed by repeated case studies.

Interim Report No 2

"The Gadaisu Timber Permit -
Angus (PNG) Pty Ltd"

This report examines in detail the formation, operations, transfer pricing and disastrous failure of Angus (PNG) Pty Ltd.

The main focus of the report is inevitably upon the role played by former Minister for Forests Edward Ramu (Ted) Diro who was deeply involved with the Malaysian Company, Malaysia Overseas Investment Corporation and its principals M A Ang and Tan Sri Ghazali Shafei and then with Angus group of companies based in Singapore. Mr Diro was chairman and 35 percent owner of the Angus subsidiary Angus (PNG) Pty Ltd before he unexpectedly became Minister for Forests in 1985.

IR No 2 describes how, instead of disclosing his interest in Angus, Forest Minister Diro concealed it beneath a variety of different covers and how he was referred to by the Code name "Andrew" in correspondence within the Angus group of companies. In his capacity as Minister he improperly allocated the permit over West Gadaisu to Angus (his own company) and granted it other favours. Meanwhile Mr Diro had been receiving and continued to receive improper benefits - firstly from MOIC and then from Angus (Singapore).

IR No 2 describes how Angus was being "milked" by its parent company and how it indulged in various transfer pricing schemes to fraudulently transfer tax free profits for the benefit of Angus in Singapore. I found also that Mr Diro was party to, and the main beneficiary of, a scheme to transfer massive profits through a New Jersey company and how he personally stood to gain USD3,292,800 overseas by way of transferred profit and USD 1,774,700 in PNG by way of "legitimate" dividend.

Finally IR No 2 describes how Angus failed and how Minister Diro finally turned against it and endeavoured to revoke its permit and how in his last two days in office, he quite improperly, and in great haste, issued a

permit to Goodwood Pty Ltd over the neighbouring timber area at Sagarai Gadaisu thus committing Port Moresby's intended reserves of domestic sawn timber to be exported overseas in log form.

The full list of Mr Diro's improper benefits is set out in the interim report at pages 43-46 and is also summarised in section 8 of this final Report.

Interim Report No 3 "The Forest Industries Council as the State Marketing Authority"

This interim report was presented in November 1988. It deals with most of the aspects relating to the FIC in the Commission's terms of reference.

The report shows how the FIC drifted towards involvement in State marketing over a period of six years after the NEC had "all mention of FIC doing any marketing" deleted. It shows how Michael Cowan and Miskus Maraleu conspired to achieve Cowan's appointment as Executive Director and FIC's appointment as the State Marketing Agency (SMA), even though it had no legal basis on which to operate. Once in control of the SMA Cowan and Maraleu pushed FIC into an expensive marketing programme, placing government funds and the viability of the FIC at risk.

Cowan came to influence Minister Diro to such an extent that it constituted an interference in DOF and Ministerial functions.

Under Cowan's management the FIC was very inefficient and, in its first six months, built up an operational loss of USD 40 000 together with contingent liabilities of between USD 500 000 to USD 800,000. Cowan

managed to misapply FIC funds to pay off a USD 21 366 bank guarantee and misappropriated at least USD 28 892 by telexed transfer to David Toms of Straits (Singapore). The way Cowan and Maraleu conspired to assist Wawoi Guavi Timber Co to gain favourable operating conditions from Minister Diro behind the back of DOF Secretary Mamalai is fully described. Interim Report 3 examines each FIC shipment and each marketing transaction of the FIC.

Despite all these faults and irregularities. I concluded that FIC involvement in marketing did achieve a substantial reduction in the amount of transfer pricing.

After FIC marketing ceased, the simple way which DOF set about performing the SMA role, as an agent rather than as a trader in logs, is described in some detail and I concluded that this involvement was more economical and efficient than FIC's rather grandiose and loss - making attempts.

My formal answers to the FIC related questions posed in the Commission's Terms of Reference are set out in Section 7 below.

Interim Report NO 4

"Timber Exploitation in New Ireland Province".

This interim Report records the findings of the Commission's inquiry into the New Ireland timber industry. Seventeen operations, involving ten foreign operators, various traders and twelve landowner companies were investigated. The detailed comments on each operation are recorded as appendices in Volumes 2-4B of the Report. Volume 1 presents an overview of the timber industry in New Ireland as it relates to the terms of reference of this Inquiry.

Uncontrolled damage:

The main value of Interim Report No 4 for experts and policy makers is to be found in the three volumes of appendices. (Volume four is published in two parts 4A and 4B). They present a great deal of factual raw material which can be used by persons more expert than myself in matters of forestry, economics, environment and sociology for the purpose of analysis. Their conclusions may differ from my own to some degree but I am sure that any fair analysis of the Commission's findings will substantiate my opinion, that the New Ireland timber industry is out of control and has blighted the hopes of landowners and devastated a valuable timber resource for very little gain to the people or government of Papua New Guinea. The report shows up failings in national and provincial ministers and forestry officers which, unfortunately, are of concern nationwide, not just in New Ireland.

Corruption:

A major concern, amply recorded in the appendices and dealt with specifically in Section 15 of Volume 1, is the evidence of blatant corruption at high levels of government and the practice of ministers and senior public servants of negligently, and sometimes deliberately, ignoring and contravening the laws of Papua New Guinea's Parliament and the policies of its government.

Transfer pricing:

Another major concern illustrated by Interim Report No 4 is the irrefutable evidence of full-scale transfer pricing and other fraudulent marketing practices of the foreign companies controlling the marketing of New Ireland logs. These same practices are (on the evidence

before this Commission of Inquiry) carried out by almost all timber marketing companies in the country. In New Ireland I found, without exception, that all marketing companies studied were transfer pricing, commonly at the rate of about USD10 per m3. (When small producers such as Channel Timbers and Leytrac, which did not conduct overseas marketing themselves, exported logs by selling to traders such as Gaisho, Shin Asahigawa and Lusco, the transfer pricing was arranged by the trader.)

Destruction of resource:

Interim Report No 4 concludes by referring to the imminent extinction of New Ireland's commercial timber resource. The detailed reasons for my claim that the total resource will be doomed to destruction at the end of the 1987 - 1991 programme of allocations are set out in Schedule 1 to Volume 1 of the interim report. The situation is absolutely critical and if there is to be any hope for managing the remaining unallocated resource on a sustained yield basis, there should be no further allocation in New Ireland which will allow for log exports.

Inadequate monitoring:

In addition I emphasised that Permit and Dealing conditions should be monitored and enforced. Lack of monitoring by the Provincial Forestry Officers has been a major contributing factor to the present critical situation. Timber companies have been allowed to carry out destructive operations, to log the slopes and to remove undersized trees with virtually no effective monitoring system (see Schedule 2 and also IR. No.6) for full discussion of the defects in the monitoring system). I recommended that all existing operations on New Ireland should now be examined most critically and wherever the

breaches of operating conditions would warrant closing down the operation, then that should be done as soon as possible.

The situation in New Ireland had been allowed to occur because the Ministry of Forests had no clear policy on allocation and preservation of the resource, because the Department of Forests did not prepare an accurate inventory survey and because some of the timber companies involved made substantial payments to national and provincial politicians, and to political parties, to ensure support for their operations and applications.

The Ministry of Forests still has no clear policy, the Department's resource estimates and calculations are still absurdly inaccurate and the same timber companies which previously bribed politicians are still receiving political support and, it is alleged, are still offering substantial payments. The most recent evidence of this was given a few days before I completed this final report when a letter signed by Francis Sia of MOI was tendered which showed that he offered a consultancy fee of K1000 per month to the current Provincial Secretary (See IR No. 7).

Interim Report No 5 "Comparison of Various Timber Areas"

Interim Report No.5 contains the results of detailed studies of three PNG mainland timber areas. The operations being conducted in these areas are on a large scale and they illustrate important aspects of PNG forestry policy and its administration. There is also a brief study of recent events in Manus Province where it seems that the same problems which have led to the devastation of the forests of New Ireland (reported in Interim Report No 4) are reoccurring.

The reports on these operations are set out in appendices to the interim report as follows:

- Appendix 1 Wawoi Guavi Timber Area, Western Province.
- Appendix 2 Vanimo Forests Timber Area, West Sepik Province
- Appendix 3 Kumusi Timber Area, Oro Province.
- Appendix 4 West Coast Manus Timber Area, Manus Province

Between them, the operations studied in IR No. 5 provide illustrations of most of the malpractices and defects in the system which are occurring and of many aspects of "defacto" policy which are described in Section 3 below. These matters are reported upon under the headings which have been constantly reoccurring throughout the interim reports:

Allocation Two of the allocation decisions demonstrate the effect of lack of planning. In two of the areas the preparatory work was seriously defective in that the timber rights were not purchased and permit not issued before the commencement of operations. (Wawoi Guavi and Kumusi)

The four allocations demonstrate four different approaches as to who should be the concession holder. Block 1; of the Wawoi Guavi timber area was originally allocated to a "sham" national company, Wawoi Guavi Timber Co Pty Ltd (WGTC), but by the time Block 2 issued WGTC presented itself as a wholly owned foreign subsidiary of Straits Engineers Contracting Pte Ltd of Singapore. I believe that WGTC has recently been sold to

another overseas company which illustrates how the original owner with whom the State negotiated can be changed during the continuance of the permit by internal share transfers within the permit holding company. Vanimo Forest Products (VFP) always presented itself as a fully foreign owned enterprise, Kumusi Timber Co (KTC) was set up as a Forest Development Corporation with 75 percent national ownership (by State and Provincial Government). The allocation of a timber permit to Kei Besau Kampani in Manus illustrated an allocation to a landowner company and its foreign contractor.

The recent declaration of Jaha LFA seems to be an illustration of a typical "puppet" landowner company seeking to be granted timber rights for the benefit of the foreign contractor which has arranged for its incorporation and which "possesses" it. (and see IR No.7)

Each of the three mainland allocations resulted in injustice being done to the resource owners. It is too early yet to assess this with regard to the two Manus allocations described in this interim report.

Interference with functions

Serious interference is described in the case of Wawai Guavi timber area in which a conspiracy between the executive director of the FIC, Michael Cowan, and David Toms of WGTC persuaded Minister Diro to grant favours and beneficial conditions to WGTC, without the knowledge of DOF, to such an extent that it was literally enabled to settle and type up its own final permit document and it was Cowan of the FIC who briefed the Minister and obtained his signature. The Acting Secretary DOF was merely given a copy after the event. In Manus the interference with departmental and Ministerial functions

was caused by Monarch Investments which manipulated local landowners and politicians to bring such pressure on Minister for Environment and Conservation Jim Yer Waim that he approved their environmental plan without waiting to consult with anyone. Similar pressure was being brought to bear on Forest Minister Stack.

Compliance with Conditions

WGTC and Kumusi both have a very bad record of non compliance with operating conditions and this is fully documented in the interim report. WGTC was prepared to accept any number of onerous conditions in order to "land the allocation". Once safely installed it proceeded to renegotiate some conditions and to ignore many of the others. It was permitted to continue operating and to negotiate much less onerous conditions in order to gain access to Block 2 and then to fall blatantly behind in the performance of the new conditions. Its sawmill for instance is still not completed and its trial regeneration plots not commenced.

Kumusi went into receivership and was then permitted by the government (which owned substantial equity) to continue to operate for the benefit of the creditors in flagrant breach of all conditions which had been imposed for the benefit of the resource owners and local community.

VFP performed its conditions more responsibly but has still failed to commence reforestation, to construct a major urban development and to conduct some important feasibility studies.

Marketing The interim report records the transfer pricing activities of WGTC and the way it has been able to manipulate its complex series of management contracts with related companies to transfer funds. Kumusi marketed through the Japanese trader Sumitomo. Some of Sumitomo's marketing devices are disclosed in this interim report others are dealt with more fully in Interim Report No.6 Vol.2 App.2. Sumitomo's practice of undergrading logs is also described.

VFP has developed creative and successful marketing strategies through its marketing agent Quarter Enterprises. These are fully described in Interim Report No.5 but are also dealt with in Interim Report No 6 which deals specifically with marketing. The Commission, after exhaustive investigation, found no evidence that VFP was transfer pricing or that it, or its agent, was involved in any other secret marketing malpractice. Similarly, on the evidence before me, I can find no evidence that either Kumusi or its contractor Ambogo sawmill were involved in transfer pricing. There is evidence however that Sumitomo indulged in large scale undergrading (as buyer), bought at an unfair price and made excessive profits on resale. It appears to have, in effect, an exclusive buying agreement with Kumusi (now Ambogo) and has provided finance for its operations in exchange. This aspect of Sumitomo's buying practices is further described in IR No 6 and requires further investigation and close monitoring.

Logging Practices and Monitoring

IR No 5 describes the poor logging practices of VFP and the comparatively satisfactory logging practices of WGTC and its logging contractors. Kumusi's bush

operations were not inspected but the monitoring performance of all three provincial forestry offices is commented upon unfavourably.

It is too early to judge the logging operations on Manus Island as they have only just commenced. It is to be noted, however, that Monarch Investments - the proposed contractor for Jaha Development Pty Ltd, moved its equipment to Manus and commenced operating in defiance of lawful attempts by the Provincial Government and the Secretary for Forests to stop it. This comparative new arrival on the PNG timber scene is showing signs of strenuous activity as it was the proposed logging contractor behind three of the four LFA's recently approved by the Namaliu government - Jaha LFA, Lolo LFA and it initially was the intended contractor for the Lower Sepik LFA.

Another contractor competing for an LFA declaration alongside Jaha is United Timbers, wishing to contract for the Kali Bay Development Corporation. Its logging practices, undergrading techniques and its habit of organising massive amounts of transferred profits through Mitsubishi are fully described in IR No.4 App.4.

National and Provincial Government Relationships

The timber operations described in Interim Report No 5 illustrate well many of the problems in National/Provincial government relationships which are described in section 3 of this Final Report.

The Wawoi Guavi operation was pushed forward under pressure from Straits (Singapore) even though it had no priority under the National Forestry Development Programme. It was opposed by the Provincial Government which at one stage briefed a prominent national lawyer to try and reverse the National Government's firm decision to proceed with the allocation. (The Provincial Government was eventually won around by false promises and "generosity").

On Manus the TRP was allocated with full cooperation between the two levels of government but failure to have a National Forestry Development Plan in place resulted in the National Minister finding himself "unable" to resist demands for the declaration of the Jaha LFA which it is claimed will overcommit the Manus timber resource. If so it could result in the agreed upon Joint venture veneer mill being starved of resources. The conflict between the National Government and the Manus Provincial Government resulted in a series of Court actions and, eventually, the enactment by the MPG of its own forestry legislation to try and block the National Minister from over committing the resource. It has resulted in a LFA declaration being made over an area which is disputed between two rival landowner companies backed by two rival foreign companies. This is a situation in which it will be most difficult for any Prescribed Authority to decide which people represent the true landowners as the matter is in dispute. Since the writing of IR No.5 the Minister has gazetted the Deputy Premier to be the Prescribed Authority. This man is, obviously, a politician. He is also one of the leading members of the Jaha group which is contesting the question of ownership. (See IR No.7)

In the Vanimo Timber area the allocation had been well planned and an intergrated project set up with full consultation with, and involmnet of the Provincial Government. Despite the fact that a National Government co-ordinator was appointed to co-ordinate the project, the level of communication between national and provincial governments had deteriorated as did communication with the company. The company got into many difficulties and alienated both levels of government, I believe that the major problem was a failure of direct and honest communication.

The Kumusi project involved both National and Provincial Government equity as 75 percent of shares were government owned. The other 25 percent were owned by the management company. After Kumusi went into receivership both national and provincial governments stood by while the receiver concentrated only on log exporting with no further regard for performance of its infrastructure and other obligations.

Benefits for the People

This section of Interim Report No 5 analyses in detail how the benefits received by the landowners have been unfairly low in each of the areas studied when compared against the benefits being openly and secretly taken by the foreign developer. The method of calculating royalties places them at about one quarter of the actual value of the standing tree and landowners have been receiving only 25 percent of royalties (recently raised in some instances to 75 percent). The share being received by landowners is in fact ridiculously low.

In the Wawoi Guavi Area, on top of royalties, the landowners received a premium of 48t per cubic metre which had been stupidly calculated at far too low a

rate. They received little more, as few infrastructure conditions had been imposed upon WGTC. The Company cheated the National Government of its proper revenue by transfer pricing which has kept it continuously in a loss situation.

In the Vanimo Area again the benefits had been limited to royalties and the hope of some increased employment and business opportunities in the local area. Few infrastructure conditions were imposed on VFP and two major ones which were imposed (reafforestation and urban development), have not been performed because of difficulties in acquiring the necessary land.

As far as Kumusi is concerned it has been a disaster for the local people. Through no fault of the landowners Kumusi Timber Co went into receivership and was then permitted to operate on for the benefit of its creditors. Being a Forest Development Corporation, and three quarters government-owned, few conditions had been imposed upon it. It was treated as the "peoples" company almost by definition and landowners were expected to gain somehow by its very existence. The few conditions of operation which were designed to benefit local people (such as the major bridge over the Kumusi River) were left unfulfilled while KTC (in receivership) cut out the people's forest. It paid off the secured creditors and some of the unsecured creditors before facing inevitable action to have it wound up in recent weeks. The landowners are now making a bid to wrest Kumusi's company houses from the creditors in a desperate attempt to gain at least these timber reminders of their former forest resource.

Whether the Manus people gain significantly from the arrangement between their landowner/Provincial Government Company and SEAL Pty Ltd will depend upon the vigilance of the former, the honesty of the latter and the profitability of their proposed joint venture veneer mill. On the experience of other similar ventures I am somewhat pessimistic about the future of the venture as there is now a doubt about the continuing availability of its resource and because conversion of the Indonesian log industry into a plywood/veneer industry is lowering the demand for veneer. On past experience also, foreign companies and some of PNG's political and business leaders have reduced the profits available for distribution to shareholders by simply taking secret profits offshore or into their personal or political party bank accounts.

Protection of the forest resource

Finally the Fifth Interim Report studies in detail the failure to address reforestation and to successfully secure the performance of natural forest regeneration obligations on any of the three mainland companies described. It also describes the problems caused by the scarce and inaccurate available knowledge of our forest resource base and how this has resulted in such a bitter dispute between national and provincial governments over the Manus resource.

The concluding comments discuss how the three mainland operations have failed to boost the economy of the three underdeveloped provinces concerned, have failed to bring substantial benefits to the peoples or governments involved and how all four studies again show

up the need for the formulation and clear statement of a National Forestry Policy and the preparation of a National Forestry Development Plan.

The report concludes by pointing out the shameful gaps in our knowledge of the quantity, quality and regrowth capabilities of our forest resources. The existing knowledge is not a safe basis upon which to plan an ambitious logging expansion programme. I repeat here the concluding comments on the four operations studied in Interim Report No 5 as they are applicable to the nation as a whole:

"When decision makers are "groping in the dark" in this way they should be taking very cautious steps and making very conservative decisions. With New Ireland as an example of what has already happened (see Interim Report No 4) and Manus as an example of what is likely to happen the 1987-92 National Forest Development Programme needs to be rethought as a matter of urgency.

That Plan aims to more than double the existing 3,377,000 hectares of already allocated resource by allocating an incredible further area of 3,463,000 hectares by 1992. Almost all of the timber to be harvested is planned for export as logs. (Interim Report No 4 Vol 1 Schedule 1 Attachment 4)

The programme needs to be rewritten so that it restricts further cutting until we have accurately calculated the national forest resource and until we have planned the optimum rate of cut and the areas where that should be occurring. Logging should be restricted (not expanded) until we have developed the laws and the Provincial manpower into an

effective forestry service capable of controlling the exploitation of our own resources, according to our own carefully thought out plans. The exploitation of this national forestry resource must be organised so as to produce the maximum, "fairly shared" benefit for all citizens, but particularly for the landowners who must become active participators in the benefits and activities which should be generated by timber operations. There must be a National Plan synchronised with the various Provincial Plans and it must cater for the total requirements for land usage. It must provide for forest replenishment where that is appropriate, forest conservation and environmental protection areas where those are appropriate and for forest plantations and other agricultural developments where these are appropriate.

These four studies demonstrate some aspects of the fog which is casting its cloud over forestry in this country. It is a mixture of meandering intellectual neglect, bureaucratic inefficiency and lack of honest political commitment to the visionary ideals of the Constitution. Underneath this fog of inertia there are very active foreign companies, in partnership with some very greedy citizens, which are using many devices to manipulate landowners and politicians for one end only. Their aim is to cut down trees and transport them to log ships waiting at the beach and in this activity they are being very successful. Some are doing it with a sense of responsibility while most are doing it in reckless and destructive haste. Unless our authorities take control, the resource will be destroyed and a great opportunity for this and succeeding generations will be gone for ever."

Interim Report No 6. "Log Marketing"

This interim report is in four volumes consisting of a full dissertation in Volume 1 covering all aspects of log marketing in PNG. It includes a survey of the major reports and literature on the subject and draws upon the Commission's detailed shipment analysis of all log dealers to set down an authoritative statement about what has been, and what is still, happening in the field of log marketing. There is also a brief survey and some comments on marketing of processed (mainly sawn) timber.

Volumes 2 to 4 set out text, schedules and documents relating to the various marketing companies each of which is included in its own separate appendix as follows:-

1. Shin Asahigawa
2. Sumitomo Forestry
3. Timbersales
4. Nam Yang Timbers
5. Stettin Bay Lumber Co
6. Open Bay Timber Co
7. Bismark Industries
8. Lusco Enterprises
9. Tonolei Development Corporation
10. Madang Timbers

Volume 1 traces the movement of logs from stump to end buyer in the country of destination and traces the movement of the financial payments from end buyer to producer through the transfer pricing middlemen in Singapore and Hong Kong. It examines in detail the question of transfer pricing and other marketing malpractices and the measures taken to eliminate or reduce these practices.

The conclusions are that almost every company involved in marketing PNG round logs is involved in serious marketing malpractices which robs the PNG government and the resource owners of very substantial amounts of money. A further conclusion is that the various control systems which have been introduced to control these malpractices are either insufficient or not enforced. The position has improved since 1986 but there is still a great deal to be done to ensure malpractices are eliminated or minimised.

Volume 1 concludes by discussing the form that future State involvement in log marketing should take.

Interim Report No 7 "Current Events"

This interim report deals briefly with some current matters which recently came to the attention of the Commission. These are:

Jaha LFA - Manus Province

Although this matter was reported in IR No 5 App.4 more recent developments, including the public examination of Minister for Forests Karl Stack are reported in this volume.

Sebulon Watt - Tabar Island

Mr Watt appeared at a public hearing in May 1989 and was examined on his continuing involvement with illegal timber operations on Tabar Island. This matter was first reported in IR. No.4 Vol.2 App.2.

Sir Hugo Berghuser - Superior Tropical Timbers

Sir Hugo's attempted involvement in the Rai Coast Timber Area through his company Superior Tropical Timbers (in receivership) is described together with details of proposed transfer pricing scheme.

Michael Somare - Lower Sepik LFA

Mr Somare's involvement, as a major shareholder in Sepik River Development Corporation Pty Ltd and as a powerful lobbyist, in obtaining the declaration of an LFA in the Lower Sepik/Angoram area is described. The declared area includes an area which is the subject of an Australian aid funded land utilisation feasibility study. The possibility of a conflict of interest between his role as Minister for Foreign Affairs and his role as lobbyist for his personal and his "people's" interest is raised.

Santa Investments - West Gadaisu

The approval of Santa as contractor in the West Gadaisu Timber Area is discussed. In view of Santa's record it is suggested that this decision be reviewed.

Long Term Trading Co - Turama TRP

The unseemly haste in which this timber area was allocated in a matter of months is detailed. The advertisement was for companies to apply for approval as contractor/developer to the Turama Business Group as Permit Holder.

The time for submitting detailed proposals was so short that it effectively ruled out all applicants except Long Term Trading Co which was already prepared. The permit was then granted to LTT (not the Turama Business

Group as had been advertised. The accepted proposal varied greatly from the proposal guidelines and was unfavourable to the landowners.

Arawe Timber Area

The recent selection and approval of Cakara Alam as developer despite the existence of other good or better proposals and before the selection has been made between two rival landowner companies as permit holder is questioned.

Francis Sia (MOI) and E Tomon

The fact that Francis Sia has recently offered "to bribe" the New Ireland Provincial Secretary by paying him a retainer of K1000 per month is reported. The Secretary says he did not accept the offer and examination of his bank accounts support his denial.

Santa Investments - Public Hearing

The results of a public hearing into the documents seized by the police from Santa's offices are reported. The documents include correspondence and financial records which disclose payment of benefits to, and requests for, benefits from politicians and public servants. Francis, Michael and Simon Sia were examined and also company Secretary Ian Shepherd.

Gasmata Resources - Public Hearing

Mr E.R Diro was examined in a private session to explain his involvement in a business relationship with Mr Chin Ah Eng of Gasmata Resources Pty Ltd. The relationship involved both of them being shareholders in a company to which Mr Eng contributed substantial sums of money. At the time Mr Diro was Minister for Forests and Mr Eng was involved in the PNG timber industry and seeking pre registration and other approvals from the

Forestry Department. I found that impropriety was not proven against Mr Diro but that it was a very unwise relationship for the Minister for Forests to have entered into. The relationship came to a sudden end after Mr Diro ceased to be Minister for Forests and after Mr Eng had financial trouble. Had it continued it would eventually have put the Minister into an extreme conflict of interest situation.

In some of the matters reported in Interim Report No 7, I have recommended that further investigations should be made.

PHOTOGRAPHIC EVIDENCE

A. Infrastructure Development

In many areas it is clear that companies are not honouring their obligations to provide long term benefits by the development of roads, bridges and building construction. In many instances there is no development at all and in other cases it is of a clearly temporary nature.

Photograph

1-5 Temporary bridges and poor quality roads in the Danfu Area (New Ireland Province). In No 1 the poor construction of the bridge can be seen and in No.3 the entire bridge has been washed away.

6. Temporary infrastructure development at the Wawoi Guavi site. (Note also the failure to comply with environmental requirements for a 50 metre buffer area around the gully).

7-9 The operations site at Napanta Nabui - New Ireland Province (Nationwide - Bruce Tsang) comprises company built bush material structures with no long term benefit.

10. Temporary building at Bereina. Luabar Logging was illegally operating under a Timber Authority which imposed no infrastructure requirements.

B. Environmental Impact

It is common for even the most basic environmental considerations to be ignored. Serious and often irreversible damage must inevitably result.



1

Temporary bridges
at Danfu extension
TRP.



2



3



4

5

Danfu Extension
TRP -
Temporary bridges
and poor roadworks



6

Temporary In-
frastructure at
Wawoi Guavi



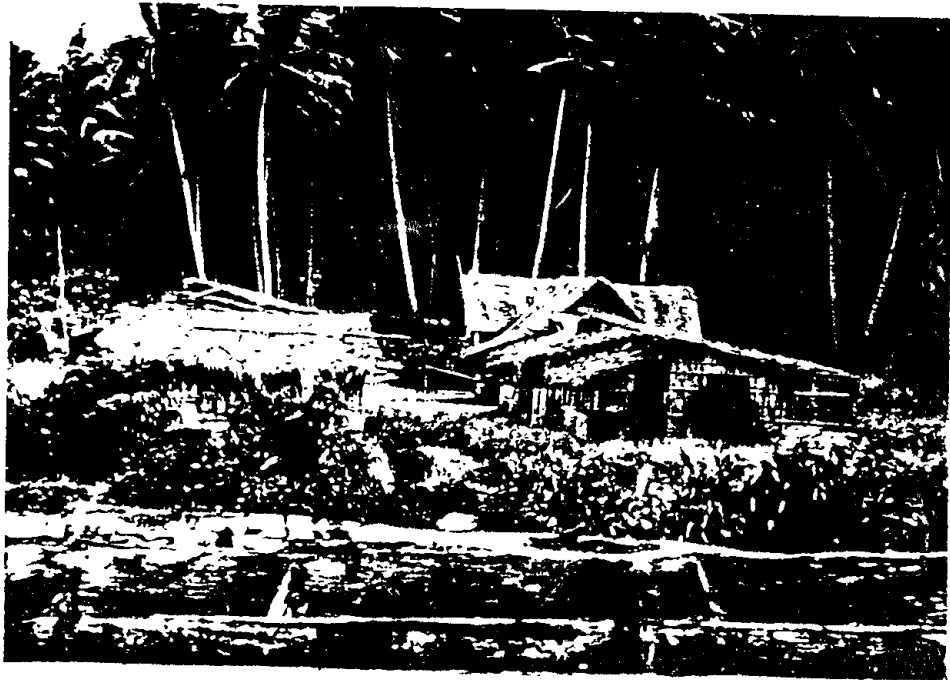
7

Bush material
Huts at operations
site - Napanta Nabui

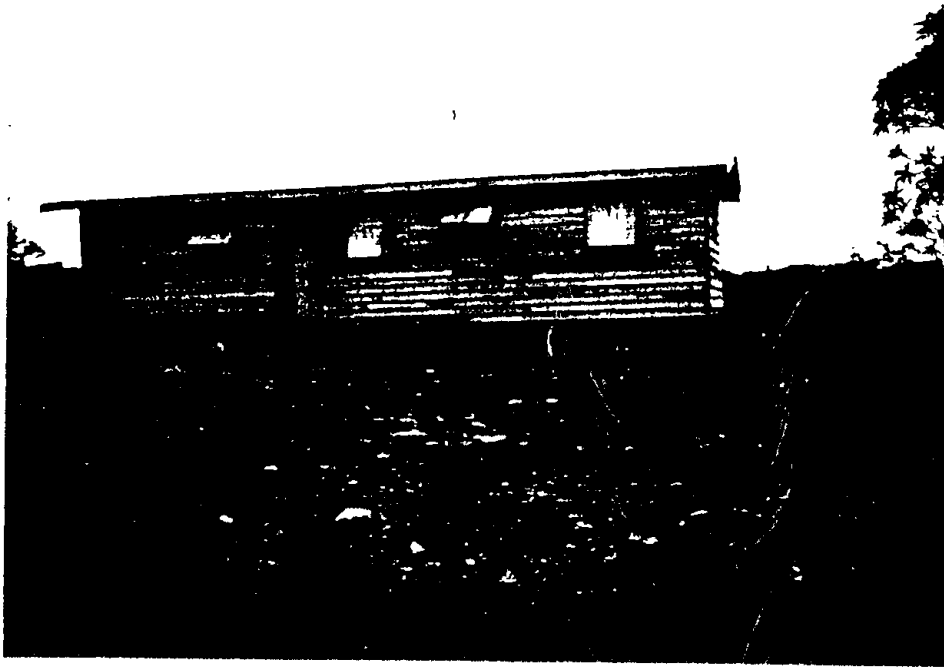


8

Napanta Nubui -
New Ireland Province



9



10

Temporary building at
Bereina. Luabar
Logging



11

The high rainfall
area at Wawoi Guavi



12

Wawoi Guavi



13



Wawoi Guavi





16

Pollution and
riverbank damage
at Baimuru
Sawmill - Gulf



17



18.

19.

Neglected
processed
timber -
Vanimo Forest
Products.



20.



21

Illegal Logging at
Bereina - Luabar
Logging



22



23

Danfu Extension
TRP



24

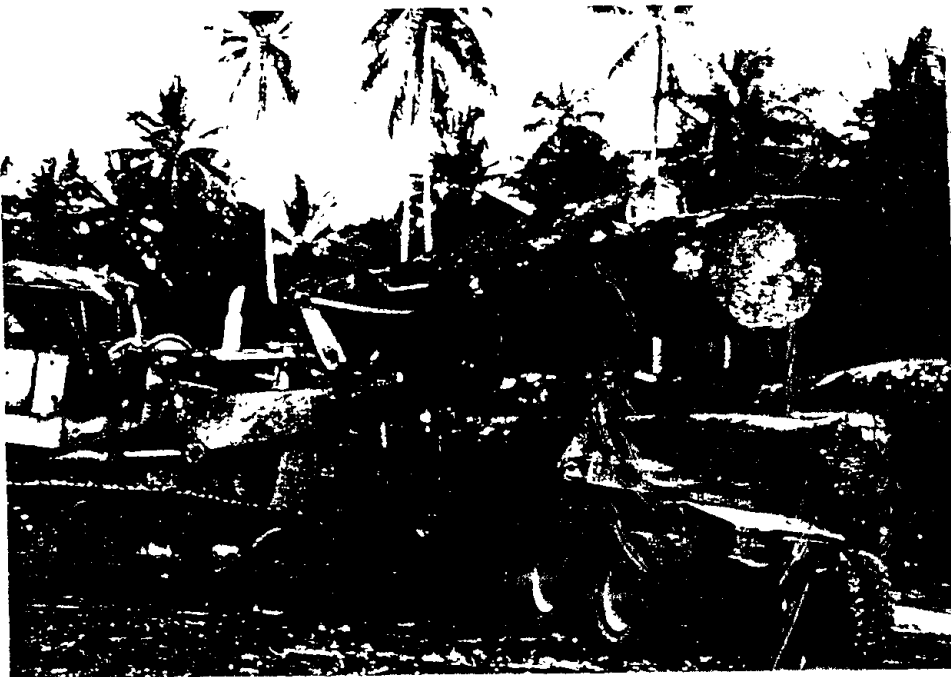


25

Log wastage
at Danfu
TRP



26



27

Danfu Extension
TRP



28

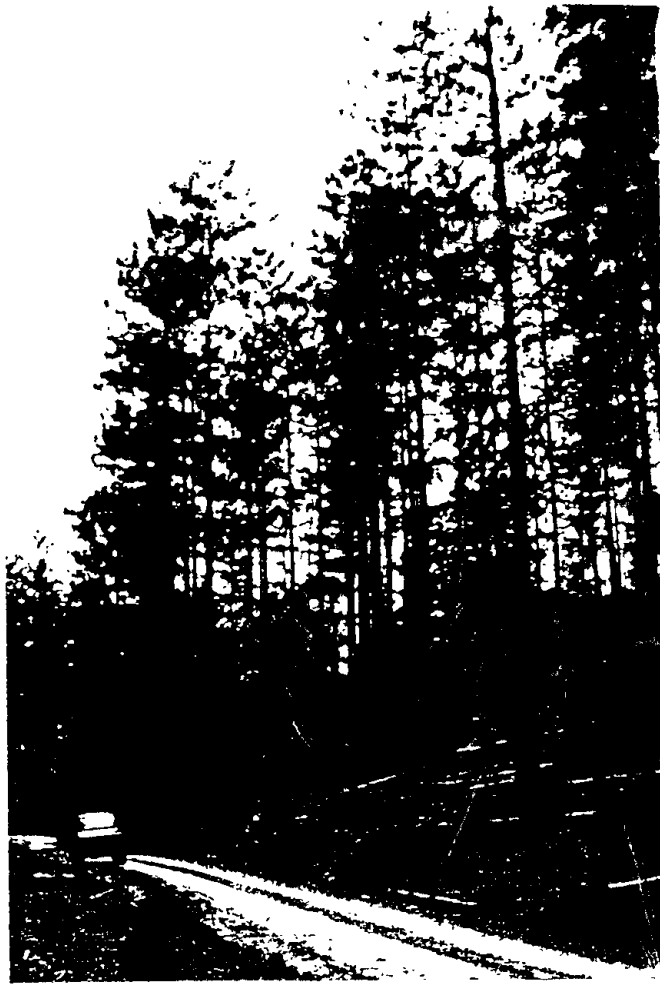


29

Reafforestation in
Bulolo Area



30

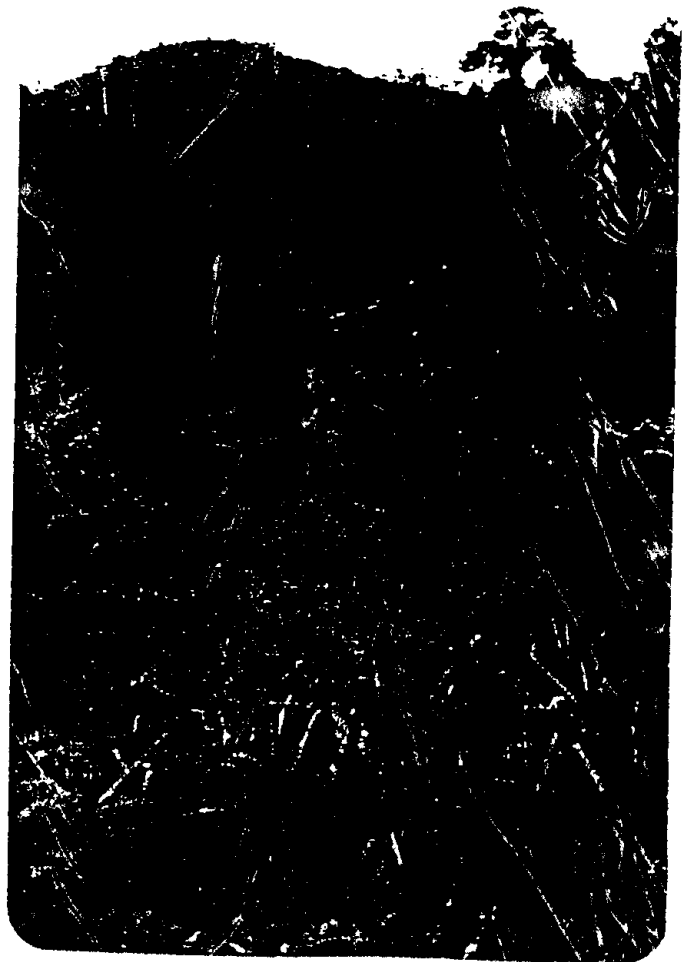


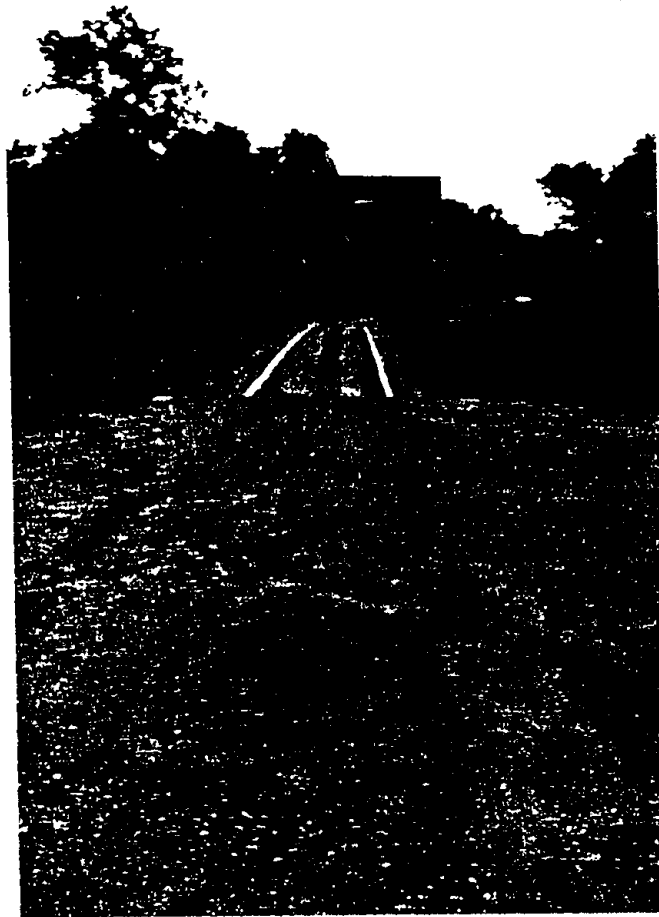
31

Bulolo

32

Tree Planting in
New Ireland





33

Bridge constructed
by SBLC



34

Wharf in West New
Britain

REPORT ON TERMS OF REFERENCE

I now proceed to report upon the Commission's Terms of Reference in the following order:-

Section 3. Definition of Policy (Term of Reference No 4)

Section 4. Functions (Term of Reference No 5)

Section 5. Interference with Functions (Term of
References No 7)

Section 6. Marketing and Transfer Pricing (Term of
Reference No 9)

Section 7. The Forest Industries Council as the State
Marketing Agency (Terms of Reference Nos 1,2,3, and 6)

Section 8. Improper Benefits (Term of Reference Nos 3
and 8)

Photograph

11-15 In the high rainfall area of Wawoi Guavi the clear impact on river, riverbanks and surrounding areas is evident. (Note: No 12 reveals a clear breach of the environmental requirement for a 50 metre buffer area from all flowing streams).

16-17 Pollution of the river by sawdust and damage to the riverbank by failing to remove logs to higher ground is clear at the Baimuru Sawmill in Gulf Province.

Photograph

13 The shed to the right of this picture is part of a sawmill that was never completed at Wawoi Guavi.

C. Local Processing

There is a clear lack of commitment to local processing requirements. In some cases operators incur high wastage by undertaking reasonably extensive saw milling in order to obtain higher export quotas.

18-20 Stockpile of sawn timber at Vanimo Forest Products showing neglect, high wastage and a lack of commitment to the on-shore industry.

D. Illegal Operations

In some instances operators simply act deliberately outside the law.

Photograph

21-22 These logs were illegally harvested at Bereina (Cental Province) by Luabar Logging under a Timber Authority. They should be used for the on-shore market but were logged for export.

E. Bad Logging Practices

Interim Report No 4 Volume 1 contains a number of photographs clearly showing instances of and the effect of bad logging practices in New Ireland.

23-24 Unnecessary widening of bush ramps and road side clearing in Danfu Ext. TRP.

25-26 Evidence of log wastage by Gaisho (PNG) Pty Ltd at Danfu Ext. TRP.

27 Use of front end loader without a fork at Danfu Ext TRP

28 Log wastage and beach pollution at Danfu Ext TRP.

F. The Other Side

There are instances where logging companies have brought long term and worthwhile benefits and have respected their obligation to the environment.

29-31 Results of reforestation at Bulolo

32 Tree planting in New Ireland Province

33 Permanent bridge constructed by Stettin Bay Lumber Co in West New Britain.

34 Wharf under construction in West New Britain by Nam Yang

3. DEFINITION OF POLICY

TERM OF REFERENCE NO.4.

"What is the existing Government policy relating to Forestry and in particular relating to resource allocation and conditions of operations, marketing and pricing of timber within the forestry industries in Papua New Guinea".

INTRODUCTION

When a Prime Minister wishes to know what the existing government policy relating to Forestry is he would normally ask the Minister for Forests and his departmental Secretary. The fact that the question has to be asked of a Commission of Inquiry indicates that there is something very wrong.

After a diligent search of the normal documentary sources of policy, after holding several policy conferences with former Forestry Minister Horik and his senior officers and after hearing Minister Stack admit that there was as yet no clear statement of forestry policy I can understand the dilemma. There is in fact no document and no person able to state authoritatively what the current National Forestry Policy is. This fact explains the appearance that the administration of this extremely valuable natural resource appears to be lurching on from one allocation to another and from one decision to the next with no clear sense of purpose.

Because of their training in days when forestry was treated as a profession, and formulations of policy accorded pretty well with what was actually occurring, the senior foresters in the Department still have a personal sense of what is right and what is wrong and how it accords with existing legislation and procedures. The legislation however dates from the highly centralised pre Independence

"colonial" period, before the introduction of Provincial government; under which "forestry" was made a "concurrent subject", the authority over which is to be shared between National and Provincial governments. It dates from times when the forests were seen as vast natural areas to be conserved until the money and the will to set up forest industries such as sawmills and plywood factories, were found and from times when to export timber as round logs was seen, almost, as a betrayal of a national trust - the sale of a national heritage.

The fact is however that circumstances have changed since Colonial times and the older foresters' personal feeling of what is right, and the legislation and procedures upon which their training was based, are no longer appropriate.

The Carson Report 1973

The policies appropriate for those colonial times were formulated by G L Carson in his 1973 report (See Appendix 1 for a full discussion of the Carson Report)

When Carson wrote his report the Forestry (Private Dealings) Act had just been enacted. He rightly pointed out that it allowed for private dealings between forest owners and private companies and that it broke the Minister's monopolistic control over forest exploitation. He warned that it introduced an alien concept which threatened to undermine the whole concept of orderly control by the national government to protect the forests for future generations and to ensure wise management.

Carson advised urgent revision and consolidation of Forestry legislation to provide rules for a proper balance between the essential requirement of government control and the legitimate desires of resource owners to be allowed to gain some benefits from their highly demanded timber. Sixteen years later this revision of legislation has still not occurred.

Carson's report was immediately followed by the publication of a White Paper "National Forestry Policy" 1974 which later received NEC approval as a full statement of all aspects of Forestry policy.

NATIONAL FORESTRY POLICY 1974

The 1974 Policy set rules appropriate for forestry in that highly centralised system. It focussed on firm national government control and the protection of the resource in perpetuity. It aimed at the planned, gradual and orderly development of timber processing industries. The text did not refer to log exports and it simply left the Forestry (Private Dealings) Act alone, as if it were some sort of alien monster which might somehow go away as unexpectedly as it had come.

As it has never been revoked nor replaced the 1974 Policy remains the most comprehensive formal statement of government policy. As such I will quote its policy directions, making a brief comment after each section:

To give effect to this policy the Government directs that:

- (A) The forest Estate
 The Department will work towards the dedication of sufficient land to achieve the productive, protective and ancillary national policy objectives.

In addition to areas managed by the Department, it will encourage and assist in the establishment and proper management of local authority and private forests.

The location of the forest estate will be determined by national needs and may be influenced by

- (a) the requirements of other land use authorities;
- (b) the requirements of the owners;
- (c) the nature of the resource;
- (d) proximity to markets; and
- (e) the needs of existing industries.

The development and management of the forest estates will aim towards the land owners participation and sharing in the benefits obtained without losing sight of the primary objective, efficiency in management.

The Department will provide the Government with clear recommendations on how to establish the necessary forest estate to meet present and future needs of the country giving regard to contemporary social and political pressures. In making this presentation it will recommend action to be taken in regard to old timber rights purchases and land purchased for forest development.

A continuing assessment of forest resources will be carried out in order to:

- (a) maintain an up to date record of the available timber resource;
- (b) enable industry to decide the possibilities of development; and
- (c) plan detailed and orderly utilisation and management of forest areas.

Comment

The concept of dedicating a national forest estate did not go ahead nor was progress made in assisting proper management in private forests.

An up to date record of the available timber resources has not been kept. The data is years out of date and notoriously inaccurate.

(B) Working Plans

The Department will have working plans prepared for the proper development of each forest estate. These plans will take into consideration:

- (a) resource management objectives;
- (b) environmental factors;
- (c) the marketing potential of the timber resources;
- (d) efficiency and cost of logging techniques;
- (e) costs, standards and location of roads;
- (f) land use subsequent to logging;
- (g) reforestation objectives and cost benefits.

These plans will be sufficiently flexible to meet changing utilisation and marketing patterns, will ensure adequate control of operations at all times, and will be the basis of future field activities by the Department.

Comment

Such plans were not developed as no forest estates of the type envisaged were established. Nor were plans of this sensible nature drawn up for the project areas which were later allocated for exploitation (such as Stettin Bay, Open Bay, Kapuluk and Vanimo)

(C) Reforestation

The Department will cooperate with other land use authorities to develop land use plans over all land the subject of forest industry development to determine those areas to be managed as forest. The basic aim will be to see that the forest resources of PNG are maintained and expanded to ensure that the permanent needs of the forest industry are met and the social and economic environment of the people is protected.

In those areas where there is a deficiency of forest crops it will undertake afforestation projects designed to satisfy local needs.

The Department will aim to maximise local participation at all levels and give particular regard to the involvement of the landowners.

Comments

Since 1974 there has been an ever decreasing effort put into reafforestation. The plantations which existed then are now rundown or harvested and there is almost no government sponsored reafforestation occurring. Reafforestation obligations in timber permits have not been properly performed or enforced. The exceptions are Stettin Bay, Open Bay (now) and (for a while) Jant. These are discussed below.

There has been little effort to formulate comprehensive and realistic land use plans and little planning of forest management.

(F) Forest Industries

The Department, in co-operation with other Government agencies, will encourage the development of forests industries in accordance with Government investment guidelines. It will encourage the use of locally processed forest products, take an active part in review of tariffs, imports and export regulations and trade agreements, and in other matters that affect the timber industry. It will within the limits of its resources keep the industry informed of the latest scientific, economic and market developments in regard to forest activities and forest products.

Main aims will be:

- (a) to increase rapidly as possible the production and export of forest products;
- (b) to diversify markets

(c) to improve the quality and extend the processing of forest products within the country, so increasing the export value and local employment;

(d) introduce suitable quality control rules particularly in regard to export products;

(e) to develop a fully integrated forestry industry of industrial complexes working within permanent forest estates;

(f) to increase employment, business and training opportunities for local people;

(g) to provide opportunities for local people to have shares in the industry and where appropriate ownership;

(h) to develop facilities of general use to the community - roads, wharves, etc.

(i) to foster the use of local forest products, and the development of local market opportunities;

(j) to foster the development of minor forest products industry, especially sago, rattan, resins, and biochemicals;

(k) to develop techniques to improve industry efficiency, especially logging;

(l) to ensure that returns to the Government are related to current market and cost criteria.

Comment

Since the declaration of this policy to increase the production and export of forest products the export of sawn timber has dropped from 51,000 m³ in 1974 to 2,700 m³ in 1987. Over the same period plywood exports have dropped from 15,700 m³ to 1700 m³ and the small veneer and chopstick trade has stopped altogether.

The record of encouraging local participation in forest industries has been abysmal.

(E) Forestry Technology

The Department will maintain sufficient expatriate staff particularly professional staff to undertake essential research work relating to resource assessment, silviculture, resource

utilisation and marketing and for the training of local officers. The Department will look for the most economic way to resolve any research problem giving consideration to the facilities available in other departments and authorities (U.P.N.G. and the University of Technology) and to those in Australia and elsewhere.

Comment

Staff levels devoted to research have been maintained at a high level but the research priorities have become outdated. Research has concentrated on 1974 policy priorities of reforestation plantations and processing whereas forestry practice has shifted to "tree mining" operations and predominant emphasis on log exporting. Research into logging practices and regeneration of natural forest commenced only recently.

(F) Training

The training of local personnel is of vital importance and the Department will maintain and, if necessary, expand its training schemes to meet departmental and industry needs. Opportunities for the training of technical and professional staff in conjunction with other tertiary institutions will receive major attention.

Comment

Training has been concentrated on the need to develop foresters capable of performing in the forestry scene envisaged by this policy. The graduates have found that those skills are not in high demand in the current log export scene and the majority of graduates are failing to

find employment in the timber industry. Graduates are being turned out at the rate of 20 diploma students per year from the Bulolo Forestry College and 5 degree students per year from the University of Technology. This is at a total cost of K600, 000 p.a

(G) Finance

A basic objective will be to maximise economic returns to the Government. Royalty will be the primary return, but the Department will in its cost/benefit considerations give consideration to other forms of benefits and returns. The Department had introduced a new system of appraising royalties which is a more objective method than has been possible in the past. Under this system the overall level of royalties will be subject to review every two years to take account of changing circumstances in the timber industry.

Comment

The government has sought to maximise returns by encouraging a rapid increase in log exports and charging an export duty of 10 percent of FOB price. The basis for appraising royalties has not been altered nor subjected to regular review.

After my most preliminary inquiries it became clear that the 1974 Policy was not being followed - hardly in any respect at all.

What happened of course was that it became overwhelmed by the political constitutional and economic events of the next five years.

INDEPENDENCE and PROVINCIAL GOVERNMENT

In 1975 PNG gained its independence. It enacted a Constitution which spells out set principles for protecting and renewing forests (as a National natural resource) for the benefit of future generations while, at the same time, exploiting them now for the benefit of all.

It guaranteed property rights of the customary owners of the forest but, at the same time, it required the National government to take firm control over the exploitation and development of the forests. In 1976 the Constitution was amended to provide for a substantial degree of decentralisation of government authority to the newly established Provincial Governments and Forestry was made a "concurrent subject" the control over which is to be shared between both levels of government. The Forestry Service was promptly divided up and control over field staff was given to Provincial Governments.

Independence introduced completely new factors into the "bywater" of PNG forestry. The already outdated legislation then became positively archaic. Unfortunately, repeated calls and directions from the NEC to draft new consolidated Forestry legislation has still not resulted in a draft bill being submitted to NEC for approval (though several were prepared and another is now with the legislative draftsman). The old legislation still sets rules intended to guide and control the actions of Ministers, public servants, timber operators and landowners.

The laws are not appropriate to control the forces which have been unleashed by Independence: a driving need for government revenue, aspirations of provincial governments and the arrival of foreign timber companies determined to take advantage of the relaxed rules on log exports.

REVISED NATIONAL FORESTRY POLICY 1979

The Revised National Forestry Policy was published as a White Paper in 1979. Unfortunately it was not a full revision and re-statement of policy taking account of Independence, the Constitution and Provincial Government; these momentous happenings were ignored and the revised policy merely dealt with log exports.

This policy revision was prompted by the need to increase national income and overseas earnings. Like all other departments DOF was directed to come up with proposals for solving this post Independence funds shortage and the answer was to graft onto the 1974 Policy (which focussed on conservation and orderly development by means of local processing) a revised policy of encouraging the rapid increase of log exports. Under the 1979 Revised Policy, guidelines for permitting log exports were set for four types of enterprise:

(a) PNG (National) Log Export Enterprises

These became known as Forest Development Corporations and were intended to be formed with government involvement and assistance. They were to be allowed to export logs with few obligations and conditions imposed. (See discussions on Kumusi Timber Project-IR No. 5 App 3)

(b) Foreign owned Timber Processing Enterprises

These were to be allowed some log export quotas to fund and encourage their processing operations

(c) Large Foreign Log exporters (not processing)

These were to be given large log export quotas in exchange for them performing substantial additional activities such as agro/forestry projects, and undertaking a heavy burden of infrastructure obligations such as construction of major roads, and bridges, urban development projects, schools and hospitals.

(d) Log export/road construction enterprises

These five year permits were to be granted to companies which have engineering capacity. The limited permit was to allow them to export a given volume of logs in exchange for constructing a stated length of highway.

As a result of this policy revision post Independence Forestry Ministers are now confronted by a very different scene than that which faced the former colonial administrators and the pre-Independence "Ministerial Members" and "Self government" Forestry Ministers. Unlike the senior professional foresters, the Ministers have not been trained in principles of sound forest management and they do not necessarily share the foresters' "feeling" for what is right. What is more Ministers, usually, have not been raised in traditions which incline them to seek departmental advice before making important decisions. Up until the commencement of the Wingti Government in 1985, Forest Ministers tended to take important decisions to the NEC. Since then the tendency has been for the Minister to make major decisions about allocation of resources without seeking NEC approval. There has also been an increasing

tendency for Ministers to seek their advice from outside the Department of Forests (This was particularly the case under Ministers Diro and Torato).

Since the 1979 Policy Revision the new forestry scene which confronts a Minister is far more dynamic and includes the following factors:

Post 1979 Scene

- (a) Log exports have become the dominant aspect of forestry and have risen from 472,500 m³ pa in 1979 to 1,442,200 m³ in 1987.
- (b) Local processing has declined in real terms from 77,300 m³ and 106,700 BDU of woodchips in 1979 to 3,508 m³ and 65,700 BDU of woodchips in 1987;
- (c) There are now many foreign timber companies pressing for the right to harvest and export logs. The rewards are so great that they have been able to pay large sums and grant benefits to national and provincial politicians, political parties and landowners in order to gain approval of, and support for, their operations.
- (d) Ministers may think that it is entirely in their discretion whether or not to allocate a resource, declare a Local Forest Area, assent to a Dealing or to reverse these decisions but, in fact, they are facing combinations of Provincial Governments, "stirred up" landowners and foreign timber companies which, once aroused, are very difficult to resist;

The fact that the legislation, technically, gives the Minister absolute power in many of these areas is misleading. He has to take account of landowner pressures. If he does not also take account of pressure from an applicant foreign timber company he is likely to find that the company has stirred up some key politicians and landowners to argue the company's case

and they will exert very powerful political pressure. Under our system of Government he must also seek and take account of the advice of the Department of Forests and other relevant government agencies (see discussion on Functions section 4 below).

Somewhere amidst the interaction between these and other factors the National Forestry Policy has dropped out of sight. I therefore as requested, set about a process of inquiry and analysis in an endeavour to find and define that policy.

Having failed to find an appropriate statement of National forestry policy I listed some requirements for post-Independence national forest management which I believe national policy must address if the resource is to be managed in accordance with the principles set out in the Constitution. The following requirements seemed to be almost essential:

Requirements for Post Independence National Management

(1) There must be a clear statement of the broad principles of a national forestry policy and it must take into account the respective roles of National and Provincial Governments;

(2) The policy must be backed by appropriate legislation which will enable the government to implement the policy and which sets clear guidelines for the exercise of National and Provincial authority.

(3) Synchronised National and Provincial Forestry Plans must be drawn up and regularly discussed by both levels of government on an inter departmental basis and updated. The plans must be consistent with National Forestry Policy.

(4) The plans should be broken down into detailed development programmes for implementation within each province over a (say) five year period. The programmes must be in accordance with short medium and long term National and Provincial plans and policies. Planning should extend right down to the planning of each timber project and, ultimately, to the planning of the forest working operational plan.

(5) The policies, plans and programmes must be based on accurate estimates of the quantity, quality and commercial viability of the forest resource as a whole, and of each forest area under consideration.

(6) Having carefully planned out in this way how the forest resource is to be managed, the National Government must then exercise firm control.

(7) The control must be aimed at:

(a) promoting orderly and planned exploitation for the benefit of the current landowners and the wider public.

(b) conserving, replenishing and developing the forest resource for the benefit of future generations. This means reducing the damage

caused during the operations, ensuring that sustainable yield management is practised (in areas where it is intended that forests are to continue) and ensuring that adequate reafforestation is occurring.

My preliminary inquiries and analysis indicated that none of those requirements for the rational management of PNG's forestry resources exist. I then set out upon a study of the historical development of forestry policy in an attempt to answer Term of Reference 4 and to define what is PNG's National Forestry Policy.

It involved studying the major written materials which would normally give a guide to government policy. These included the Constitution, the Forestry and other legislation and official statements of policy.

Policy Conferences:

During the course of that study the Commission convened several conferences on policy which were attended by Ministers and public servants of several key departments. The aim of those conferences was to promote communication between the Commission and between the various people who should be contributing to the development of forestry policy. In this way the Commission's endeavour to define existing policy would involve all relevant persons and the benefits of the Commission's own policy analysis would be passed on immediately to government officials who had the wider task of formulating PNG's future Forestry policy.

An outline of the historical development of National Forestry Policy is included as Appendix 1 in the hope that it may assist those who are still involved in formulating an appropriate policy. At the conclusion of that outline I formulated broad statements or postulates of the

(theoretical) principles of National Forestry Policies and more detailed implementation strategies which are derived from the documentary sources studied. My aim has not been to formulate what forestry policy should be (as that is outside my terms of reference). My aim has been to look at all major documentary sources and to draw from them broad policy postulates (ie what policy would appear to be from reading these major "governmental" statements).

I now reproduce the broad policy postulates here in the text (without further reference to the sources) as a kind of "policy platform" from which to examine the performance in practice of successive National (and provincial) governments. The policy postulates are consistent with, the detailed policy formulation of the 1974 White Paper and the 1979 Revision but I have taken into account also the attainment of Independence and the introduction of Provincial Government. The policy postulates are also consistent with, but fuller than, the most recent paper of "The Renewable Resources Working Group published as part of the Government's Medium Term Development Strategy 1989-93 Vol 4: Forestry Subsector.

BROAD POLICY POSTULATES

1. WHILE RECOGNISING CUSTOMARY OWNERSHIP OF FORESTS ON CUSTOMARY LAND ALL FORESTS WILL BE TREATED AS A NATIONAL ASSET TO BE CONTROLLED BY THE NATIONAL GOVERNMENT.
2. PROMOTE THE ORDERLY EXPLOITATION OF THE FOREST RESOURCE WHILE AT THE SAME TIME PROTECTING AND EXPANDING IT FOR THE BENEFIT OF FUTURE GENERATIONS.

3. DECENTRALISATION OF THE FORESTRY INDUSTRY TO AN EXTENT SUFFICIENT TO SATISFY LEGITIMATE DEMANDS FROM THE PROVINCIAL GOVERNMENTS FOR INVOLVEMENT IN DECISIONS AFFECTING THE SOCIETY, ENVIRONMENT AND THE ECONOMY OF THE PROVINCE.
4. PROMOTE EQUALITY BETWEEN CITIZENS IN THE SHARING OF BENEFITS FROM FORESTRY EXPLOITATION AND STIMULATE THE ACTIVE PARTICIPATION OF PNG CITIZENS IN FORESTRY AND ASSOCIATED ENTERPRISES.
5. THE GOVERNMENT TO ACTIVELY FIND TECHNIQUES FOR PROMOTING "PAPUA NEW GUINEA WAYS" AND PAPUA NEW GUINEA FORMS OF TRADITIONAL ORGANISATION AND SOCIETY AS AN INTEGRAL PART OF FORESTRY EXPLOITATION.
6. STRICT CONTROLS ON FOREIGN INVESTMENT IN THE TIMBER INDUSTRY TO STOP IT ATTAINING A POSITION OF DOMINANCE TO THE EXTENT IT WOULD COMPROMISE PNG'S NATIONAL INTEGRITY.
7. THE STATE TO BECOME A PARTICIPANT IN MAJOR TIMBER ENTERPRISES.
8. TO ENSURE A FAIR RETURN TO LANDOWNERS THE STATE AND PROVINCIAL GOVERNMENTS FROM TIMBER ENTERPRISES.
9. PROMOTE MEDIUM AND SMALL SCALE FOREST PROCESSING AND ASSOCIATED INDUSTRIES OWNED BY NATIONALS.
10. DEVELOP LARGE SCALE PERMANENT FOREST INDUSTRIES INTEGRATED INTO A PERMANENT FOREST ESTATE PROCESSING TIMBER AND OTHER FOREST PRODUCTS AND PROMOTE ON SHORE PROCESSING GENERALLY.

- 11 INCREASE FOREIGN EARNINGS AND SUSTAINED ECONOMIC GROWTH BY PROMOTING LOG EXPORTS.

- 12 TRAINING
DESIGN TRAINING PROGRAMMES WHICH ARE RESPONSIVE TO MANPOWER NEEDS OF THE GOVERNMENT FORESTRY AND FOREST INDUSTRY SECTORS.

- 13 RESEARCH
CONDUCT AND COORDINATE RESEARCH DESIGNED TO ACHIEVE NATIONAL FORESTRY POLICY REGARDING MANAGEMENT, UTILISATION AND CONSERVATION OF THE FOREST RESOURCES

ASSESSMENT OF POLICY PERFORMANCE

Policy Objectives 1 and 2 are best considered together.

POLICY POSTULATES

1. WHILE RECOGNISING CUSTOMARY OWNERSHIP OF FORESTS ON CUSTOMARY LAND ALL FORESTS WILL BE TREATED AS A NATIONAL ASSET TO BE CONTROLLED BY NATIONAL GOVERNMENT.

2. PROMOTE THE ORDERLY EXPLOITATION OF THE FOREST RESOURCE WHILE AT THE SAME TIME PROTECTING AND EXPANDING IT FOR THE BENEFIT OF FUTURE GENERATIONS.

These two policy objectives contain three main concepts which should be fully discussed in the light of what is actually happening in practice. These concepts are:

- i) customary ownership
- ii) national control and orderly exploitation.
- iii) protection and expansion of the forest resource for future generations

These are really intended to be the basic concepts behind PNG's forestry policy and they are derived directly from the Constitution itself.

CUSTOMARY OWNERSHIP

Determining who are the owners of land by custom is important when purchasing timber rights, when appointing agents to represent the owners, when signing certificates of authority certifying that the signatories to Dealings represent the true landowners and at all other times when the interests of the owners by custom must be considered.

In this regard there are two main areas of concern.

Firstly what does "customary ownership" mean?. Rarely, if ever, is there a thorough investigation into the nature of customary ownership in a particular area. Is it correct to assume (as we now do) that all members of a customary land group must agree to, and sign, the purchase document or in some areas should agreement of a land chief be sufficient agreement if made on behalf of his or her people according to custom.

The Forestry (Private Dealings) Act seeks to avoid this problem by the appointment of Agents certified by the Prescribed Authority as representing the owners by custom. This merely sweeps the problem under the carpet as, on the evidence before the Commission, Prescribed Authorities (in the few areas where one has been appointed) rarely make an independent investigation into customary ownership. The Authority in each case has been the Provincial Secretary and he simply signs the Authority when it is presented to him.

For instance in the case of Tabar (IR No 4 Vol.2 App.2) and Napanta Nubui (IR No, 4 Vol.4A App.7 p. 67-8) the New Ireland Secretary signed documents prepared by the lawyer acting for the foreign timber company in a matter of minutes and without any investigation at all.

A very recent development has seen the position of Prescribed Authority being politicised by the appointment of a Deputy Premier (who is also a leading member of one of two disputing customary landowner groups). (See IR No 7).

Secondly, when an attempt is made to gain the signature of all customary owners it is rarely obtainable as some are away and some refuse to sign. In most cases operations have nevertheless been allowed to commence. This often happens upon the delivery of a "letter of intent" (to allocate) signed by the Minister or Secretary. Often the TRP is never completed and yet Permits have issued and operations have commenced and have been completed. (For some examples see; Kumusi Timber Co. IR No.5 App.3, Danfu extension IR No.4 Vol.3 App.6 and SBLC IR No.6 Vol.3 App.5).

It is obvious that it is not policy that the rights of all landowners must be protected. Normal policy is to allow the operation to go ahead if 75 percent of the owners agree. What legal rights the remaining owners who were not consulted, or whose objections were ignored, may have against the government and/or the company has never been tested in Court.

NATIONAL CONTROL AND ORDERLY EXPLOITATION

For the national government to control the orderly exploitation of the forest resource effectively, and in the national interest, requires that at least the following basic requirements must be met:-

- (1) clear policy aims
- (2) accurate knowledge of the resource
- (3) proper plans
- (4) appropriate laws
- (6) monitoring and enforcement of conditions
- (5) honest independent leadership.

The requirements of control and orderly exploitation are so crucial, and so obviously lacking, that they deserve consideration in some detail.

(1) Policy aims Although there is no full clear statement of National Forestry Policy, it has often been said that its basic aims must include these first two basic policy objectives now under discussion.

- i) orderly development/exploitation for immediate benefits to landowners, governments and people; and
- ii) conservation and replenishment of the resource for future generations

(2) Knowledge of the Resource

One of the first prerequisites is to have knowledge about the quantity and quality of the commercially viable resource, province by province and area by area, so that areas, or even whole provinces, are not overcut in ways which damage or destroy the resource. The National

government should have an accurate, area by area, forest inventory. It should have knowledge of the rate of growth of the major species in these areas so that it can determine how soon a logged over forest will be regenerated. It needs to know exactly what it means by the term "sustainable yield forestry" and be able to apply it to each forest area being considered because it is said that

"The guiding principle for all forest development shall be sustained yield management"

("The Renewable Resources Working Group Paper 1988)

The Commission's detailed study of New Ireland and its brief study of Manus Province have convinced me beyond doubt that the National Government does not have this basic knowledge of the timber resource in these two provinces. On the evidence given at public hearings and policy conferences and from my study of files and statistics made available by DOF I believe that the figures included in the National forest inventory are similarly and dangerously unreliable. To compound this problem, because of years of neglecting research into forestry matters, the Government is shamefully ignorant of the basic growth characteristics of our major species. (See 1R No 4 Vol 1 Sched 1 and 1R No 5 App. 4). Without this basic knowledge it simply is not possible to manage the forests according to sustainable yield principles.

(c) Proper Plans

To ensure orderly development and protection of the future resource in accordance with National Forestry Policy, requires there to be a National Forestry Development Plan which is consistent with the clearly stated National

Forestry Policy. Perhaps because the policy is nowhere clearly stated, there is no National Forest Development Plan.

Do we plan to reduce log exports from certain provinces, to convert so many hectares of grassland to forest plantations? Do we intend (like the Indonesians) to abolish log exports in favour of plywood manufacturing? Is it our plan to work out, on an interdisciplinary basis and in conjunction with Provincial governments, total land use plans for certain areas deciding which forests should be selectively logged and regenerated, which land should be converted to plantations and which forests (if any) should be clearfelled for a more suitable land use, such as an agricultural or cattle project?. Is there a plan to educate landowners about the potential benefits and dangers of a logging operation and to prepare them to be capable of protecting the interests of their environment and their own social and economic well being? These and many other questions should be answerable by reference to a continuously updated National Plan.

To work up a National Forestry Development Plan would force our professional foresters, bureaucrats social and physical scientists and politicians to face and resolve certain very basic issues. As implied by the Constitution and Organic Law on Provincial Government the process of developing a creative and practical national forestry plan would have to involve full co operation with the Provincial Governments and would encourage them to prepare compatible and matching provincial plans. The planning should include short, medium and long term plans.

At present there is only a National Forestry Development Programme which merely lists the areas for allocation by name, size and volume and schedules the timetable for allocation. Such a schedule for allocation should have come after the long term and more detailed medium and short term plans had been thoroughly thought out and co ordinated. Before deciding upon the programme for allocating resources it is necessary to consider and provide for many social and economic considerations. These include things like the need for ensuring a continuous supply of resource to major towns and long term processing plants, the possible advantages and disadvantages for the road network of the area, whether the customary owners have been prepared for the project and a hundred other considerations. Some of these matters are undoubtedly thought about during the process of compiling the programme but there is no predetermined and coherent integrated plan.

The NFD Programme 1987-1991 proposes to allocate over 4.5 million hectares of additional forest land to be harvested, mostly for log exports. The bottom line of the sum has been written before the "planning" calculations.

The planning must take account of the current constitutional and political situation which consists of a decentralised system containing national and provincial governments. As a matter of law and practice planning will not work unless the plans have been worked up in conjunction with, and taking account of, the legitimate aspirations of Provincial Governments which, under the Organic Law on Provincial Government, exercise concurrent power over Forestry. Few provinces have developed a provincial forestry plan but all should be encouraged to do so. It should be developed in close co operation with the National

Government and should be in accordance with national policy aims which, in turn, must be in accordance with the Constitution.

With compatible and "Constitutional" plans in place at national and provincial levels the Minister's authority will be immensely strengthened when he tries to resist the strong demands which frequently come from "foreign inspired" landowners and individual politicians in the provinces. If demands for an unplanned LFA declaration are made, the National Minister would be able to simply point to the Constitution which directs protection and wise exploitation of the resource and to the carefully prepared plans which are truly based on sustainable yield management and genuine social and economic considerations.

He could then refuse to make such declarations on the grounds of "national interest" and the Courts would support him if he is challenged under Section 8 of the Forestry (Private Dealings) Act.

The example of Manus is a good illustration of how such a system of genuine national control, exercised in harmony with provincial aspirations, could work (and how at this stage it seems not to have worked). The Manus Provincial Government is one of the few provinces which have a Provincial Forestry Plan (See I.R No. 5 App.4 Sched.1). This plan is compatible with both the Constitution and the scattered expressions of National Forestry Policy. If there was a National Forestry Plan the Manus Plan would synchronise well with it, as it takes careful account of the known size, quality and regrowth rate of the resource and the social, economic and environmental consequences and possibilities of a large scale logging operation in the Manus island environment. The plan relies upon the establishment of a veneer mill from capital raised from a

three year, carefully controlled, logging operation and is designed so as not to exceed the rate of cut which could be sustained continuously. The West Coast Manus TRP area had long been on the National Government's list of priorities and all aspects of its allocation to a local landowner company, and of its contracting out the logging and marketing to SEAL Pty Ltd, were handled well. At that stage there was close co operation between the two governments. What was missing however was a National Forestry Plan which would have planned to hold in reserve the balance of the island's resource to ensure that the proposed veneer mill would be assured of a continuous supply of timber, cut at a safe and sustainable rate. This would have been for the long term benefit of all resource owners and of the Province (and therefore of the Nation as a whole).

Without such a National Plan, when two small landowner groups, backed by determined and frustrated foreign timber companies, applied for the declaration of LFA's over the balance of Block 1, the National Minister capitulated, saying that he felt he had no grounds on which he could refuse. (See I R No.5 App 4 and IR No 7).

Another example is the unexpected application from the Gulf Province for the huge 187,733 ha. Turama LFA. The pressures from Provincial Government and landowners were so strong that Acting Forest Minister (and Prime Minister) Pias Wingti actually signed the LFA declaration but then, wisely, refrained from gazetting it. Forests Minister Horik then visited the area and, under great pressure, negotiated an agreement with the landowners and the Provincial Government that a Permit would be issued within (3) months.

This was not in accordance with any National Plan and resulted in manpower being diverted in a desperate effort to commence TRP procedures, surveys and other essential work within the arbitrarily imposed time frame. The Permit was issued on schedule but the process was, unavoidably, seriously defective.

This drama occurred during the course of this inquiry and so a summary of the allocation of the Turama Permit is included in Interim Report No 7.

The list of unplanned allocations which were rushed through with very serious consequences is very long. Some of these are reported upon in the various interim reports:

Wawoi Guavi Timber Permit (IR No 5 App.1)
 Turama Timber Area (IR No.7)
 Goodwood's permit area (IR No.2 Part 2 App.39).
 Bruce Tsang's operations at Kotmanse, Noatsi
 East Kaut TRP, Kabil area and Napanta Nubul.
 (all described in IR No.4 Vol.4 App.7)
 Danfu Extension (IR No.4 Vol.3 App.6)

When the National Government is so often allocating resources as an unplanned reaction to pressures from the Provincial Governments, landowners and/or timber companies, it is inaccurate to describe the process as occurring under firm National Government Control or as orderly development.

Project Planning

When a project which has been included in the (non-existent) Forest Development Plan is ready to be advertised and implemented the next vital step should be to plan the project, deciding what benefits should be achieved, for whom and how to obtain them. This will be a fine balancing act

as the National Government, the Provincial governments and the landowners all have competing claims to share the benefits; depending on the nature of the area and the needs of the people. The most desirable benefits could, in a particular area, for instance, be to insist on reafforestation or on clear felling for use in agriculture; in other areas it could be more beneficial to insist on local processing, which could be designed so as to provide job and associated business opportunities. Some projects may be situated in areas where it would be sensible to insist on the construction of a section of the national or provincial highway system.

To plan the project, of course, requires very accurate knowledge of the value of the resource and the cost of extracting it as, without this knowledge, it is not possible to assess the value of the "benefits" which can be extracted from the project while still leaving the company sufficient profit to encourage it to take the risks involved.

To decide upon the desired conditions and how to divide them between the three legitimate claimants requires full consultation between relevant government departments. Thus the Department of Lands must be consulted and be fully and effectively committed to making the necessary land available for such purposes as re-afforestation and urban development, the Department of Works must be fully involved to ensure that any roads, highways and bridges are as compatible as possible with National and Provincial plans and design standards. One consideration which must of course be taken into account is the future road maintenance costs, as the country-side is presently despoiled in timber areas by deteriorating roads which Provincial Governments have no

funds, and sometimes no desire, to maintain. Quite obviously the package of benefits to be written into the project plan requires the fullest possible consultation and co operation with the relevant provincial government.

The next requirement to get a project off the ground is to negotiate with the successful applicants to obtain the desired conditions and (importantly) to ensure that the applicant is capable of fulfilling them and is not merely making wild promises in order to "win" the concession. If no applicant measures up to the project requirements the concession should not just be let out to the highest bidder.

This has frequently been the case and Permits have been issued which bring in pathetically small returns to the landowners and provincial governments merely to get a project started and some level of revenue flowing. In many cases it would have been better simply to postpone the allocation, as many resources have now been exploited for very small returns to the landowners or the government. Examples are Wawai Guavi and Kumusi Timber areas (IR No.5 App.1 and 3 respectively).

Once the conditions are agreed upon it is essential that they be incorporated in binding legal documents (Permit Conditions, Dealings and other agreements) in ways which bind the concession holder and its contractors. It is not sufficient to merely issue a "letter of intent" which, under the existing legislation, has no binding effect. It is not sufficient to phrase key conditions as merely requiring a feasibility study or to write-in qualifying clauses such as "if it seems desirable to the company".

Constitution. It is a serious challenge which needs to be resolved in the Supreme Court as soon as possible. (See P. Donigi "The State and Property Rights in Papua New Guinea" (published in abbreviated form in "The Times" of PNG July 1988)).

In the middle level of the legislative framework is the Forestry (Private Dealings) Act Ch No. 217. This was enacted in 1971 and introduced a serious inconsistency into the law. It granted customary owners the right to make private dealings with non citizens, thus providing for exploitation of the forests, to some extent, outside the National Government's controlled planning or programming process. The way the Act has since then been administered by successive Ministers and the DOF has resulted in an unnecessary abdication of National authority over allocation of resources and also an unnecessary withdrawal by the DOF from the monitoring and supervisory role of national and provincial foresters. (See full discussion in IR No 4 Vol. 1 p. 35 et seq).

At the bottom level of the legislative framework there simply is no law to control the exploitation of rattan cane and timber harvested (for export) under Native Timber Authorities. There is now a large export trade in cane and logs occurring under the authority of NTA's issued pursuant to Forestry Regulation 17. The regulation was clearly intended to allow sale of timber not exceeding 40 cubic metres for domestic purposes such as building a mission station or trade store.

Under the specific written (but illegal) authority of former Secretary of Forests Mamalai, NTA's or multiple NTA's are being issued to harvest up to 5000 m³ of logs and unlimited quantities of rattan cane. As the Acting Secretary said on oath "the situation is now total chaos".

The administration of the Forestry Private Dealings Act is now right off course. In New Ireland there has been, in effect, a trade in LFA declarations with a corrupt former Premier recommending approvals for cash returns and excessive use of LFA allocations. It has contributed to the destruction of the New Ireland forests. Elsewhere huge areas have been sought as LFAs (eg the 187,733 ha LFA in Gulf Province and a 400,000 ha LFA application in East Sepik. In other areas LFAs have been declared for the benefit of small local pressure groups at the expense of longer term Provincial and/or national planning (eg. the lower Sepik LFA and the Jaha LFA on Manus Island (IR No 5 App 4 and at p 60 above). Both these current matters are summarised in Interim Report No 7.

The fact that the legislation is so inappropriate to cope with existing situations has led the Secretary and his officers to step outside the law and to lead others along that diverging path towards further lawlessness. When the Secretary is advocating procedures which are clearly illegal there is no standard left for junior law enforcers to follow (but there are then precedents to which timber companies can refer when promoting or justifying their own illegal activities).

A clear illustration of how the "extra legal" system has been working is in the Kabil Timber area in New Ireland. In that area Bruce Tsang's company Sakai Management Pty Ltd, having made a defective and unsuccessful application for an LFA declaration, proceeded to log the Kabil area until it cut out. He then applied for Timber Authorities to be issued (after the event) to enable his company Sakai Management to be granted a licence to export the logs. This was issued, illegally, at the express direction of Secretary Mamalai who overruled his own officers who were trying to

enforce the law and seize the logs as illegal forest produce (which they undoubtedly were). In the process of Bruce Tsang's illegal, but officially sanctioned, operation the landowners were cheated, the resource was badly damaged and the moral and legal authority of the government was seriously undermined. (IR No 4 Vol 4A App 7)

Other examples which illustrate this willingness of the government to not only tolerate illegal operations but also to act outside the law itself include the many instances where operations were allowed to commence on the basis only of a "letter of intent" signed by the Minister. These include:

- i) Kumusi Timber Area (I R No 5 App 3) where no Permit was ever issued and the operation has now been completed with serious injustice being caused to landowners. (The government was a major shareholder in this enterprise).
- ii) The Danfu Extension TRP where the Gaisho Company was allowed to operate on the basis of a mere letter of intent despite the fact that the purchase of the timber rights were not completed and a substantial number of landowners were refusing to sign (IR No 4 Vol 2)
- iii) Wawoi Guavi Timber Area. The foreign owner Wawoi Guavi Timber Company operated for two years on the sole basis of a letter of intent (IR No 5 App.1)

Stettin Bay Lumber Co Probably the most surprising "illegal" operation is that of the SBLC in West New Britain in which the National Government holds a 17 percent interest (formerly a 25 per cent interest). This subsidiary of the massive Nissho Iwai Company of Japan has conducted a multi million kina enterprise for seven years on no legal basis whatsoever. It was granted a letter of intent and permission to commence operations at Stettin Bay in September 1982 (which superseded its earlier permits).

Despite its increasingly desperate endeavours to formalise the situation, SBLC was not granted a Permit and received no formal documentation until a Project Agreement was eventually signed in early 1989. Even now no Permit has issued and so SBLC has no legal authority to log. Meanwhile this "illegal operation" has exported about 240 000 m³ of logs and processed about 40 000 m³ of sawn timber per annum. SBLC is committed to invest K75 million to plant up 22,500 ha of forest plantation and its capital expenditure by 1987 already exceeded K44 million (IR No.6 Vol.3 App.5).

(5) Honest independent leadership

The Commission's inquiries have disclosed many instances where the National Minister for Forests and/or the Secretary DOF have failed to exercise control of the allocation process on behalf of the nation. This failure occurs whenever the Minister or Secretary is manipulated by an interested party and is tricked into making a decision biased in that party's favour. Failure of National Government control also occurs when a Minister or Secretary consciously favours a particular party who provides benefits to him personally or to his political party. In those cases the Minister is abusing his authority and not exercising control on behalf of the nation. Instances where the Minister and or Secretary have been manipulated by outsiders include:

- i) **Wawoi Guavi** where Toms of Straits Engineering and Cowan of the FIC by passed DOF and manipulated Minister Diro when he was setting the operating conditions on WGTC. (IR No.5 App 1).
- ii) **Vudal** It occurred in the Vudal allocation where Ward of Weco, working through Cowan and Maraleu of the FIC, tricked Mr Diro into first revoking his decision regarding allocation of the Vudal TRP and then persuaded him to abdicate his decision-making

role, by appointing FIC chairman Maraleu (who was also consultant to Weco) to decide the issue between Weco and a rival company - Timbersales. The permit, naturally, was allocated to Weco. (IR No.3 Vol.1 pp.50-52) I consider this to be another indication that National Control over forestry matters wavers frequently.

- iii) Angus A further example of control not being exercised on behalf of the Nation occurred when Minister Diro made a series of decisions favouring Angus (PNG) Pty Ltd in which company he secretly held 35% of the equity. (IR No 2)
- (iv) Gasmata Resources where Mr Eng obtained pre registration for his company by bribing DOF Secretary Mamalai. (IR No.7)
- (v) Santa Investment paid more than K50,000 for electoral campaign materials for Minister Paul Torato. (IR No.4 Vol 4A p.91).

Many other instances are mentioned in the various interim reports.

With regard to Minister Diro's close business involvement with Mr Eng of Gasmata Resources at a time when Eng was seeking various approvals from the Department of Forests I have given Mr Diro the benefit of the doubt as there is no conclusive evidence that he made Ministerial decisions favouring Mr Eng which were related to the benefits he was receiving from Eng personally, for his political party or on behalf of the people of Central Province. (See section 8 and Interim Report No.7)

Whenever the Minister or Secretary, whose jobs are to decide and implement government policy, steps off the straight path, for whatever reason, the wider "government control" over forestry begins to waver. When vested interests take control of the decision maker by trickery, flattery, bribery or campaign contributions the Government of PNG begins to lose control over forestry.

(6) Monitoring and Enforcement of Conditions

Let us assume that the well planned project, approved in accordance with the carefully conceived forward planning, has commenced to operate in accordance with the legally binding conditions of the permit and/or agreement. To ensure that the National government's control over the exploitation is effective it is necessary that the operation be carefully and strictly monitored. Monitoring must include supervision and enforcement of obligations regarding such matters as infrastructure, logging practices, environmental protection, social and economic development, feasibility studies, marketing, and the the payment of all royalties, duties, levies and taxes. It is also necessary to monitor compliance with approved forest working plans and conditions, about local processing levels and approved levels of cut. Without exception, the supervision of these conditions, in every one of the many projects studied, has been found to be very seriously inadequate.

This serious inadequacy is due to a variety of factors:

(a) Monitoring staff:

- i) Decentralisation of the field services and removal from National control has proved to be an

organisational nightmare. Having no central authority the Minister and Secretary cannot direct, control, administer or discipline provincial monitoring staff (see p 50-51 below);

ii) Staff numbers are totally inadequate. The National Forest Development Programme approved by the NEC in August 1988 accepted that the monitoring service was 107 officers below required strength despite the fact that the rate of resource allocation was rising rapidly. (See IR No. 4 Vol. 1 Sched. 1)

iii) Lack of funds and transport. The shortages witnessed by the Commission were drastically severe and in some provinces had almost brought all monitoring to a stop. In Oro Province for instance Ambogo Sawmills Pty Ltd was openly supplementing the Forestry Office funds and maintaining its vehicle so that it could carry out the essential functions required for Ambogo's own operations (IR No.5 App. 3). In Namatanai the telephone was disconnected for non payment of account and in some other offices the forest inspectors were largely dependent on the major timber company for transportation to and from the logging operation.

iv) Inexperienced officers: Most of the officers doing the field work are young and have little practical experience in logging operations. They do not have the confidence or will to stand up to the companies' tough logging bosses. Having never seen an excellent and responsible logging operation they seem hardly able to even see the recklessly caused damage surrounding them; let alone to rectify it.

v) Lack of support: When clear breaches of conditions were reported to headquarters there were many instances where the young officer's correct recommendations were overruled by the Minister or Secretary who then directed the continuation of the operation, the issue of the permit, the recommendation of the export licence or refused to direct seizure of illegally cut logs. This lack of firm support from the top has undermined the morale of national and provincial Forestry Services.

Examples of this lack of support include:

(i) Angus PNG Pty Ltd IR No.2 where Minister Diro directed the issue of a permit against sound departmental opposition;

(ii) Kabil Area IR No.4 Vol.4A pp 28 - where Minister Diro overruled his Acting Secretary and directed that recommendation should (wrongly) be given for the issue of an export license to Sakai Management;

(iii) Danfu Extension IR No.4 Vol.3 App.6 pp.17-23 where Minister Waka (under pressure from Sir Julius Chan and landowners) overruled advice of DOF and the State Solicitor and issued a letter of intend before the TRP had been completed. It resulted in Court action.

(vi) Lack of committment: Many officers demonstrated a serious lack of committment to their work. Very few seem to have a sense of belonging to a professional forestry service and their personal appearance, work attendance and efficiency levels were low.

One has only to read the history of unfulfilled conditions, unsupervised logging and loading operations, unpaid royalties, undetected transfer pricing, broken promises and severe environmental damage set out in the Commission's Interim Reports to realise that the monitoring system is not working and that existing controls exercised by provincial officers, or directly by national officers, are very weak and, in some cases, almost non-existent.

(All aspects of the monitoring system are exhaustively discussed in IR No.6 Vol.1).

(b) Permit Conditions not adequate

i) Conditions to protect the environment are not project specific. They are far too general as they are expressed, usually, as standard conditions to be included in all permits. (This situation has improved in recent months as the Minister for Environment and Conservation has at last begun to require Permit holders to submit detailed environmental plans pursuant to the *Environmental Planning Act*. This has begun to happen since the matter was discussed at policy conferences organised by the Commission. The conditions on environmental protection written into timber permits and agreements however still need to be tightened up and made compatible with these Environmental Plans. Alternatively (and preferably) the conditions in the Environmental Plan should be deemed to be conditions of the Permit. Possibly all Forest Inspectors could be given delegated authority under the *Environmental Planning Act* in addition to their powers under Forestry Legislation.

ii) Forest Working Plans are not yet required to be sufficiently specific although, again, this situation has improved since the Commission's policy conferences dealing with logging practices and monitoring. Some of the practices recommended by the FAO Research team, a member of which attended the conferences, have been written into the Vanimo Forest Products' Forest Working Plan (FWP). More typically however the FWP is a sterile and unhelpful document which, if submitted as required, often fails to gain DOF approval. Almost universally, however, operations have been allowed to continue despite the fact that the FWP has not been given approval. The cease work order imposed upon Vanimo Forests Products (partly) for failing to present a FWP in the form required by the Permit, which occurred during my visit to the Vanimo Timber Area, is probably the only case so far where DOF exercised this potentially useful form of control over a timber operation. There are many examples where operations continued with no approved FWP.

One of the few companies that regularly updates its FWP and submits it every three months as required, is the Stettin Bay Lumber Company. (Perhaps this is because it is about the only legal document which shows it is operating with government approval, as neither Permit nor Project Agreement had been signed. (IR NO.6 Vol.3 App.5)

At this stage it has not been decided what logging procedures should be insisted upon. There is disagreement whether the conditions recommended by the FAO Research team are practical and economically viable. The team says that there should be a one hundred percent inventory of all bole sized trees in a cutting coup and that the whole logging

set-up should be pre marked on the ground by an appropriately trained professional Forester. Logging roads and snig tracks should be mapped and marked with plastic tapes as a guide to the bulldozer drivers and their width pre determined. The FAO team recommends that all loading ramps should be similarly marked and that they should be of minimum size and number. It recommends that trees to be cut should be marked with an arrow indicating the direction of fall, so as to cause the least possible damage to residual trees and to facilitate the task of snigging the logs out without causing further damage. The FAO team further recommends that residuals to be saved should also be marked appropriately and that, after logging is completed, the coup should be immediately inspected by an officer to estimate the damage which has been caused, and this should be costed out at the company's expense. (See IR No.5 App.2 pp.24 et seq and Schedule 4 for a discussion of the FAO research on which these recommendations are based).

I feel that the question of what pre logging, logging and post logging standards should be applied must be decided as a matter of priority. To help obtain the data upon which that decision should be based a requirement should be written into new agreements that suitable experiments must be carried out, under strict government supervision. Reputable companies conducting existing operations could probably be encouraged to assist also.

Whatever standards are to be set there should be a post logging assessment of damage immediately after logging is completed in each cutting coup and before cutting commences in the next coup. The Forest inspector should be able to simply note the damage and calculate the monetary damage compensation to a pre set scale. The damage assessment

should then be delivered to the Company's bank where the sum would be automatically drawn against a replenishable performance guarantee which the company should be obliged to establish with its bank.

To introduce any of these remedial measures will require the companies to be far better organised, with coups clearly marked, and Forest Inspectors to be far more closely involved in operations in a meaningful way than at present. But this should be a minimum requirement of any controlled and well ordered system.

PROTECTION AND EXPANSION OF THE FOREST RESOURCE FOR FUTURE GENERATIONS

The inability of the National Government to protect the existing natural resource by administering firm control over the allocation process, according to proper plans and by carefully monitoring and controlling the harvesting operations to prevent overcutting and unnecessary damage to residual trees, has been described above. It is also illustrated throughout the various interim reports.

Another way to protect the rights of future generations is to energetically pursue a policy of stimulating natural regeneration after logging has been completed and to promote and enforce an enlightened policy of reforestation. It is quite obvious from my inquiries that this policy also has been sadly neglected.

Natural Regeneration :

An FAO research team has been conducting very useful experiments on improved logging practices and forestry management. Field research plots were recently set up in the Wawoi Guavi and Vanimo Timber Areas and their methods and results are reported upon in IR No.5 App.1 and 2.

Except for this research, being carried out by an outside body, there is really no sign that government policy takes the process of stimulating natural regeneration very seriously. Standard conditions requiring good silvicultural practices are written into the conditions of most operations and the conditions often mention technical words relevant to this silvicultural practice (such as "enrichment planting" and "in line planting" but nothing is expected to be done and nothing is done. Occasionally a forest inspector, confronted by a very bare and erosion-prone, abandoned loading ramp may direct that suitable species should be planted to cover it. It is very doubtful if this is ever done or, if so, whether the young trees would have any after-care. I have seen no sign in the inspection reports that such directions are ever followed up by the forestry officer nor that breach of such silvicultural practice conditions should be used as the basis for formal directions to an operating company.

Reafforestation

The main examples where reafforestation is being carried out systematically and on a large scale are at Stettin Bay Lumber Company, Open Bay Timber Company and to some extent Jant Pty Ltd. These are large companies with substantial processing commitments. SBLC has planted approximately 3 700 ha and plans, eventually, to plant 22,500 ha. (See IR No.6 Vol.3 App.5 for a full report on

SBLC's plantation programme. This is the largest reforestation project. Open Bay has planted 2100 ha and is on schedule with the requirements of its permit. It is obliged to plant 14,000 ha. The current planting schedule is 900 ha p.a. Jant has planted 3720 ha. and is frustrated from further plantings because of the government's inability to make land available. This reforestation is being carried out by Gogol Reforestation Co Pty Ltd which is a joint venture involving Jant (51% and the State (49%).

I examined Jant's plantations briefly and was disappointed that the nursery was an amateurish affair which looked neglected and almost empty. Management complained that its planting programme had come to a halt because the government had not been able to make State land available for development as plantations. I was also disappointed that Jant had made no progress stimulating local agro-forestry projects except that one local landowner (and former Jant employee) had been helped to plant a small plantation underplanted with cocoa. The potential for promoting the development of such plots with Jant undertaking to harvest the timber and process it through the chip mill at a later date seems good but neither Jant, a forestry extension unit or the local landowners are generating much enthusiasm for agro forestry projects.

SBLC's reforestation scheme is described in IR No 6 Vol 3. Although it is the best in PNG the visiting World Bank team confirmed my view that it could be much better and more scientifically progressive if the company's heart was really in it as a long term project on secure title land. (IR NO.6 Vol.6 App.5).

Open Bay Timber Company's reforestation project was not inspected.

The other timber operations are sometimes bound by conditions requiring reforestation but in the majority of cases these have not been carried out. Often the reason is the Government's inability to make suitable land available. Vanimo Forest falls into this category (See IR No.5 App.2) as does Tonolei Development Corporation (See IR No.6 App.9). Other than the three companies mentioned no other company is carrying out any significant reforestation programme.

The National Government's own plantations were handed over to Provincial Government control after Independence and they rapidly began to run down. Provincial Governments are reluctant to spend money or manpower to maintain plantations and are not taking this matter seriously.

The 1979 Policy was to impose a reforestation levy on companies instead of obliging them to carry out the process itself. If the government is collecting this levy it certainly is not being used in reforestation. (At public hearing in the last days of the Commission Forests Minister Stack indicated that in recent months the levy is being collected).

Not only is there little reforestation occurring on the ground (none at all in New Ireland for instance except for Leytrac's small balsa plantings and a small New Zealand aid pilot plot - (both described in IR No.4) only but there is no clear policy position on reforestation. If, for instance, it is now intended for the government to establish and maintain the plantations where are the plans, what sites have been chosen, what species, methods, staff and funds will be used? It is not clear whether plantations should be established on logged over land to build up a replacement forest in that area or whether other land with easy access to a suitable deep water loading point should be chosen.

The feasibility studies and planning for a government or private sponsored plantation/processing operation have not been prepared.

Proper logging practices, under firm supervision and control, followed by appropriate post logging assessment and after care to promote natural regeneration, would go a long way to preserve existing natural forests for future use and enjoyment by later generations.

The establishment of integrated plantation/log export/local processing ventures would also take the pressure off the natural forests and, would be more economical in the long run. They could be planned in such a way as to bring greater benefits for the people and government of Papua New Guinea.

The available evidence indicates that not much attention, effort or funding is being given to the policy principle of protecting and expanding the forest resource for the benefit of future generations.

SUMMARY

At the conclusion of this discussion on the first two principles of policy it is worth restating them as I believe they really are the basic principles which should underlie the national forestry policy.

1. While recognising customary ownership of forests on customary land, all forests will be treated as a national asset to be controlled by the National Government.

2. Promote the orderly exploitation of the forest resource while at the same time protecting and expanding it for the benefit of future generation.

It should be a cause of major concern that the findings of this Commission show that these basic principles are not being observed in practice. My findings on these two policy principles can be summarised as follows :

1. There is no clear national forestry policy - not only no coherent statement of it but no overall policy;
2. There is no National Forestry Development Plan (long, medium or short term).
3. There is very little effective project planning.
4. The accurate knowledge of the quantity, quality, accessibility, commercial viability, and growth rate characteristics of our Forests does not exist. To base allocation programmes on the "knowledge" we have, in the planning vacuum which exists, is to invite disaster.
5. The Forestry legislation is outdated and quite inadequate to provide a control mechanism to govern forestry in post-Independence Papua New Guinea.
6. Such legislation as exists is frequently ignored and contravened by Ministers and Secretaries for Forests and, of course, also by the lower ranks and the timber operators themselves. This is partly due to its inadequateness and its inappropriateness

7. Though the policy is based on recognition of the rights of customary owners of the forest resource, in many instances we take little care to determine who the owners are and whether all, or all the customary leaders, agree to the purchase and or planned allocation of timber rights. The benefits to those owners after the operation commences are almost always unjustly low.

8. Since the understaffed national forestry service was "decentralised" there has been no effective forestry service. The monitoring and control of field operations is consequently very inadequate and it is getting worse as the rate of allocation increases with no corresponding increase in staff.

9. As a result of these various defects in policy, planning and implementation, what has been happening to the national forest resource cannot be described as orderly development.

10. In view of the huge increase in log exports, the lack of control over logging operations and the insufficiency of reforestation and national regeneration practices it cannot be said, either, that the forests are being effectively protected and expanded for the benefit of future generations.

These obvious requirements for exercising national control over forestry, so as to ensure orderly exploitation for the benefit of present and future generations, are easily stated. My inquiries however have uncovered so many practical instances where some, and sometimes all, of these requirements are missing that I have concluded that there is little effective national control over what is occurring. There is no clear policy, no accurate knowledge of the resource and no proper planning. In these circumstances how can national control possibly be exercised effectively? The next requirement for exercising effective control is the ability to enforce the government's will as a matter of law.

(d) Appropriate Laws

Armed with clear policies, accurate knowledge and firm plans, the Minister would then require appropriate legislation to enable him to keep order in the timber industry and to enable him to enforce the policies and implement the plans. Once again, however, this weapon, also, is lacking-and seriously lacking.

Since 1974 the need to revise and consolidate the Forestry Legislation has been recognised as an urgent necessity but, despite specific directions from the NEC and annual "budget time promises" from the DOF, the pre independence legislation is still in force. As mentioned above, the situation has been seriously worsened since Independence and the enactment of the Constitution and provincial government legislation.

At the top end of the legislative framework the whole basis of the National Minister's power to restrain unauthorised exploitation of the forest resource by its customary owners has been challenged as an interference with their property rights in contravention of Section 53 of the

POLICY POSTULATE

- 3 DECENTRALISATION OF THE FORESTRY INDUSTRY TO AN EXTENT SUFFICIENT TO SATISFY THE LEGITIMATE DEMANDS FROM THE PROVINCIAL GOVERNMENTS FOR INVOLVEMENT IN DECISIONS AFFECTING THE SOCIETY, ENVIRONMENT AND THE ECONOMY OF THE PROVINCE.

Legitimate Rights of Provincial Governments

There is no question that Provincial Governments have a legitimate right to be involved in forestry policy making and implementation.

They have responsibilities for the economic and social well being of the province and for provincial planning. The decision whether to allocate a large forest project, and on what terms and to whom, will have major repercussions on the economy, environment, social conditions, road network and (because of royalties and derivation grant) provincial revenue. It will also directly affect provincial expenditure as it will increase the workload of the provincial forestry office and its demand for funds and transport. It could also have a substantial indirect affect on future road maintenance costs as a forestry project will create roads, whether desired by the Provincial Government or not, and unless they are important "National roads", their up-keep will be the responsibility of the Provincial Government. A forestry project will also create other demands on provincial government services in the fields of welfare, law and order and business development.

The Recognition of Provincial Government Rights

The need for provincial involvement was recognised and provided for by Constitutional Amendment No 1 of 1976 which provided for the establishment of the system of provincial governments and by the Organic Law on Provincial Government under which Forestry was declared to be a concurrent subject matter with authority being shared between National and Provincial governments.

After the decentralisation of Forestry was provided for in this way under Constitutional Laws the next steps to convert this ringing pronouncement into an effective policy of decentralisation, and to implement it in practice as regards forestry, should have been to make provisions for:

(a) **Analysis of Government Functions:**

It was necessary to list and analyse all government functions involved in forestry. Such a list would include such functions as:

- i) compile and update an accurate inventory of forest resources;
- ii) formulate and update national forestry policy.
- iii) prepare long, medium and short term national forestry plans for the management of Forest resources in accordance with the national forestry policy.
- iv) prepare long, medium and short term provincial plans for management of forest resources in accordance with the national forestry policy and consistent with the National forest development plan;

- v) Carry out research into the characteristics of the major forest species, (including such things as rates of growth, suitability for processing), forest management, logging techniques, afforestation, agro-forestry, integrated land use techniques, social and economic factors relevant to forestry, marketing of forest products and various types of processing.
- vi) Training at all levels from professional degree courses to short inservice courses on specific skills and village extension work;
- vii) Allocation: Community awareness campaigns, purchasing timber rights, preparing project guidelines so as to ensure appropriate benefits are obtained by State, provincial government and resource owners, evaluating applicants for concessions allocating concessions, negotiating conditions of permits and project agreements;
- viii) Monitoring operations: inspecting logging practices, directing improvements, checking species identification measurements and grades, inspecting road works and construction of infrastructure, monitoring compliance with conditions, checking log returns, royalty payments, loading operations, issuing permits, stopping illegal operations, assessing damages and hearing landowner complaints.
- ix) Marketing: checking FOB prices and shipping details, exercising State Purchase Option and arranging overseas log sales.
- x) Communications: Liase and co operate with all other relevant National government departments and agencies including Lands, Environment, Works, Bureau of Water Resources, liase with provincial governments on all aspects of planning and allocation and monitoring of forest resources.

This list is by no means comprehensive but when it is compiled in sufficient detail, it becomes apparent that any process of dividing the functions between national and provincial governments must be done with extreme sensitivity as each function requires a contribution from both levels of government and both national and provincial governments have an interest in the performance of each function. For instance compilation of national resource inventories and research into forest species may be considered primarily a function of the National government but provincial government staff and provincial resources will be used in the process. If the function is not carried out, or is carried out badly, the forests and people of the provinces will suffer. Similarly monitoring of timber operations may be considered to be primarily a provincial government function but they will be monitoring conditions imposed by the National government and the recommendations of the field staff will (usually) be implemented by an order given by the National Minister.

Granting a permit to exploit a major forest resource may well be done by a decision of the National Minister but the major social, economic and environmental effects will be felt in the province and many of the government actions which will flow from the project will be required of the provincial government.

It follows as a matter of inescapable logic and from practical necessity that, if authority over Forestry is to be exercised concurrently, and therefore shared between National and provincial governments, there must be the utmost degree of shared planning and co-operation between them.

(b) Consultation :

A first step therefore to implement a policy of decentralisation would be to work out devices for consultation between the two levels of government. One obvious way to achieve this would be to introduce interlocking planning programmes. This would encourage national and provincial officers to work together on the National Forest Development Plan and the various Provincial Forest Development Plans so that all voices are heard and all aspirations and requirements are taken into account. Nothing else makes sense.

(c) Reallocation of Staff

The reallocation of staff needs to be done in a way which enables the National Policy and the National and Provincial Plans to be implemented by a unified and professional forestry service under a central command structure but responsive to the requirements of both National and Provincial governments. It needs to be a forestry service with adequate opportunities for promotion and suitable postings and which gives a sense of job satisfaction to its officers.

Bureaucratic decision making at provincial level needs to be handled by experienced senior professionals with access to higher promotion and improved job opportunities within the province or elsewhere. Decision making at National Headquarters needs to be carried out by officers with extensive field service. They need also the satisfaction of knowing that there is authority to ensure that decisions are carried out. They will need, however, to be trained in the arts of discussion and co operation and there must be a formalised structure to ensure that they are responsive to political direction not only from the National Minister but also from Provincial and/or regional politicians.

(d) Substantive Authority :

If decentralisation is to be meaningful then one would expect to find that power of decision over some substantive matters would be devolved or delegated to the provincial or regional level where Provincial Government can participate effectively in the decision making. The participation in the decision making process can be a mixture of full and effective consultation together with final power over some matters.

(e) Funds:

It goes without saying that decentralisation cannot occur effectively unless sufficient funds are made available to Provincial Governments to enable them to exercise the powers and carry out the functions given to them.

PERFORMANCE OF DECENTRALISATION POLICY

Once again the actual performance of this so called policy of decentralisation has been so poor that one is forced to question whether decentralisation is in fact National Government Policy at all.

(a) Analysis of Government Functions :

No detailed and sensitive analysis of governmental functions in the field of forestry has been carried out with a view to recreating the governmental system to accommodate the legitimate requirements of Provincial governments. Nor has the Forestry legislation been revised with this requirement of decentralisation in mind. The administrative system limps on, somehow, with legislation which places all power in the National Minister who, for practical reasons, is obliged to delegate a multiplicity of powers to Forestry Inspectors (most of whom are in the Provinces and are no longer under his control).

(b) Consultation :

No effective consultative planning procedures have been formalised and informal attempts to formulate inter linking provincial and national forestry plans have come to nothing through the inability of the officers, and their respective political masters, to co operate.

Consequently there is still no National Forestry Development Plan (and this is partly because the planners at the centre no longer have access to reliable information from the provinces where such plans must be implemented).

There are also few effective provincial forestry development plans. This is partly because such plans cannot really be prepared unless the National Government is co ordinated within its own departments and, through the Minister and Secretary for Forests, can put forward to provincial planners what it proposes should be done.

The fact that this interlocking forestry (and wider integrated land use planning) is not occurring is partly explained by an inability to cooperate but it also explains the lack of cooperation. Until the formal planning starts there is nothing to co operate about and few opportunities to do it.

(c) Staff:

Far from carrying out a careful rearrangement of staff to ensure the survival of a unified professional service with high morale and efficient officers sensibly posted throughout the country in strategic places, the method of rearrangement was arbitrary and unbelievably simplistic. As if a mad butcher attacked the carcass of the National Forestry Service with his chopper, all staff who happened to be on posting within a province at the time of the

butchering were simply chopped off the carcass and became the Provincial Forestry Service for that Province. All those at that moment posted at headquarters or in training/research institutions were left on the carcass and became the truncated National Forestry service. Two of the five regional officers became provincial officers and the remaining three were posted to national headquarters. The result has been diasastrous.

At national level there are administrators, decision makers, experienced monitoring experts and planners but they are merely the trunk without arms and legs. There is no one obliged to feed them information or to carry out their orders or to implement their decisions.

The Provincial Services are run by the comparatively junior and inexperienced officers who happened to be on the spot at the time the system changed. They are now cut off from their professional peer group and their lines of promotion. Their career opportunities, professionalism and morale have been seriously impaired.

For the first couple of years the previous "old boy" network continued to operate and there was a (diminishing) residue of respectful cooperation between former colleagues in the defunct national forest service. Thus a senior Headquarters man could request, and usually be given, information, help and obedience from his former junior officer; even though the junior may now be the Provincial Assistant Secretary for Forests responsible, through the Provincial Secretary, to the Provincial Government. As these "network" ties have gradually weakened, and the provincial staff has come under more pressure from the provincial governments, the system has become increasingly unworkable.

During the last year three Regional Offices have been re-established to look after the national interest in monitoring and inspections.

(d) Substantive Authority :

About the only substantive power of decision delegated to the provinces has been the power to issue Native Timber Authorities. Legally this is a very minor power limited to issuing authority for non natives to acquire up to 40 m3 of forest produce from customary owners for domestic use.

With the encouragement of the Secretary DOF this power has been misused to enable the provincial Assistant Secretary of Forests to issue multiple timber authorities to allow timber companies to harvest thousands of cubic metres of timber and to export them. This was being done without any control by the Minister for Forests, and subject to no supervision to ensure that fair benefits flow to the land owners or to the Provincial Government.

Timber Authorities are still being issued by Provincial Forestry Officers to permit the purchase and export of large volumes of rattan cane. This is occurring outside any government guidelines and the situation is now, as previously stated, chaotic.

Another power delegated to the provincial forester is the power to issue export permits. The PFO's have not known the reason for these permits and have been issuing them automatically if the export licence has been issued. (See IR6 Vol.1 p.186 for a discussion of how the power to issue export permits could become a meaningful control mechanism).

Attempts to participate in the exercise of substantive authority by becoming meaningfully involved in the process of planning and consultation have failed because that process is not occurring on any sustained and rational basis.

(e) Funds :

The main source of funding available to the provinces for carrying out their forestry functions is by way of budget allocation.

Budget allocation:

Some provinces are treated as having full financial "responsibility" and tend to receive the major part of their budget allocation in a lump sum to distribute as they choose in accordance with provincial priorities. The amount of the lump sum is calculated by reference, mainly, to the amount which was spent on the present "provincial functions" by the National Government, before the establishment of provincial government. Having received its lump sum in this way it is then up to these "financially responsible" provincial governments to decide how much to allocate for forestry expenditure as opposed to the other calls on their funds.

Provinces which do not have full financial responsibility are, for funding purposes, treated as if they were national government departments and their funds are allocated division by division, item by item. The amount which the National Government will allocate to a provincial government Forestry Division is calculated, in the main, by reference to the amount previously spent on "forestry" in that province before the introduction of provincial government. The way the Division will spend its allocation is also determined by the item by item allocation.

If there has been a substantial increase in forestry in the province since the establishment of provincial government the base figure will probably have been adjusted as a result of negotiations between the provincial and national government bureaucrats.

Royalties:

Under the Organic Law on Provincial Government a province is also entitled to receive one hundred per cent of the royalties paid on harvested timber less the National Government's cost of collecting them. The National Government has been charging 25 per cent of the royalty for this service which is exorbitant and "unconstitutional". As 25 percent was being given to the landowners provincial governments have usually been receiving only 50 per cent of royalties. (Currently the landowners are receiving 75 per cent and the provincial governments only 25 percent of royalties. The State is allowing its share to be paid to the landowners in an attempt to give them a fairer share of the returns from timber operations.

Derivation Grant:

Provinces are entitled to a grant calculated upon the value of the exports produced in their province. For forestry this amounts to 1.25 percent and is taken from the State's export duty collection of 10 percent of FOB price.

Unfortunately for the "forestry" provinces however, the derivation grant is reduced by the total value of all royalties paid in the province. In the past this rule has been applied in a way which actually produced a negative effect for, if royalties exceeded the derivation grant it not only cut out, but further deductions to the province's budget entitlements used to be made to off set its "royalty windfall". The negative effect has now been removed and the effect of receiving royalties which exceed the amount of the

calculated derivation grant entitlement is merely to cut out the derivation grant completely.

Grant by way of a National Forestry Programme: The only way for a provincial Government under this system to obtain a prompt increase in its allocation to allow it to promote provincial forestry is to persuade the national government to include its desired project in a National Forestry Programme and obtain NEC approval for it. Thus in the early 1980s small provincial forestry programmes were included as part of Primary Industry Sectoral Programmes. The experience has been that such funds are easily diverted by National or Provincial politicians to "non project" purposes. This happened to Simbu reforestation funds in 1981 and 1982 so in 1983 the project funding was stopped.

Up until 1987 DOF did not submit its own National Forestry Programme and so no extra boost up for Forestry occurred through that means prior to that date. When the National Forestry Development Programme 1987-1991 was given NEC approval it set out on the one hand a timetable for an accelerated programme of allocation of forest resources. On the other hand it included a list of requirements for staff and funds to enable the programme to be carried out. The programme was approved "subject to funds availability". Although the timetable for allocation has been approved and implemented the staff increases have not been funded. As a result the monitoring capability will inevitably deteriorate even further.

The process of communication and negotiation on funding between provincial and national government is, like the communication on planning, not functioning well. For the financially "responsible" provinces a lump sum is handed down after discussions between the Finance sections of both levels of government. The process of sub dividing that

total between various provincial divisions and projects is left entirely to the provincial budgetary process. In the financially dependant provinces the inter government discussions occur between the two finance sections and then the amounts are allocated to each provincial division.

There appears to be no satisfactory process whereby joint planning and funds can be discussed horizontally between the various divisions in the province and within the National Government nor a process whereby the vertical inter-government planning and funding negotiations can occur.

This weakness was recognised in 1988 when a National Provincial Relations working group was established to try and improve National/Provincial communications on such matters. It is said to be making some progress.

The performance by successive national governments in implementing the policy of decentralising the forestry functions is very unimpressive on vital matters regarding division of functions, consultation, staffing, transfer of power and provision of adequate funds.

The performance of the provincial government in exercising the powers they actually do have, and in administering such functions as they have been given, is also very unimpressive.

(f) Legislative Power

"Forestry" is listed in the Organic Law on Provincial Government as a concurrent subject matter. It follows, therefore, that provincial governments have the power to enact legislation on any aspect which is not already covered by national legislation. Potentially this is an effective

power which has been "decentralised", particularly as the National legislation is so inadequate and leaves so many gaps which could be filled by provincial legislation.

This potentially effective power has been ignored by Provincial Governments right up until now when the Manus Provincial Government has just enacted a law to try and strengthen its policies on forest management by enshrining it in legislation. (See discussion in IR No 5 App 4).

(g) Joint Ventures:

Another way for a provincial government to promote the decentralisation of the forestry function could be for provincial governments to become partners in major projects operating as a joint venture involving the foreign timber company and the provincial government and perhaps also a landowner company. For this to amount to decentralisation, the joint venture agreement would need to ensure that the provincial government gained an effective measure of control and a fair share of reasonable profits.

The few attempts by provincial governments to participate in the process of forestry by way of involvement in joint venture operations have also, so far, been a costly failure:

Participation in Kumusi (IR No 5 App 3) and Ulabo as Forest Development Corporations failed to give the provincial governments effective control in the operation or shares of its profits. In fact substantial losses were incurred with very few benefits for the landowners, provincial government or people. Participation in Stettin Bay Lumber Company was by the National Government. When a chance was offered to take up more equity the National Government refused and the chance was not offered to the Provincial Government. The State also took 20 per cent

equity in Open Bay Timber Company. The huge losses made by this company are dealt with on page 104 below (and IR6). The State also had equity in Ulabo Timber Co. and Wewak Timbers (see below p.105). The latest joint venture attempt is in Manus Province where the Provincial Government is a major shareholder in the landowner company Kei Besau Kampani which, in turn, proposes to enter a joint venture arrangement with SEAL to operate a veneer mill. (IR No.5 App.4 and IR No 7).

Provincial Forestry Offices

The lack of funding, lack of staff organisation, effectiveness and morale and, generally, the lack of government commitment to meaningful decentralisation of forestry matters was very evident from the state of the various Provincial Forestry Offices which I visited. The Commission saw offices with no telephone, no adequate transport, no overtime funds, and no funds for field work.

The five Provincial Forestry Offices whose performance the Commission examined in some detail present a very dismal picture of the decentralisation process in action:

Central Province Central Province forestry officers have been quite unable to supervise and control nearby operations where gross illegalities have been occurring. Under their very noses the Amazon Bay Sawmills operation continued for years as an illegal operation based on improperly issued timber authorities. It failed to start up its sawmill and merely harvested logs for export inside, and probably outside, its concession area. It built up a deep sense of resentment and divided the community. The community leaders have now "impounded" the Sawmill and equipment as "Security" for a claim for unpaid "commission" on log sales which was promised in writing but not paid.

The Goodwood operation is woefully behind in its permit conditions and is reported to be breaching its conditions regarding environment and logging practices. It is now over one year late constructing its sawmill and has continued to operate with apparent impunity. (Action to cancel the permit is now under consideration).

The three forestry officers located at Kupiano to oversee operations of Goodwood and MacDui did not even have a bicycle between them to travel to operating sites.

MacDui. This company purchased the ANG sawmill at Kapari and related facilities at Kupiano. It was originally allowed to cut logs for its sawmill on T.A's issued by Central Province Forestry Office. The company had a completely inadequate capital base and pressed for log exports to produce funds. It was then allowed to stock pile logs for export until it persuaded the Secretary to grant permission to export. The shipment of export logs ended up being a disaster.

Luabar Logging Pty Ltd was able to illegally harvest and exploit teak from Brown River, in close proximity to the Forestry Base there, through an outlet at Bootless Bay, 20 minutes drive from the Central Forestry Office. It was also able to commence another illegal operation under the guise of building a road to the Iva Inika timber area until it was interrupted by the Commission's own inquiries. On inspection by the Commission it was found that about 5000 - 6000 m³ of illegal logs were awaiting shipment. (Some of the logs were then seized and sold by the State for the benefit of the landowners. Others have been allowed to lie in the bush or at bush ramps and not as DOF could not extract them).

The practice of issuing Timber Authorities illegally to allow short term "hit and run" timber and cane operations is rampant at Central Forestry Office. After exposure by the Commission the delegation to issue such Authorities was withdrawn from the two senior officers (by revoking their appointment as Forest Inspectors).

At the the Brown River Station the Commission found 16 staff stationed though there is little work for them there since the plantations had been handed back to customary ownership. They stayed because there is accommodation there but, because there is no transport, many of them are seriously underemployed. Some use private transport to attend at the town office.

One of the middle level officers Dennis Hoivo was found to have wrongly accepted K1,000 cash from Angus (PNG) for "services rendered" when he was supposed to have been overseeing the loading of an export log shipment.

The Provincial Forestry Officer Misi Henao was found to have paid royalty moneys into and out of his own private bank account and to have retained funds in that account in cases where entitlement to royalties was "disputed". Such a practice constitutes an invitation to misuse funds but in the period studied, Mr Henao had not yielded to that temptation.

Oro Provincial Forest Office: This office was desperately starved for funds and had no access to permanent transport. Morale was very low and the office was almost inactive. The loading operations at Oro Bay were dominated by Sumitomo, had not been inspected for two years and

provincial forestry funds had on two occasions been supplemented by Ambogo Sawmills. (IR No 5 App 3). Since my inspection the office has burned down with the loss of all records.

West New Britain: This office was visited only briefly and it was noted that the administrative organisation within the province was inappropriate, as the head forester was out of touch with his District Foresters, had no easy access to transport and did not report directly to the Secretary of the Province but through a non specialist District Manager with no forestry experience. At Dami Station (only five miles from SBLC's mill) there was a general air of lethargy and neglect with officers sitting around doing nothing because "no transport".

New Ireland: The Forestry Office there was led by Mr Jack Masu who I have found was far too closely involved with some of the timber operators and gaining benefits from them. He received a regular supply of beer by the carton from Bruce Tsang and was obviously a heavy drinker with little commitment to his work. It is perhaps not surprising that his commitment is weak as he was for several years the top forester responsible to Premier Robert Seeto's Cabinet and somehow managed to survive in a situation where cronies like Seeto, Gila and Watt (as unofficial Cabinet Adviser) were planning to formalise an existing practice of selling political favours to timber companies by developing it into a full scale extortion racket, using Watt's Company, Niubils Consultancy, as a "front". (see IR No. 7).

Far too many staff were posted at Headquarters and in other "no work" locations instead of being posted to where the action is.

Western Province: The inspection of this office showed that attendance was poor, and efficiency low. It had no access to vehicle transport and no funds for flying. The Assistant Secretary and another officer were investigated for possible misuse of royalty funds and the junior field officer has been charged. One officer is placed full time at the WGTC project which is almost the province's only project,. He had recently arrived and was still keen. One wonders how long this will last though as he is isolated away from his fellow officers in a very wet environment where he is dependent on the company for all his basic needs - company house, company transport, food purchased at company store and companionship of company employees. The only recreational facility is the company mess. It would be extremely difficult for him to form and express a strong critical view of the company's operations in these circumstances.

West Sepik: The Vanimo Forestry Office was a ten years old, "temporary" bush materials building with thatched roof. As the headquarters of a forestry division administering a major project it was an absolute disgrace. It can only be a matter of time before it burns down with all the records, as has already happened at Popondetta.

The Provincial Forestry Office has only one vehicle and finds it difficult to gain access to the Pool Car. Very little effective monitoring of VFP's operation was being carried out by the Provincial Foresters. More was being done by the National Project Team which should however have been doing other tasks. Despite the existence of a National Government Project Coordinator, horizontal communication between provincial departments and vertical communication with National Government Departments seemed to be poor. (See IR No 5 app 2)

SUMMARY

There is then very little sign that decentralisation is an active element of national Forestry Policy. Despite the provisions in the Constitutional Laws which first raised the issue the Forestry Legislation does not promote or even recognise decentralisation. There is no integrated national and provincial planning which effectively involves the provinces in planning the exploitation of the resource. National Forestry Development Programmes involve a degree of consultation but that process is frequently by passed when "outsiders" interfere with the process or when National Ministers respond unexpectedly to pressures, promises and payments and allocate resources outside the scope of the current programme. Staff has been reorganised in a way which creates confusion and stagnation. There is no meaningful involvement of provincial governments in a dynamic process of developing a national forest resource. No meaningful final power of decision making has been devolved or delegated to provincial governments (except delegation over timber authorities) and the funds being expended on provincial forestry are inadequate to provide the manpower, transport and facilities required to carry out their tasks. The potentially effective power to legislate on Forestry matters, which was granted under the Organic Law on Provincial Government, has been used only by the Manus Provincial Government. (Though the East Sepik legislation on land mobilisation will have an effect on forestry see p 121 below and IR No.7)

POLICY POSTULATE

- 4 PROMOTE THE ACTIVE PARTICIPATION OF PNG CITIZENS IN FORESTRY AND ASSOCIATED ENTERPRISES AND ENSURE THEY RECEIVE A FAIR SHARE OF THE BENEFITS

It has been accepted that foreign enterprises and foreign capital will be required in order to exploit PNG's forests but it is clearly accepted (if not stated) policy that, after the foreigners have received a fair return for their money and effort, the benefits flowing from forestry exploitation should flow to Papua New Guineans. The landowners in particular are not to be left as idle spectators while their forests are felled. They must be enabled to participate in forestry and associated activities. They must also of course receive a fair share of the proceeds from the sale of their logs. Papua New Guinean participation and sharing can occur at the level of the landowners and their clan groups, incorporated landowner companies, Village and Provincial Government Development Corporations, Provincial Governments and the National Government.

Various methods have been devised to stimulate this type of Papua New Guinean involvement and benefit sharing.

- A. Timber Rights Purchase and Royalties
- B. Ownership of the permit or price sharing arrangement
- C. Premium arrangement
- D. Promotion of business and economic development
- E. Local processing benefits
- F. Employment opportunities

A. Timber Rights Purchase and Royalties

The purchase by the State of the Timber Rights and the subsequent distribution of royalty payments is of course a benefit to customary landowners. As discussed elsewhere however this benefit is far below the true value of the resource. (See IR No.5 p.35). In 1987, out of total royalties amounting to K5,597,015 only K1,399,253 was paid to landowners.

B. Ownership of the Permit

Various ways have been tried to give Papua New Guineans equity in the corporate vehicle which holds the Timber Permit. The idea is to give them some control of operations and marketing "from the inside" and a share of the profits.

(a) Forest Development Corporation: This concept was put forward in the Revised National Forestry Policy 1979. The two main examples are Kumusi Timber Company and Ulabo Timber Company where the Provincial and National Governments became the major shareholders. In fact the foreign manager retained full control and no profit was made for distribution to shareholders. In the Kumusi Area the governments and landowners suffered severe losses (see IR No 5 App. 3)

(b) Large active National Company:

Several attempts have been made to form companies with at least 75% of the shares held by Papua New Guinea citizens or organisations. The intention was for the company to be actively involved in the control of the operation.

Two examples studied by the Commission were Angus (PNG) Pty Ltd and Wawoi Guavi Timber Company. Both were in fact foreign owned but put up a sham "national" front (See IR No 2 and IR No 5 App 1). In neither case did Papua New Guineans gain control or a share of any profits.

Two other examples of smaller companies, which were not studied in detail by the Commission, are Tonolei Development Corporation and Bougainville Forest Enterprises Pty Ltd. Tonolei appears genuinely to be owned by land owning groups and it has very recently sought to buy out its contractor. It should now be in a position of genuine control and its Papua New Guinea landowner groups should be well placed to receive the profits by way of dividend distribution. (See IR6 App9)

Bougainville Forest Products is managed by Groomes and sells through Sumitomo. Aspects of its marketing are reported upon in IR No.6 Vol 2B App 6 but nothing else has been studied.

(c) "Inactive" Landowner Companies:

Many small companies have been established with landowners being involved as the shareholders. Sometimes these companies genuinely represent landowning groups sometimes they comprise or include "outsiders" whose claims to be considered as landowners are often hotly contested.

The great majority of these "landowner" companies are organised and incorporated by the foreign timber company which proposes to carry out the logging and marketing as contractor pursuant to a logging and marketing agreement which, theoretically, should be approved by the Department of Forests.

It is common for the foreign contractor to provide its own lawyer, consultant and accountant, and sometimes its secretary, to ensure that the landowner company applies for the Permit, LFA Declaration, Assent to Dealing or approval of the Logging and Marketing Agreement. If it takes too long to gain approval for these formalities the contractor frequently commences work (illegally) and orchestrates the landowner company to support and protect its illegal operation until the formalities are completed. In all except three cases studied by the Commission, the landowner company was a mere puppet created to enable the foreign timber company to gain access to the resource. Such landowner companies do not participate in the operation at all. The exceptions are the Djaul Development Corporation from New Ireland which made a genuine attempt to control the operations of its "contractor", Gaisho Co (NG) Pty Ltd. DDC has recently started in business itself (IR No 4 Vol 2). Another possible exception is Tasukolak Pty Ltd from New Ireland which, after starting off as "puppet" from the beginning, is now showing some signs of an independent business life of its own (IR No 4 Vol 3). Most recently the Kei Besau Kampani was incorporated to hold the West Coast Manus Permit and (eventually) to be a joint venture partner with its contractor SEAL Pty Ltd. KBK is partly owned by landowner groups and partly by the Provincial Government (IR No 5 App 4)

Whether the so called landowner companies receive fair benefits from the timber operations will depend upon:

- 1) whether the Logging and Marketing agreement provides for a fair division of the FOB price. There are many examples where the agreement is unfair and this is partly attributable to the fact that neither Provincial nor National Forestry

officers have adequately checked the agreements and because many operations have been allowed to commence despite the fact that logging and marketing agreements were not approved by the Secretary DOF.

The unfairness is sometimes due to the fact that the lawyer/consultant advising the landowner company is also acting for, and owes his first allegiance to, the foreign contractor.

ii) Whether the Contractor is disclosing the true price for the logs. All but one company studied by the Commission has obviously been transfer pricing itself or the company through which it does its marketing has been transfer pricing or using other means to pay an unfairly low FOB price in PNG. (See sections 6 and 8 of this report and IR No 6) If the Landowners' share is calculated upon an unfairly low FOB price then the landowner company's share of the benefit will also be unfairly low even if the agreement provides for a fair division.

iii) Whether the Contractor is cheating in other ways. The companies who cheated by way of taking improper deductions, under measuring, undergrading, misdescription of species, forgery and fraud are listed in Section 8 of this report.

C. Premium Arrangement

In the case of the Wawoi Guavi Timber Area an attempt to benefit the landowners by payment of a premium of 48t per cubic metre, instead of equity ownership and substantial infrastructure conditions, backfired. They ended up being very poorly treated because the premium was wrongly calculated (IR No 5 App.1)

Even when landowner companies do receive and retain a share of the FOB price it does not always follow that the proceeds are passed on for the benefit of the landowners themselves. It is most common for the landowner company to spend a large proportion of their proceeds on administrative and management expenses such as management salaries, Directors fees and expenses, trips, purchase of desirable items such as 4 wheel drive trucks, PMVs, outboard motors and on rent of office space and luxury goods.

Landowner companies which spent virtually all their receipts from log sales in these ways include Ahia Development (Gulf), Brothers Logging, Noatsi, New Ireland Industries, Danfu Logging and Agriculture Development and Mamirum Timbers (IR No 4 and Appendices)

In summary it can be fairly said that very little cash benefit has been gained by Papua New Guinea landowners or companies from equity involvement in the concession holding companies. The only companies which have paid dividends seem to be Tasukolak and possibly Djaul Development has paid cash benefits to members.

Cash benefits have been received by way of Timber rights purchase, royalties and sharing of FOB price arrangements but the benefits have been unfairly low.

(D) Promotion of Business and Economic Development

Many attempts have been made to use the capital and energy of a timber company to promote business development and to ensure that Papua New Guineans (particularly the landowners) are given first chance to take advantage of the existence of a major timber project in the province.

It is also quite common for a condition of the permit to oblige the company to establish or assist in the establishment of an agricultural, cattle, agro-forestry or reafforestation scheme intended to be of benefit to the local landowners.

In every case studied, the results of such schemes have been, failure or disappointment. Quite elaborate provisions to promote business, and economic and social development were written into the Vanimo project agreement and a National Project team was set up to co ordinate it. In my opinion it has failed to achieve this purpose. Similar clauses were written into the Wawoi Guavi Block 1 agreement but not fulfilled (For discussion of these operations see IR No 5 App 1 and 2).

No other project seems to be providing significant benefits from this type of approach. Mostly the wider social and economic development projects never got started. Sometimes this was because land was not made available by the National Government for the particular project (Vanimo Forests Products and Jant reafforestation projects). Sometimes it failed because no firm binding condition was imposed on the company but merely an obligation to conduct feasibility studies (Wawoi Guavi IR No App 1, Bismark Industries IR No.6 App.7).

Sometimes it has failed because the company was half hearted about it or because the company simply failed to perform the condition and it was allowed to continue operating by the government with no remedial action being taken.

(E). Local Processing Benefits:

One way of attempting to provide benefits to the local people has been to encourage the establishment of local processing such as a Sawmill, Chipmill, Veneer Mill or Charcoal Pyrolysis Plant.

The records show many instances where, in breach of conditions, such operations have never commenced (eg Wawoi Guavi, New Ireland Otsuka, Goodwood, Open Bay) or commenced very late. The only significant local processing now occurring in association with a log export operation, is at Stettin Bay, Open Bay, Vanimo and until recently, Kumusi,. These operations produce job opportunities for some PNG citizens but very little by way of spin off industrial and business development. Such opportunities as arise to service the companies are usually taken up by foreign firms. The most successful has been the local vehicle hire contracts let by VFP but even that carefully planned project has failed to stimulate significant business development for PNG citizens in Vanimo. The Jant chipmill project was intended to stimulate agro-forestry projects but has failed to do this.

Some small scale sawmilling operations such as MacDui, Balmuru and Madang Timbers have provided employment and some spin off benefits.

Some Permit holders have been required to set up Agricultural and Community trust funds. Where this has been done (such as by Gaisho and DLAD in New Ireland) few obvious lasting benefits seem to have resulted. (See IR No 4).

(F) Employment Opportunities

Every logging operation naturally provides some employment opportunities for citizens. Whether significant opportunities for the skilled and managerial positions are offered will depend upon the outlook of the foreign company, whether it is operating on a long term basis and whether the Department of Labour and Employment is enforcing the labour laws effectively.

For the short term "hit and run" operators like MOI, Bruce Tsang's Companies, United Timbers, Luabar Logging and Santa Investments there is little incentive to conduct in-service training and seek to localise the operation. My observations of the longer term operators indicates that they also prefer to employ expatriate Asians or Europeans in the skilled and managerial jobs, even when skilled Papua New Guineans are available. For instance Wawoi Guavi's contractors brought a full team of Asians with them into PNG and I received in camera complaints from middle level PNG employees of Japanese companies that they were not being offered training for, or experience in, higher level management jobs.

On all my forest inspections I was struck by the number of Asians employed in semi skilled jobs for which many PNG citizens are trained and experienced, such as bulldozer operators, jinker drivers and chain saw operators. It was a frequent cause of complaint at logging camps (for example at Tabar Island (IR No 4 Vol 2 App 2) and at Luabar Logging camp at Iva Inaka in Central Province where PNG operators were sitting idle watching less competent Asians doing the jobs. It is quite clear that the Labour laws are not being

properly enforced and that the co operation between Forestry Officers and Labour Department officers is poor. It is only since the Commission started drawing attention to these facts that DOF has begun to be consulted on approval of Training and Localisation Plans for timber operations.

The usual explanation given by the foreign timber companies for this practice is that Asians are more productive and less trouble. They are content to spend long periods in difficult conditions without their families, receiving little more than pocket money. The balance of their pay is frequently paid in their home countries on a tax free basis. (See Wawoi Guavi IR No 5 App 1)

One most unfortunate result of allowing this situation to continue is that better trained graduates from our training institutions are unable to find employment because the Asians are preferred and skilled forest workers and equipment operators are being denied employment.

SUMMARY

Policy Principle No 4 is to promote active participation by PNG citizens in forestry and associated enterprises and to ensure they receive a fair share of the benefits. My inquiries quite definitely show that such participation is not happening on any significant scale. The inquiries also indicate that landowners and landowner companies are not receiving a fair share of the benefits from forestry. Success stories are of modest success only and they are rare, isolated instances. Thus Djaul Development (now) shows moderate success as does Tasukolak, but it is hard to find other successful business enterprises.

There are of course benefits from royalty payments and the purchase of timber rights but I believe the payments are far too low. (Benefits from infrastructure conditions are discussed at page 153-4).

POLICY POSTULATE

5. THE GOVERNMENT TO ACTIVELY FIND TECHNIQUES FOR PROMOTING "PAPUA NEW GUINEA WAYS" AND PAPUA NEW GUINEA FORMS OF TRADITIONAL ORGANISATION AND SOCIETY AS AN INTEGRAL PART OF FORESTRY EXPLOITATION

I saw no sign at all that the National Government has implemented measures to carry out this stated policy principle in the field of forestry. The nearest that the government has approached to the vast subject of traditional forms of social organisation is that, in TRP procedures, some trouble is taken to ascertain the landowning groups to whom the TRP money, and later the royalties, should be paid. No sign of developing new forms of legal entities has emerged. The use of existing legislation regarding registration of customary land groups has not been encouraged and, in fact, this whole vital area of developing appropriate legislation to handle PNG's land ownership and use problems has been shamefully neglected by successive governments since the 1970s.

I believe however that a consultant retained by the National Government to examine the question of registering customary land in priority areas recently presented his

report. It included drafting instructions for "Framework Legislation" for a National Customary Land Registration Act. Instructions for a Model Provincial Government Law, which would neatly tie in with the National Act, were also included. This initiative appears to have been allowed to lapse.

The only instance of creative legal and social thinking in the realm of land and forestry which was brought to my attention was in a lengthy submission from the East Sepik Provincial Government. In that province plans were well advanced to develop an area of about 90 000 ha. in the Wewak Angoram area for integrated land usage based on customary land owning groups registered under the East Sepik Customary Land Registration Act.

The Provincial Government had engaged consultants and enacted appropriate land utilisation legislation. Funding had been promised by an Aid agreement between the PNG and Australian governments whereby the latter promised K550,000 to fund a feasibility study. The land to be studied was identified and the landowners were interested in co operating in a scheme of planned land development involving sustained yield forestry on appropriate portions and agriculture or forest plantations on other portions of the land. The Consultants have almost completed the study and are understood to be recommending a mix of rubber plantation and forest plantations with only limited involvement in agricultural cash crops owing to the nature of the soil. It is reported however that the scheme is under threat from a group of "landowners" who are involved with a foreign contractor wishing to exploit the resource by the usual overcutting logging techniques. The landowners formed a company, the Sepik River Development Corporation Pty Ltd and applied for an LFA to be declared over portion of the land being studied by the Australian funded research team. From

DOF files and on evidence before the Commission the company is strongly backed by the Foreign Minister Mr M T Somare, who is its major shareholder. The Acting Minister for Forests Mr John Giheno declared the LFA after the documentation had been prepared in great haste on Ministerial direction. Far from promoting "Papua New Guinea ways" and PNG forms of traditional organisation the National Government appears to be undermining the only experiment along these lines which is occurring. (Further details of this situation are provided in IR No.7)

SUMMARY

The government is not apparently seeking techniques for promoting PNG ways and forms of social organisation. One exception to this negative statement could be the hiring of a consultant to draft interlocking national and provincial government customary land registration Bills - if this initiative comes to anything.

POLICY POSTULATE

6. STRICT CONTROLS ON FOREIGN INVESTMENT IN THE TIMBER INDUSTRY TO STOP IT ATTAINING A POSITION OF DOMINANCE TO THE EXTENT THAT IT WOULD COMPROMISE PNG'S NATIONAL INTEGRITY

This policy principle is derived directly from National goal and Directive Principle No. 3 of the Constitution.

STRICT CONTROLS

Various strategies have been adopted to try and impose the controls necessary to put this principle into practice. None have been effective. The strategies include:

- (a) Pre-registration with DOF;
- (b) The 1979 Guidelines;
- (c) NIDA;
- (d) Central Bank Guidelines;
- (e) Control over acquisition of goods and services;
- (f) Control over Transfer Pricing;
- (g) Monitoring and Control of operations;
- (h) Leadership Code;
- (i) The Criminal Law.

(a) Pre registration with DOF: All foreign companies wishing to engage in the PNG timber industry are required to pre register with the Department of Forests. As part of that process the applicant company must provide details and evidence of its financial resources and experience in the timber industry. The aim of pre registration is to ensure that unsuitable foreign companies are not allowed to negotiate with landowners and to put pressure on the Minister for Forests in the hope of gaining approved access to timber by avoiding proper scrutiny.

A pre-registration committee was set up to recommend on these matters to the Secretary who had power of final decision on pre registration. It used to be the practice to check in the applicant company's home country through the relevant Embassy and to check with the United Nations Commission for Transnational Corporations. In recent years these checks were discontinued.

From my inquiries it is obvious that some very inappropriate companies have managed to ignore pre-registration altogether. An example of this is Malaysia Overseas Investment (PNG) Pty Ltd (MOI) (see IR No 4 App 1). Other very unsuitable companies posed, falsely, as national companies and avoided the requirement that way. These include Angus (PNG) (IR No.2) and Wawoi Guavi Timber Co Pty Ltd in its first operation (IR No 5 App 1). Gasmata Resources Pty Ltd was at first rejected for pre registration but, after its principal Chin Ah Eng made gifts to Secretary Mamalai and his wife, Mr Mamalai simply directed pre-registration without reference back to the Pre-registration Committee.

(See IR No.7)

Gasmata, Wawoi Guavi and Angus were all inexperienced and under capitalised. MOI was desperately undercapitalised. These factors should have meant denial of pre-registration. In each case the operation got into extreme financial difficulties and it resulted in the resource being harvested for little or no benefit to the landowners except royalties (and even royalty payment has often been delayed). Gasmata's company Madang Timbers has recently gone into receivership with royalties of approximately K200,000 unpaid. (Santa Investments was forced to pay substantial royalty arrears from its operation in Gulf Province as a condition of being considered as contractor for the Gadaisu TRP area).

b) The 1979 Guidelines:

One of the purposes of this policy was to issue guidelines for foreign companies involved in the export of round logs. A basis of the policy was to direct foreign investment capital into the capital intensive sector of the timber industry and areas requiring high levels of technical

skill. Foreign investment was to be directed to firms involved in large scale local processing or to logging firms carrying out major road and bridge making tasks or performing some other major obligations requiring a high degree of skill (such as a large agriculture project).

It is quite clear that this policy has not been enforced except for SBLC, and, Jant and the few small to medium sized sawmills referred to at pages 174-176 below as the major involvement of foreign timber companies and their overseas capital is in simple log exporting ventures. (See App.1 and pages 176 - 205 of this report. See also IR.No.6 Vol.1 for further discussion of the 1979 Policy).

(c) National Investment and Development Authority
(NIDA)

NIDA was established to screen potential investors to ensure that they functioned only in appropriate sectors of the economy. All foreign timber companies were therefore obliged to acquire NIDA approval and should have been subjected to strict NIDA tests before commencing operating. Thus all foreign companies merely involved in log exports should have been refused NIDA approval because of the 1979 Forestry Policy.

NIDA checks have been applied very weakly and, in most cases, NIDA approval followed automatically upon DOF certification.

Many foreign firms simply avoided the NIDA requirements altogether and were allowed to operate regardless. Examples are:

- i) Bruce Tsang's companies Sakai Management and Nationwide Consultants (IR No 4 Vol 4A)
- ii) Angus PNG Pty Ltd (IR No 2)

- iii) Wawoi Guavi Timber Co. (IR NO 5 App 1)
all of which companies avoided NIDA by falsely posing as National companies and
- iv) MOI which simply operated without NIDA registration relating to timber though it applied (IR No 4 Vol 2 App 1)

To gain NIDA approval requires giving full details of the enterprise and its financing. None of these companies could have passed this test. (See IR. No.6 Vol.1 for full discussion)

(d) Central Bank Guidelines

The Central Bank requires a debt equity ratio of 3:1 on all foreign investment as a means of stopping undercapitalised foreign enterprises commencing and to prevent excessive domestic borrowings by such enterprises.

This method of controlling foreign investment however has not been firmly applied and almost all foreign timber companies operate at well above that ratio. Even Stettin Bay Lumber Co needed to make a new share issue in 1988 to correct the balance. Companies clearly operating well below this debt equity ratio include MOI, Sakai, Angus, Kumusi, WGTC, Gasmata and (Wewak/Madang Timbers). As many of these companies tend to lease all their logging equipment at high rates it means their financial position is chronically poor and their operations suffer as a result. (see IR No.6 Vol.1) assessing.

In assuring debt equity ratios a misleading impression is also given if operating. Equipment is treated as a revenue item (because it is leased) rather than a capital item requiring borrowing.

(e) Control Over Acquisition of Goods and Services:

Foreign Timber Companies are permitted to acquire goods and services from related corporations overseas. The Central Bank authorises remittance out of PNG or allows retention of funds off shore to pay for these goods and services. There is no check made to see if the goods and services were actually supplied, and if so, whether the price paid equalled or exceeded their value. This provides an excellent opportunity for transfer pricing and many examples were studied by the Commission:

- i) Shin Asahigawa's management fees (IR No 6 App 6)
- ii) WGTC barging fees (IR No 5 App 1)
- iii) Kumusi - Fletcher's Management fees (IR No 5 App 3)
- iv) Stettin Bay Lumber Co - Management charges (IR No 6 Vol 5 App 5)

In general terms there also seems to be a lack of knowledge of marketing fees properly payable to overseas sales agents which vary from 6% of FOB price to 20c per m3.

(f) Control Over Transfer Pricing

The various devices which have been used to transfer price by under-stating the true value of log exports have been referred to throughout the interim reports and Section 8 of this report. Until the FIC became involved in log marketing in mid 1986 this practice was allowed to go on unchecked and it has meant that PNG has lost a very substantial portion of the benefits it was entitled to receive from foreign investment in the timber industry. This aspect is discussed in great detail in IR No.6

(g) Monitoring and Control of Operations

Control of the logging operations by DOF is intended to be a major weapon for controlling the way foreign investment is used in the timber industry. Monitoring is intended to ensure that the companies perform their obligations, protect the forest and the environment and treat the landowners fairly.

The shameful weaknesses in our system of monitoring operations has been fully discussed above at pp 77-83 and in IR No.6. These weaknesses have allowed logging companies, most of which are foreign owned or dominated, to exploit the resource at cheap cost regardless of damage to the residual resource.

The way the foreign timber companies have created and/or "taken possession" of landowner companies and then used them to apply extreme pressure on Provincial and National politicians, Ministers and public servants is further described at pages 84 and 85 of this volume and in the various interim reports (particularly (IR No 4 Vol 1 pp.9-18 which deals with New Ireland). The pressure has been mounted by paying benefits and bribes, orchestrating local constituency pressure groups, commencing operations illegally and loading log ships illegally. The result has been that, in many instances, the foreign inspired landowner agitation and support forces DOF to allocate an area outside the approved programme, influences the selection process and succeeds in obtaining more favourable operating conditions. The foreign timber companies also make contributions directly to politicians and Ministers in order to gain approval for, or to by pass approval of, unfair agreements

with the landowners. Having gathered widespread support by these methods, the foreign timber companies free themselves from government controls and can commence operations illegally and, when convenient, discontinue them arbitrarily.

(h) Leadership Code:

"Quality of Leadership

1. The success of a nation, we believe, depends ultimately on its people and its leaders. No amount of careful planning in governmental institutions or scientific disciplines will achieve liberation and fulfilment of the citizens of our country unless the leaders - those who hold official positions of power authority or influence - have bold vision work hard and are resolutely dedicated to the service of their people".

C.P.C Report Ch 3 P.1

There was no doubt in the minds of the authors of the CPC Report and of the Constitution of Papua New Guinea that the proper administration of the government and the interests of all people would be openly challenged by foreign business interests. The Committee members foresaw that this would come in many forms, but most notably by attempts to manipulate, corrupt and compromise the nation's leaders.

The CPC Reports states:

"48. We are only too well aware of the experience elsewhere, especially on developing countries, where foreign corporations have dictated the nature and pace of development within the country through indirect control of the economy. There is no more effective way for foreigners to control our resources than to silence our leaders by enticing them into partnerships or the acceptance of shareholdings in their businesses. Our leaders must, we believe, resist this temptation if they are going to be true spokesmen and representatives of the ordinary people".

In the light of the current state of the forest industry statements like this assume an almost prophetic quality. The same may be said of the following recommendation:

"53. For similar reasons to those which underline our recommendation that leaders should not hold shares in foreign controlled companies or be partners in foreign controlled firms we recommend that leaders should not accept any loan other than a normal bank loan, hold any office or accept any benefit or advantage from a company or firm which is effectively controlled by foreign citizens. We do not believe that our leaders should be obligated to foreign citizens or enterprises in this way, as such an obligation is likely to undermine their independence as leaders".

And similarly:-

"55. We view with concern the growing practice, particularly among overseas businessmen, of giving or attempting to give favours, "gestures of appreciation" and other forms of gifts to our leaders in decision making positions, in order to obtain from these leaders favourable consideration in their business dealings with the Government"

I have quoted extensively from the recommendations of the C.P.C Report because it must be stressed that nobody can claim that the kinds of practices currently corrupting the forest industry were not foreseen and forewarned from the very outset.

When I read these passages I can readily re construct the conversations and events surrounding Mr Chin Ah Eng's proposed business venture with the wife of Secretary Mamalai and his gifts to Mr and Mrs Mamalai in Singapore. His proposals for an extensive business venture with Minister Diro in the Kemp Welsh area of Central Province seem all the more ominous in the light of these warnings. The same can be said of Minister Diros' involvement with the Angus Group

and his covert 35% shareholding in Angus PNG and of Minister Torato's dealings with Santa Investments and Bruce Tsang. The requests by Diro, Seeto, Sigulogo, Torato, Ope Oeaka, Roy Evara, Samson Gila and Stephen Raka for contributions from Santa Investments, Bruce Tsang and Moi for election activities and other purposes were the very kinds of actions that the authors of the CPC Report envisaged would lead to the control of the nation's resources being taken away from the proper authorities. There is no question that they were right. (These matters are all described in IR No.7)

It cannot be said that these most alarming developments were not foreseen and it equally cannot be said that nothing was able to curb or deter them.

The Leadership Code in Division 111.2 of the Constitution is a direct response to the recommendations of the CPC Report and the clear need to ensure that leaders act responsibly and in the nation's interest.

The Leadership Code applies to the persons listed in section 26 which include all Members of Parliament, provincial premiers, constitutional office - holders, Departmental Heads, ministerial staff and other specified persons.

The responsibilities of office are onerous and are generally reflected in the wording of Section 27 (1) which reads:

- "27 (1) A person to whom this Division applies has a duty to conduct himself in such a way, both in his public or official life and his private life, and in his associations with other persons, as not-
- (a) to place himself in a position in which he has or could have a conflict of interests or might be compromised when discharging his public or official duties; or
 - (b) to demean his office or position, or

(c) to allow his public or official integrity, or his personal integrity, to be called into question; or
(d) to endanger or diminish respect for and confidence in the integrity of government in Papua New Guinea".

The Organic Law on the Duties and Responsibilities of Leadership gives more than adequate effect to the Constitutional provisions of Division 111.2. The Organic Law further prescribes the Responsibilities of Leadership and makes provision for investigations and enforcement by the Ombudsman Commission. Leaders are obliged to submit comprehensive annual Statements divulging shareholdings, directorships and a range of other financial and commercial information.

Most particularly the acceptance of bribes or loans is prescribed as misconduct in office.

Under Section 28 of the Constitution a leader found guilty of misconduct in office can be dismissed from office or may be dealt with in any other manner recommended by the Independent Tribunal.

It is my opinion that the provisions of the Constitution and the Organic Law are an adequate response to the clear need to regulate and investigate the actions of leaders. Some changes may be appropriate and I shall mention these later.

What is of greatest concern is the very clear indication that these provisions are not being enforced to the extent that is clearly warranted. It is patently obvious from the findings of this Commission of Inquiry that these provisions are not being used effectively to control or deter the improper influences being brought to bear on our National Ministers and Members of Parliament, Provincial Premiers, Ministers and Public Servants. I note

the statement by Mr Sebulon Watt to this Inquiry when he informed me that the intention of Mr Seeto, Mr Gila and himself to extort bribes and gifts from companies associated with the forestry industry was motivated by the known ease by which such payments could be induced or extorted in this industry compared with any other industry. Notwithstanding this clear common knowledge, there has been no effective investigation or regulation of leaders associated with forest exploitation.

It is most alarming that the Ombudsman Commission is faced by such huge backlogs and that many leaders against whom there is clear proof of most serious misconduct have not yet been dealt with. In the meantime they continue to operate in the public arena. In the context of my findings Mr Diro and Mr Sigulogo fall into this category. Others such as Messrs Seeto, Torato, Raka, Oeaka, Evara and Gila escape for reasons outlined below.

Apart from the apparant operational constraints on the Ombudsman Commission there are also some fundamental problems associated with the enforcement of the Leadership Code.

The Code applies to a group of people that is clearly too narrow. It is also possible to avoid its provisions when one ceases to become a leader either by resignation or by other prior removal from office. As a result people like Robert Seeto and Roy Evara and others listed above can no longer be brought to account for their actions while they were leaders as they have ceased to be covered by the Code.

In these circumstances I offer my personal support to some of the recommendations made by the General Constitutional Commission in 1983.

The Commission recommended that the Leadership Code should apply to an extended list of people including all provincial assembly members. It also stressed the need to be able to investigate and proceed against a Leader who had vacated his office for one reason or another. Another worthy recommendation concerned preventing any leader found guilty of misconduct in the office from holding any other public office for at least 5 years.

Above all, the Commission recommended that the Ombudsman Commission be given sufficient resources to ensure that all investigations and prosecutions be completed within a six month period from the date that the case was referred to it.

I support these proposals which are urgently needed.

Criminal Law

My findings in relation to the offering and receipt of improper benefits in the form of bribes or by activities such as transfer pricing make it clear that the criminal law has neither prevented nor deterred wrong doers.

There can be no doubt that the timber industry, by its very nature, is conducive to acts of a criminal nature and to acts contrary to law and proper government administration. The fact that the system of permit and licence allocation requires the exercise of individual discretion makes it prove to attempts to pervert the proper administration of the industry. Moreover, the sums of money involved and the potential for large profits, particularly where illegal transfer pricing activities are practised, promotes actions from individuals in both industry and government to offer improper payments and to openly seek them. The lack of effective monitoring and control

Throughout the industry encourages less scrupulous operators to embark on improper and criminal ventures in order to maximise returns. This is done with little fear that they will be held to account for their actions.

The CPC Report predicted that unscrupulous foreign operators would continue to gain access to the nation's resources and it was right. The Report also anticipated that the nation's leaders would be compromised and become willing participants in the improper exploitation of Papua New Guinea resources and there can be no doubt that it has happened. Minister Stack has admitted that he has great difficulty in effectively monitoring operators due to staff shortages, inadequate training and an inability to discipline forest officers. No serious attempt has been made to remedy this.

In these circumstances the Criminal Law must have a crucial role to play in regulating improper conduct and in deterring such practices. In practice it does not.

There can be no doubt that many of the nation's leaders and the vast majority of the population will assess the effectiveness of this Commission of Inquiry by the number of prosecution that are successfully under taken and by the punishments given to the wrongdoers. It is unfortunate that this is the case as the criminal law does not appear to be appropriate or effective as it now stands.

Recent media reports indicate that Robert Seeto, Francis Sia and Michael Sia are not likely to be prosecuted.

I do not intend to deal with this matter in depth. I recommend that the whole area of criminal liability for official corruption be carefully considered. The Law Reform Commission may be the appropriate body to do this.

The following matters appear to be of major importance:

1. It must be a criminal offence for any politician or public servant to seek or receive payments or benefits in return for any action taken that is related to any performance of an official or public function regardless of whether that person has the ultimate or the sole decision making power over it.
2. Equally it must be an offence to offer or pay any such payment or benefit.
3. The law must recognise that people can be compromised by payments made to their spouses or children.
4. Any attempt to compromise a Private citizen (ie somebody who is not a politician or public servant) and to induce him to act contrary to his legal responsibilities should also fall within the scope of the criminal law. In this way corruption should not be restricted to a limited view of "official" corruption.

FOREIGN DOMINANCE

Because of the failure of these various strategies for controlling foreign investment it is apparent that it has obtained a position of dominance in the timber industry. This can be seen by the way some of the foreign timber companies are able to gain access to timber areas despite law and PNG policy. Some have

sought to gain timber concessions on the strength of their own merits but for many others the words used in IR No 4 at p.85 are quite applicable, especially to the hit and run specialists like Bruce Tsang, Santa Investments, MOI and United Timbers:

"It would be fair to say, of some, that they are now roaming the countryside with the self-assurance of robber-barons; bribing politicians and leaders, creating social disharmony and ignoring laws and policy in order to gain access to, rip out, and export the last remnants of the province's valuable timber.

These companies are fooling the landowners and making use of corrupt, gullible or unthinking politicians, lawyers and leaders. It down-grades Papua New Guinea's sovereign status that such rapacious foreign exploitation has been allowed to continue, with such devastating results to the physical and social environment, and with so few positive benefits to weigh against the irreplaceable loss which has been occurring. It is doubly outrageous that these foreign companies, having got the logs so cheaply for themselves, but at such high cost to the people and to the environment, have then transferred offshore, secret and illegal extra funds, at a rate of about USD 10 per cubic metre at the expense of the landowners and the PNG government".

COMPROMISING PNG'S NATIONAL INTEGRITY

The capacity of National and Provincial Politicians and Forest officers to control foreign investment and to monitor the forestry industry has been quite inadequate. It seems, often, that the foreign companies are controlling the landowners and the politicians. In many ways the foreign investment which most compromises our national integrity is the foreign investment which has been put into gaining control or influence over our leaders. For instance:

- i) Santa Investments has invested heavily in Premier Seeto, Provincial Minister Gila and National Minister Torato. (IR No 4 and p IMP B of this Volume)
- ii) Bruce Tsang invested heavily in Seeto and invested in Torato's executive officer Lindsay Lailai (IR NO 4 Vol 4A P.69 and 91)
- iii) Gasmata Resources invested in Secretary Mamalai and Minister Diro (See Section 8 and IR No.7)
- iv) MOI invested in National member (and former Minister Gerard Sigulogo) See IR No 4 Vol 2 App 1)
- v) Angus invested in Minister Diro (IR No 2)

At a lower level it is commonplace, in fact almost standard practice, for timber companies to invest in the leaders of landowner companies and communities to gain support for their applications and activities.

Working through landowner companies and local and provincial leaders the companies obtained favourable results in many instances. Some examples can be listed:

- (i) Such pressure on Minister Waka persuaded him to grant a "letter of intent" over the Danfu Extension

Permit in New Ireland actually referring to the pressure by saying.

"I am desirous of avoiding continuous pressures on this matter from Directors of Tasukolak, their consultant company, Gaisho and Sir Julius Chan by issuing this Permit quickly"

(IR No 4 Vol 3 App 6 p 18)

He later said in a Minute to Secretary Mamalai -

Secretary, should we have any problem in this project I know the politicians of the area including Sir Julius Chan are equally to be blamed".

(IR No.4 Vol.3 App.6 p.21).

ii) Bruce Tsang's pressure on Minister Diro (assisted by John Kasaipwalova and Miskus Maraleu) gained him approval in Kabil (for which K5000 was paid to Angus) and Noatsi (IR No 4 App 4)

iii) Sir Tore Lokoloko's "Angus-inspired" pressure on Minister Torato gained favours for Angus (IR No 2) and he altered his decision to withdraw its permit.

iv) Pressures from Turama landowners and provincial leaders on Ministers Hcrik and Palias Wingti almost gained an unplanned LFA for exploitation by Long Term Trading Co. and eventually gained it a Timber Permit in near record time. (See IR No.7)

v) In Manus Province, pressures mounted by Monarch Investments, working through Jaha Development, pushed Forests Minister Stack to declare a LFA and Minister Waim to approve an environmental plan. (IR No 5 App 4)

vi) In West Gadaisu "Santa-inspired" landowner pressure persuaded Acting Minister Genia (the MP for the area) to approve an agreement for Santa Investments. (see IR No.7)

vii) Under extreme pressure from rival landowner companies, orchestrated by rival foreign timber companies (Santa and Nationwide), Minister Stack approved two dealings in the one Local Forest Area at Napanta Nubui (contrary to legal advice and with disturbing consequences. - IR No 4 Schedule 5 p 5)

viii) Minister Stack is currently under extreme pressure from landowners of the Bonua Margarida permit area in Central Province and from the Arawe area of West New Britain.

Investment in Political Parties:

One of the major causes of worry is the degree of foreign investment being put into PNG political parties. The Commission did not set out to probe this matter, in the belief that political parties' source of funding was well outside its terms of reference. It was not possible however to turn a blind eye when, in the course of my investigations into the activities of timber companies, I crossed the trail of payments to, or requests for payments from political parties. It is quite obvious that foreign timber companies are prepared to pay large sums of money to political parties, or to individual politicians, in order to gain specific favours or merely to compromise and "hold" them in the hope of gaining benefits in the future.

The size and confident tone of the requests made by Messrs Diro, Sigulogo and Seeto for payments to be made by Santa Investments and MOI, and the size of the payments actually made by those companies to various politicians and political parties, is evidence that foreigners involved in the timber industry are using their funds to seriously compromise PNG's national integrity.

The CPC Report made very clear recommendations and sounded very clear warnings in this context. At page 17 of Chapter 6 the following recommendations are made:

"105. A contribution to the funds of, or the conferring of a benefit upon, a registered political party or political association by a non-citizen, or by any company, firm or other body which is effectively controlled by non-citizens shall be prohibited. ('Contribution' includes money to establish a political party or association)

106. In view of the need to ensure that national political parties have sufficient funds to continue to function effectively without relying on donations and other benefits given to them by foreigners (corporations and individuals), the government should immediately explore ways of fairly distributing finance among such parties from central fund made up of monies derived from -

- (a) a specific tax or taxes (or levy), for example on all companies which pay income tax; and
- (b) donations from foreigners"

These recommendations were adopted, to some extent, by section 129 of the Constitution. This section permits an Organic Law to require all political parties to register with the Electoral Commission their assets and income and the sources of them. It is provided in section 129 (1) (b) (c) that the Organic Law may prohibit "non-citizens from membership of, and from contributing to the funds of any such party or organisation".

No organic Law has ever been enacted in respect of these matters.

SUMMARY

The various controls listed in this section are too weak or too poorly enforced to implement Policy Principle No 6.

The controls are not "strictly enforced" and foreign investment has achieved a "position of dominance" which has enabled foreign "investors" to exploit the weaknesses in PNG's legislation, policy and administration and thereby gain dominance in the timber industry. In some instances this has been done by tricking Ministers and Departmental Heads, in other instances it has been done by compromising them by gifts and thereby gaining their support. In other instances it has been done by encouraging the PNG leader to become a willing partner in their enterprise with the promise of a share in the profit.

It is for these reasons that I say that foreign investment does compromise PNG's "national integrity". For a National Minister or political party to receive payments from a foreign timber company in exchange for "business favours" is only one step away from receiving such payments directly from a foreign government (or its agency) in return for "political favours". In this context it is not surprising that the payment by General Murdani to Forest Minister (and later Foreign Minister) Diro got confused with a timber related benefit during the Commission's public hearings. The two types of payment are closely related.

It is for these reasons that it is a matter of very serious concern to see that current Foreign Minister Somare is involved as a major shareholder with foreign investors in a timber company and why that matter should be investigated.

(The next page is 144)

(See 121-122 above and IR No.7). It is for these reasons also that it is of concern to see Mr Eng of Gasmata Resources compromising DOF Secretary Mamalai, arranging a business partnership for his wife and then entering into a business venture with Forestry Minister Diro aimed at helping the people of his electorate.

It is also of concern to be the recipient of further continuing evidence of the current malpractices involving foreign investment and of timber companies even as I write this final report. (These current allegations which require further investigation are listed in IR No.7)

POLICY POSTULATE

7 THE STATE TO BECOME A PARTICIPANT IN MAJOR TIMBER ENTERPRISES

There must have been two main reasons at least behind this policy:

(a) By becoming part owner the State will gain a position on the company's Board of Directors. This will give its representative access to all reports placed before the board and should permit an informed involvement in the company's decision making process. From this position the State's representative should have an effective say about logging and marketing practices. It should be harder for a company to engage in transfer pricing or destructive logging practices while the State representative sits on the Board.

(b) As a shareholder the State would be able to receive its fair share of any dividends payable should the company declare a profit.

Following this policy the State took up equity in several major enterprises.

- 1) Stettin Bay Lumber Co. The State invested K150,000 in SBLC which bought it 25 per cent of the equity and gained it one director on the Board. The director is a public servant from the Department of Finance. In 1987 SBLC issued further shares to improve its debt equity position but the State did not take up the shares offered to it. These were taken up by the other owner, Nissho Iwai of Japan (the mother company) and the State's share dropped to 17 per cent.

Considering the size of its turnover SBLC has made minimal profits for the State so far. This is shown by SBLC's tax situation.

SBLC paid company tax in the years 1974, 1979-1982, 1984 and 1987 but the total company tax payment was very small. In the 18 years between 1969 - 1987 (inclusive) the total company tax paid amounted to only K1.338 million. This should be compared with my findings on SBLC's transfer pricing which, in the two years 1986 and 1987 alone, amounted to well over two million kina. Clearly the profits are not flowing to the State but to Nissho Iwai - the major shareholder.

SBLC did declare dividends between 1980 - 1984 (inclusive) totalling K3.4 million and the State's 25 percent share of these dividends amounted to K850 000. The amount was not paid as cash dividend however but as bonus share issues. This has raised the par value of the State's equity in SBLC to K1 million.

There is no sign that the State Director is an active participator at Board meetings or that he gains access to "secret" information. It would be very easy to keep information from such an outsider (especially as many reports are written in Japanese) and of course there is nothing to stop "sensitive" decisions being taken outside the board meetings.

In fact the Commission's detailed study of SBLC's marketing practices disclose that it consistently indulged in transfer pricing from its first shipments and that practice was still continuing right up until 1988. (It probably still is).

ii) Kumusi Timber Co

The State, together with the Oro Provincial Government, took up 75 percent of the equity in Kumusi and each obtained one director on the Board. Within three years Kumusi was in receivership owing over K3 million in debts. Between them the State and Provincial governments ploughed into the ailing company a further K900,000 (by way of foregoing export duty and royalty payments) which was never recovered. KTC has now ceased operations and there is no chance the governments will recover their original equity or the later advances. KTC never declared a profit. (IR No 5 App 3 p 4-6)

There is no sign that the government presence on the Board influenced KTC's decisions before it was taken over by the receivers. If there was any degree of government control the sudden and disastrous collapse of the company seems to indicate it cannot have been very successful.

iii) Open Bay Timber Co Pty Ltd

The government took up 20 percent equity in Open Bay.

It has made profits only in some recent years. It has accumulated massive losses however and there is no chance that it will declare a dividend for many years to come. (See IR No.6 App.6).

It is in a hopeless financial position, its performance of its operating obligations was disgraceful and it was a systematic transfer prices for the benefit of its Japanese parent company.

Clearly any degree of Government control or participation was a complete failure.

iv) Wewak Timbers (later Madang Timbers)

At one stage a controlling interest in this company was purchased by the Investment Corporation of PNG from its previous owner Mr E Fitzgerald. It proved to be an unprofitable investment and, after the Secretary of the Department of Forests, Oscar Mamalai, made the necessary introductions to Chin Ah Eng of Gasmata Resources, it was sold to Gasmata at a low price. It is said that, in order to finalise the sale of the agreed number of shares, the Investment Corporation was forced to purchase the balance of Fitzgerald's shares, at a very high price (but this has not been checked thoroughly). When Wewak/Madang Timbers went into receivership in early 1989 Mr Eng had already departed PNG leaving many debts. It is said that the Investment Corporation is now liable for debts outstanding at the time of the sale to Gasmata amounting to K 300,000 (See section 8 and IR No.78).

Madang Timbers currently owes about K200 000 in unpaid royalties.

Once again the Government's participation in a major timber enterprise proved to be absolutely unprofitable and gained it no degree of control over the operation whatsoever.

v) Ulabo Timber Co Pty Ltd

This is another FDC in which the Provincial Government took up substantial equity. The operation was not studied in detail by the Commission but DOF records indicate that it has not been successful, paying no dividends to its shareholders. The Provincial Government has confirmed this. One reason may be the exclusive marketing arrangement that its Manager Grooms appears to have with Sumitomo Forestry Company. (See IR 6 App.2).

vi) Woodlark Island Development Corporation and Bougainville Forest Enterprises are two more small companies in which Milne Bay Provincial Government and the North Solomons Provincial Government respectively took up equity. They have not been studied by the Commission regarding this aspect. It is understood WIDC has not made substantial dividend returns to its shareholders, is controlled by its logging contractor and sells through the transfer pricer Lusco Enterprises. BFE is managed by Grooms and through its Manager appears to have exclusive marketing arrangements with the trader Sumitomo Forestry. (See IR No.6 App.2).

vii Kei Besau Kampani (West Coast Manus (KBK)

The latest instance of government involvement in a timber enterprise concerns the Manus Provincial Government's part ownership of the "landowner" company KBK which was awarded the West Coast Manus Timber Permit. It is said that the aim of the Provincial Government's involvement is to ensure that proper

agreements and arrangements are set up and that the contractor, SEAL Pty Ltd, honours the terms of the Logging and Marketing agreement. After three years of conducting an export logging operation SEAL will be obliged to construct a veneer mill to be run as a joint venture with KBK. The aim is for the Provincial Government to then progressively hand over its share of the equity in KBK to local ownership.

So far the Provincial Government's heavy involvement has resulted in the achievement of a strong set of conditions being agreed to by SEAL which include a substantial performance guarantee and realistic environmental, marketing and logging conditions. Whether the venture proves profitable in the long run to the Provincial Government (and the landowners) will depend on whether SEAL honours its commitment to construct and operate the veneer mill and whether that joint venture proves to be profitable.

To this stage the Provincial Government's involvement has definitely given it a controlling say in the affairs of KBK but it is too early to say whether it will be similarly influential in the conduct of SEAL's logging operation and later in the operation of the veneer mill. (See IR No 5 App 4 for a discussion of Manus timber affairs and see above at p 120-121 for a Case Study of the application of National Forestry Policy in relation to Manus - and see follow up in IR No.7).

SUMMARY

The State did seek equity in a few timber enterprises but it is hard to see many benefits from its having done so.

POLICY POSTULATE**8. TO ENSURE A FAIR RETURN TO LANDOWNERS AND THE NATIONAL AND PROVINCIAL GOVERNMENTS**

The question of ensuring a fair return from timber enterprises for landowners and neighbouring people has already been discussed in relation to Policy Postulate No 4. at pages 110 and following. The question of ensuring a fair return for National and provincial governments has been touched upon during the discussion on planning and orderly development of the resource as that is one of the major aims to be considered during the planning process.

I shall now list the major means whereby the National Government seeks to gain revenue and other benefits from timber enterprises:

National Benefits

Royalties: The National government was, until 31 December 1987 retaining 25 percent of the royalties paid by timber operators. As previously discussed this was probably excessive and contrary to the provisions of the Organic Law on Provincial Government (Page 100) . Since then the Government has paid 75 per cent to landowners and only 25 per cent to Provincial Governments. This too appears to be unconstitutional.

Under the Forestry (Private Dealings) Act there is no requirement to pay royalties to government but this is sometimes provided for as a condition of assenting to a Dealing.

In 1987 the total royalties paid amounted to K5,597,015 of which the National Government is said to have retained K1,399,253. (Landowners also received K1,399,253 and the) (Provincial Governments received K2,798,507.

Company Tax: Company tax is levied on the profits of all companies according to the normal principles of income tax law. The rate currently applicable is 30 percent plus 15 percent withholding tax. The tax is levied on the income which is disclosed in PNG and normal deductions are allowable including deductions for seven years from the date the loss was incurred.

One of the most startling results of this Inquiry is the extent of the transfer pricing fraud which has enabled many, many companies to disclose losses in PNG while at the same time building up transferred sums in overseas tax havens at the rate of about USD 8 to USD 10 per m3. (The details are set out in IR No 6 and elsewhere throughout the Commission's reports). The practice has resulted in massive tax evasion and has very seriously eroded the benefit the National Government expected, and was entitled to receive by way of company tax and dividend withholding tax. The size of the loss can be gauged by the fact that 13 companies and 4 individuals have paid or agreed to pay over K3 million in avoided tax. Further assessments of over K6 million have issued concerning 6 companies and 4 individuals and another eight companies are under investigation. A list of the companies which I have found were transfer pricing in substantial amounts is set out in sections 6 and 8 (and see IR. No.6).

Group Tax: This tax is meant to be deducted by a company from the wages of its employees at the time the wage is paid and remitted monthly to the Taxation Office.

I have found numerous instances where timber companies have paid a substantial part of their expatriate employees' wages overseas and failed to disclose the payments or deduct group tax. Again the size of the problem can be gauged from the fact that, on the strength of evidence collected by the Commission group tax of K747,568 has been collected from, 1984 or agreed to by, four companies. More are under investigation concerning group tax avoidance.

Import duties: Like all other enterprises, timber companies are obliged to import a great deal of equipment, machinery and other items. In the process they pay import duty which is therefore a benefit received indirectly from forestry by the National Government.

Export Duty: The duty on the export of logs is 10% of FOB price. Through a bureaucratic error this duty, from May 1984 until June 1987, was being calculated on the minimum export price rather than on FOB price. The MEP has almost always been well below FOB price and this has resulted in considerable loss to the PNG government (and to Provincial Governments whose derivation grants are calculated as a percentage of export duty paid). The error in the system was pointed out by this Commission and immediately corrected. This error has cost hundreds of thousands of kina in lost revenue in some years.

A greater loss has been caused by transfer pricing and other methods of understating the disclosed FOB price. In New Ireland for instance I have calculated that the average amount of transferred price has been about USD 10 per m³ and that prices actually paid by the end buyers were about 20 percent higher than the disclosed FOB price. Had the duty been paid on the true price it would have led to a significant increase in PNGs revenue.

In regard to export duty the present requirement is that the amount should be paid before the ship departs. A fairer procedure might be to let the ship depart first but to insist that each company gives its bank an irrevocable direction to pay export duty out of the proceeds of the letter of credit as a first charge.

Foreign Revenue Earnings: One of the benefits which flow from any export operation is that it will contribute foreign earnings to the overseas balance of payments (assuming the company exports more produce than it imports as equipment and materials etc). The common practices of understating the value of exports and overstating the value of imports has drastically worsened PNG's balance of payments situation. (IR No.6 Vol.1)

Infrastructure constructed by timber enterprises: If the conditions of a permit or project agreement have been well thought out, and if they are fulfilled by the Company, then a timber enterprise may bring major benefits to the National Government (and to provincial government and people). Thus if a company constructs many kilometres of necessary roads and bridges as part of its infrastructure conditions it will be a major benefit to the government which otherwise would have responsibility to construct the roads. Companies which did this to an acceptable level include SBLC and Open Bay Timber Co which are both constructing roads which will form part of the Kimbe - Rabaul Road; Vanimo Forests Products has built a road which will eventually link Vanimo to Aitape and therefore to Wewak; Jant has upgraded the Gogol to Madang Road and Leytrac has constructed many kilometres of road as part of the New Ireland South West Coast Road; Ulabo Timber Company constructed a road which will form part of a proposed Alotau - Port Moresby Road. (Roads which were constructed by Angus (Santa) at Gadaisu and by Ulabo at

Sagarai should have been aligned so as to link into this major road. DOF planners however did not write this condition into their permits and the roads they have constructed have been aligned purely for accessibility to timber and are unsuitably aligned for use as a national highway).

On New Ireland Danfu Logging and Agriculture Development has constructed a road which links several villages to Namatanai.

The Nam Yang permit included major road construction conditions but these were not fulfilled.

As well as roading, conditions requiring construction of other "governmental" projects have been written into some permits. Thus VFP was obliged to construct a major urban development in Vanimo township (but has not done so) Vanimo and Nam Yang were also obliged to build substantial wharfs and have done so. New Ireland Otsuka's wharf building obligation was, however, dishonoured.

Provincial Government Benefits:

Royalties: In a similar way to the National government provincial governments also stand to gain by receiving royalties from timber enterprises. As previously stated, their entitlement under the Organic Law on Provincial Government is 100 per cent of royalties less costs and the lower payments they are currently receiving are in breach of those provisions. On 1987 K2,798,507 was paid to provincial governments as royalties.

Derivation Grant: Theoretically a provincial government's revenue may be boosted by a forestry project if the logs are exported out of the province. In those circumstances the Provincial government is entitled to receive 1.25% of the

total FOB value of the logs. This is deducted from the National Government's 10% export duty. The current practice however is for the amount of any royalties received in the province (by landowners and by provincial governments) to be deducted from the derivation grant otherwise payable under the "1.25%" formula. In the past, if royalties exceeded the amount of the derivation grant this has sometimes led to additional monies being deducted from other funds due to the province. That practice has now been stopped and if royalties are in excess of the derivation grant that merely results in the cancellation of the derivation grant.

Budget Allocation: The principles and procedures for allocating funds from the National Government to the provinces has been previously described at pages 99-102.

The amount of the general untied grant, or of the "tied" divisional allocation, is largely determined by reference to forestry expenditure prior to the establishment of provincial government. There are however limited ways whereby a province which has subsequently experienced a substantial increase in forestry activities may gain an increased allocation. This could be treated as an additional return to provincial governments.

Landowner Benefits:

This subject has been exhaustively dealt with at pages 110-120 above.

SUMMARY

There is no doubt that the National Government gains some benefits from forestry in the form of various forms of taxes and duties. It may also gain by way of increase in foreign exchange earning and by being the beneficiary of infrastructure such as roads and bridges. It is an

unfortunate fact, however, that on many of these items, the government is being cheated by companies which indulge in transfer pricing and which fail to perform the infrastructure conditions of their permit.

Provincial governments do not seem to gain a great deal from most timber enterprises as their royalties have been undercut and the derivation grant is cut back in proportion to royalties received. Their involvement in joint venture timber enterprises has been singularly unsuccessful.

As previously described the landowners appear to receive the smallest, most unfair share of all.

The lack of effective joint planning and consultation between national and provincial governments described earlier explains to a large degree why effective steps are not being taken to ensure that provincial governments, national government and landowners are all getting a fair return from timber enterprises. Through the various gaps and defects in the governments system for controlling the timber industry the lion's share of the profits are being shipped overseas. Only the left-overs are available for distribution in Papua New Guinea. (IR No.6 Vol.1)

At present not enough is being done to ensure a fair return for all these potential beneficiaries. The landowners are usually unfairly treated but sometimes the National and Provincial Governments also do very badly from the timber project.

POLICY POSTULATE

9 PROMOTE MEDIUM, AND SMALL SCALE FOREST PROCESSING AND ASSOCIATED INDUSTRIES OWNED BY NATIONALS

The Commission did not attempt a specific study of this policy.

The sort of things envisaged by this policy would include:

(a) Agro Forestry plots where village groups would be encouraged to plant up appropriate stands of timber and underplant with (say) hybrid cocoa. This is actually being attempted from the Madang Forest Office where an officer has the task of planting up trial village plots as demonstration models with the eventual aim that the timber will be harvested and processed through the Jant chipmill. There is very little response from the people and little progress so far.

(b) Charcoal Production: This type of project was originally written into the Wawai Guavi Timber Permit for Block No 1 - to establish a charcoal/pyrolysis plant but it was not proceeded with (IR No 5 App.1)

(c) Other uses of waste products: One would hope that off cuts from sawmills, dockings in the bush, reject logs could be put to some use by a small local enterprise. For instance reject logs could be fed into a small forest mill or wokabout sawmill. Local carvers or furniture makers could be using some of the prime species as the raw material for their business. These sorts of enterprises just do not seem to be operating and are not being actively encouraged by government. One of the complaints against Vanimo Forest Products was that it refused permission for the local

townspeople to collect trimmings from the waste pile at its sawmill which could be used for cladding on low cost houses in nearby villages and settlements. VFP insisted on burning this "waste" timber which had such potential value. (By contrast Fitzgerald's small sawmill in Madang made this type of timber available free of charge).

(d) Involvement in production

For a short period SBLC employed two local contractors using a forest sawmill and a wokabout sawmill to cut flitches in order to boost the production of its sawmill. Potentially this could be a useful sort of associated business enterprise. It is not being actively promoted by government nor written into the terms of permits and project agreements. Beechwood Pty Ltd, however, is utilising small village sawmills as "breakdown" mills to feed its sawmill near Mt Hagen (See P 174 below)

There are general obligations written into some agreements to promote local business enterprises. The example of Vanimo Forest Products is discussed in IR No 5 App 2. That company encouraged the formation of a plant hire firm, some PMV businesses, a chainsaw group, village grass cutting groups and a security firm to service the requirements of the company. That is probably the most sustained effort made along these lines and was supported by a National Government Project team.

The security firm and the chain saw group were sacked for non performance but there is some success with the vehicle hiring groups.

SUMMARY

The overall impression I gained was that very little attempt is being made to utilise the potential created by the existence of a timber operation so as to actively stimulate the development of small and medium size PNG enterprises.

POLICY POSTULATE

10 PROMOTION OF ONSHORE PROCESSING

(A) DEVELOP PERMANENT FOREST ESTATES SUPPORTING LARGE SCALE INTEGRATED ONSHORE PROCESSING FACILITIES

(B) ENCOURAGE SMALL AND MEDIUM SCALE ONSHORE PROCESSING AND REPROCESSING INDUSTRIES WITH HIGH DEGREE OF OWNERSHIP AND PARTICIPATION BY PNG CITIZENS

Onshore processing and reprocessing has been stated to be a major aim of PNG Forestry policy since well before the 1974 White Paper on National Forestry Policy. In early years processing was limited to foreign owned, small scale sawmilling for the domestic and export market and to the Bulolo pine plywood industry based on the Wau/Bulolo government planted pine plantations.

The 1974 Policy reflected the first "self governing" Government's "Eight Point Plan" philosophy of national ownership of, and participation in, small and medium scale processing, which would benefit village development and encourage self help schemes. The policy's main concentration however was on "large integrated operations

producing sawn timber, veneer and/or plywood and woodchips "as the best method of stimulating onshore processing" ("National Forestry, Policy 1974")

A LARGE SCALE INTEGRATED PROCESSING

This aspect was well thought out and formulated. It was realised that saw milling and plywood manufacturing are wasteful processes which require large volumes of logs but have, at the most, a 50 percent recovery rate. To gain the maximum benefit from the trees cut it is preferable to encourage a large integrated processing facility to be established in each forest area. It was envisaged that there could be several smaller sawmills and plywood or veneer factories operating nearby (preferably with a high degree of national ownership and participation) - possibly geared in with village run plantations and agro forestry plots. These would be centred around a large industrial complex involving a sawmill and or ply or veneer mill integrated with other processing facilities which would utilise the waste. Ideally the facility would produce, amongst its various products, a product like medium density fibre board, the production of which would use up virtually all the waste from the sawmill, veneer mill or plywood mill and which would supply a domestic as well as an export market. Another possibility would be to integrate a chipmill into the industrial complex to produce chips for export or possibly, eventually, to feed a local paper mill.

The policy required that these forest estates be "permanent". This was to be achieved by progressively establishing forest plantations which would supplement and eventually replace the natural forests as the source of supply for the mills. In the early days, of course, the supply would come from the natural forests until the plantations were mature enough to harvest.

Jant Pty Ltd: In fulfilment of this policy Jant was encouraged to establish a chipmill in the Gogol forest near Madang. It had an obligation to plant up forest plantations and to encourage the establishment of village plantations and agro forestry plots so that the local people could benefit from the existence of the company which would clear fell their forests. Jant was given no log export quota. All its sawmill quality logs were expected to be sold to the adjacent sawmill run by Madang Timbers (formerly Wewak Timbers) and the rest would be chipped to supply its parent company the giant Honshu Paper Company of Japan.

Nam Yang Timbers (PNG) Pty Ltd was established in West New Britain in 1981 with a similar obligation to establish plantations and a chipmill. While waiting for the plantations to mature Nam Yang was to log the natural forest and it was permitted to export logs for the first years pending completion and commission of its chipmill, due in 1983.

Stettin Bay Lumber Company was encouraged to build a large sawmill in West New Britain and to plant up extensive forest plantations to supply it. The long term plan was to extend into other forms of processing such as veneer, ply, fibre board and/or chipmill and feasibility studies for these projects were to be carried out. Meanwhile SBLC was granted a quota to export logs to help finance these processing facilities. (IR No 6 Vol 3 App 5)..

SBLC was also obliged to carry out extensive road and bridge building operations to provide a benefit for the wider community.

Open Bay Timber Company was encouraged to commence operations in East New Britain and was similarly obliged to build a sawmill and establish plantations. It was given roading obligations to link in with SBLC's road construction so as to form part of the proposed Rabaul - Kimbe highway linking the provincial capitals of the two provinces.

Vanimo Forest Products The attempt to establish a similar integrated processing complex in the Vanimo Forests Timber Area eventually resulted in Vanimo Forest Products being granted an (interim) five year permit to establish a sawmill and conduct feasibility studies for further processing facilities. The company undertook an obligation to promote local business development and associated industries as well as to establish trial forest plantations. The aim was to, eventually, replace the natural forest by plantations as the source of supply for the sawmill and associated processing facilities. To this end VFP was obliged to establish a small trial forest plantation with a view to extending the plantation when the long term permit was granted. To promote the wider social and economic development aspects of this onshore processing policy a Project Co ordinator was established as head of a National Project Unit.

VFP was also obliged to carry out a large scale urban development project to provide housing for approximately 200 of its employees in Vanimo township. Meanwhile the company was granted rights to export approximately 200,000 m3 of logs p.a. (IR No 5 App 2)

Wavoi Guavi Timber Company: A similar attempt to set up an integrated processing facility in Western Province was commenced when WGTC was permitted to start operating in the Upper Bamu region. The conditions originally imposed on

WGTC included the establishment of a charcoal-pyrolysis plant and various other agricultural, cattle and crocodile/fisheries projects. The conditions were hastily and badly thought out (for reasons fully discussed in IR No 5 App 1)

POLICY PERFORMANCE EVALUATION - ONSHORE PROCESSING

None of these projects has fully achieved the stated policy objectives of establishing a permanent forest estate supporting large scale integrated onshore processing facilities.

Since the widening of forestry policy in 1979 to promote log exports the focus of all these operations shifted to this aspect (See Appendix 2 and IR No 6 Vol. 1).

Nam Yang completed its chipmill about six months behind schedule but the chipmill never operated and the plantations were never established. Its permit was cancelled in 1985 after it had been operating for some four years entirely as a log export operation. It has since been granted a new permit (see below at page 169).

Vanimo Forest Products has carried out a log export operation. The trial plantations have not been established (mainly because the government has not made land available). Its feasibility studies for further processing indicate that a chipmill is feasible but it has made no headway in studies into further processing such as veneer, plywood and fibre board and the chipmill, promised by 1988, has not yet been constructed.

VFP did establish its required sawmill within the prescribed time period. It produces the required volumes. For this it is granted an additional log export quota and a 50% discount on export duty payable on log exports. It has very low recovery rate which does not indicate a commitment to efficient sawmilling. The fact that it has made no progress on studies like further processing, reprocessing, natural regeneration and reforestation indicates its lack of interest.

Wavoi Guavi Timber Co managed to avoid most of the conditions imposed on its operation in Block 1 and commenced operating in Block 2 as a straight out log exporting enterprise with an obligation to operate a sawmill. Completion of the sawmill is now more than two years overdue (IR No 5 App 1)

Madang Timbers always had a log export quota to operate alongside its sawmill operation. It was expected to process poor quality logs through Jant's chipmill. Increasingly it has tended to utilise its own reject logs to process in its old and inefficient sawmill instead of buying from Jant. (It also operates a small chipmill). Consequently Jant's market for its sawmill quality logs is drying up. Madang Timbers is now in very serious financial difficulties (See IR No.7) and a receiver has been appointed.

Jant With Madang Timbers drastically reducing its demand for Jant's sawmill logs (from 15000 m³ to 750 m³) these valuable logs are all being "thrown away" into the chipmill. Jant has continuously called for a permit to export logs and to export an increased number of flitches. Until recently this has always been refused. Meanwhile modern technology has enabled its parent company to convert to using recycled paper to replace 70 percent of its timber

input requirements. To make Jant's position even less secure it had been promised the South Naru resource and had completed its feasibility studies there before it discovered that the government had purchased the timber rights for an incredibly short period of only five years. Jant was not granted the permit as promised because the TRP had already expired.

Recently Jant has ceased replanting the plantations it has cut out because the various government leases granted to Jant will expire before the end of the next rotation period. Most recently Jant has been granted an export quota which enables it to export a portion of the annual harvest from the plantation. The export logs are thin poles and the effect is that these plantation plots will probably be clear felled. As the government is allowing Jant to run out of resources it appears likely that Jant will depart PNG in the near future, leaving the government owned plantation land, and the locally owned nearby natural forest, clear felled. Virtually none of the wider aims of the integrated processing policy have been fulfilled.

Stettin Bay Lumber Co This company has gone further than any other to fulfill the government's stated policy. It has established extensive plantations and the species are selected so as to be usable in plywood and veneer processing. It has established a sawmill which has always processed below the required rate. It has conducted feasibility studies into further types of processing. It nevertheless is predominantly and primarily a log exporting enterprise exporting over 200,000 m3 p.a.

The sawmill is inefficient and is processing mainly reject logs and the wastage is consequently very high. It achieves a recovery rate of only 30 percent and the huge pile of scrap off cuts used as corduroy on SBLC's roads are

included in the calculations as processed timber. It exports sawn timber to Australia and New Zealand but 70 per cent of its produce is sold domestically.

The degree of the Government's commitment to this type of operation must be questioned as it allowed SBLC to commence and operate for seven years with no legal permit or project agreement and without giving it secure title to the plantations it was establishing at a cost of K 75 million. During this period SBLC continuously fought to put its operation on a legal footing but could not budge the government. It is a sign of how profitable the log export market must be that SBLC was prepared to carry on investing at such a high rate when the government was unable or unwilling to give it any security whatsoever. (From its log export operation SBLC was, I have found, making a massive illegal profit by transfer pricing (See IR No 6 Vol 3 App 5).

SBLC has recently been granted rights over the very large Ania Fullerbourn Timber Area. It appears that the government has failed to push strongly for its integrated processing policy as SBLC has actually been allowed to reduce existing levels of sawn timber production in the short term and has not been obliged to commence the wider, more integrated, processing which would reduce its uneconomically high rate of wastage and which would provide local employment and increased foreign earned revenue in the process. SBLC now operates under a signed project agreement but still has not been issued a permit.

The Managing Director of SBLC produced to the Commission the results of feasibility studies already carried out by the Company through its parent Nissho Iwai's research facilities in Japan which show that timbers available to the company in the natural forests and planted

in its plantations are suitable for Veneer, single ply and zephyr board production. SBLC is, I believe, willing to commit itself to the very sort of integrated processing on a permanent forest estate required by government policy. The Government however has not required this wider processing of SBLC nor granted the long term security of title required to make the heavy investment practicable.

Open Bay Timber Company was in disgraceful breach of its conditions (See IR 6). It now claims to be on schedule with the light burden of reforestation required of it to date. This year however the burden increases and it will be required from now on to plant at a very high rate of 1100 ha per annum (compared with 750 ha required of SBLC). It still has six more years before it is obliged to construct its chipmill and, in the meantime, it is enjoying the benefits of a log export company. As Jant has apparently persuaded the DOF that its chipmill operation is not really profitable enough to pursue, despite its assured market to its powerful parent, one wonders whether the Open Bay Chipmill will ever be built or, if built, whether it will remain unused like the Nam Yang chipmill.

In retrospect it seems that the 1979 decision to allow large scale processing enterprises to export a limited volume of logs to stimulate cash flow and thus support the processing operation has come to dominate the entire operation. If a company is allowed to export a high volume of logs then it faces a problem of what to do with the high volume of rejects which were not up to export standard. If there is a sawmill available the obvious thing is to saw them. In the absence of a chipmill or fibre board plant the only other option is to burn them. Most of the logs being fed into the Vanimo, Stettin Bay and Open Bay mills are therefore rejects with twists, hollows and other defects. For this reason the wastage is high and the quality is low.

In addition, as the companies are looking to log exports for easy and greater profits the sawmills tend to be outdated and poorly run.

The result of these factors is that the companies are really log exporters who carry out onshore processing and (sometimes) reforestation rather reluctantly or avoid this obligation altogether. This trend has apparently been continued in recent allocations.

A further result is that the good quality logs are being processed in foreign countries supporting processing industries and providing employment. Only the logs which these foreign countries do not want and reject are being used to feed local processing facilities.

With this bad start and a lack of redundancy processing obligations to utilise wastage local processing is at a great competitive disadvantage. Another company that was in open and disgraceful breach of its infrastructure conditions while it concentrated on log exports was New Ireland Otsuha Development (See Ir4).

Recent Allocations:

Ania Fullerbourne TRP area: The project agreement signed with SBLC has a reduced sawmilling condition, massive log exports and no specific requirements to commence further types of processing.

Jant: Instead of being given secure title to enable it to replant the logged plantations and to plant up new areas Jant has instead been given a limited right to harvest and export logs from the plantations. This seems to indicate a recognition by the government that the Jant chipmill venture is doomed.

Manus As previously described the National Government seems to be no longer supporting the Provincial Government backed proposal by Kei Besau Kampani which aims at establishing a veneer mill in three years time.

Arawe The permit for the Arawe timber area in West New Britain has been allocated to a landowner company (despite strong opposition from a rival "landowner company" claiming to represent the true customary owners). It is said to include a condition requiring 25% of the volume of logs exported to be processed through a sawmill within five years. There is an intention to carry out downstream processing later on by way of moulding and possibly a veneer mill. It is said also that reforestation has not been decided upon and is awaiting finalisation of the logging and marketing agreement.

By adding a sawmill condition onto a predominantly log exporting operation it will again result in reject logs being used and a high wastage rate with no secondary processing planned which will use the waste.

Nam Yang Timbers has again been issued a timber permit at Kapuluk. This time it will be predominantly a log exporting operation but with a condition attached to process 30,000 m³ input through a sawmill by the end of year 2. There is to be no requirement to reforest but a reforestation levy of K1 per cubic metre is to be charged. It is intended that this will be paid into a reforestation trust account and used for that purpose. (In addition there will be a K1 per m³ land use levy).

There is no policy on whether reforestation should be carried out in the vicinity of the project or elsewhere in the country and no policy whether it should be done by government or private enterprise. The maximum permitted

level of export is 200 000 m3 p.a and at the rate of K1 per m3 a sum of K200 000 will be raised for reafforestation. SBLC claims it spends K3334 per hectare on reafforestation and, at that rate, the sum raised from Nam Yang would fund only about 30 hectares of reafforestation per annum. It still leaves the other problems, of where the plantation is to be planted, by whom and for whose benefit, to be solved. The present Minister has a partly thought out idea of involving unemployed youth in planting programmes but, at this stage, it hardly amounts to a reafforestation policy.

The future of the Nam Yang's still standing, virgin chipmill has not yet been decided but the indications are that it will never operate unless the market for chips improves.

Government Plantations

The sad story of the fading interest in local processing is also illustrated by the failure of the government established plantations at Bulolo, Brown River and Kerevat which, potentially, could have been the basic resource of integrated processing industries on permanent forest estates.

Bulolo Pine Plantations

The earliest example of onshore processing based in a permanent plantation estate was at Bulolo where the natural pine forest and the government plantations were used to provide the resource for a plywood factory which built up a sizeable export trade. Of recent years the operation has been run by PNG Forest Products Pty Ltd but has been running down. The operation is now based entirely on the plantations but they are not being properly maintained and the product is deteriorating. Exports fell off to nothing

and the operation now limps along selling its rather inferior quality plywood on the domestic market. The equipment is outmoded, poorly maintained and inefficient by modern processing standards.

Brown River Plantations These government teak plantations were declared to be customary land after court proceedings in 1982. Whatever potential for exploiting this long term and substantial government investment, and using it as the basis for an onshore processing industry, was lost at that stage. Since then the plantation (and its customary owners) have been the victim of one raiding party after another. It was first "raided" by Rod Patterson and his Luabar Logging company which operated on Timber Authorities for the landowner company Varagadi Resources Development Pty Ltd. The T.A. allowed export of up to 20 000 m³, the T.A. was revoked by the Secretary DOF as being contrary to policy which banned export of teak logs and as being illegal. It was reissued at the direction of Minister Torato. Under Minister Horik an attempt to stop loading of the teak at Bootless Bay was unsuccessful because Sir Julius Chan (as Minister for Trade and Industry) granted an export license contrary to DOF recommendation. Luabar therefore had somehow gained dispensation to export teak "thinnings" in log form by way of wrongly issued Timber Authority. Patterson's operation severely damaged the plantation because he took the best trees as thinnings instead of leaving them to mature.

After that operation was stopped the plantations were "raided" by Austpac Timbers (PNG) Pty Ltd which tried to export the teak illegally as "two sided flitches" until its shipment was stopped at Lae and the logs were off loaded as illegal forest produce.

Most recently the plantations are being harvested by PNG Enterprises whose manager is Patrick Tay (formerly of the FIC and of Wawoi Guavi Timber) who is also selling it off as flitches for processing overseas.

The lack of true commitment to a policy of promoting onshore processing can be shown quite dramatically by reference to the official table published in the DOF Annual Report 1987. (figure 1)

It is shown even more dramatically, in more detail and with absolute accuracy by the Commission's own calculations regarding log exports and all types of processed timber products exports (Figure 2)

Kerevat Plantation

The Kerevat government plantation was established in the 1950's and consists of 1800 ha. of teak, hamarere and balsa. Its original purpose was to supply Rabaul's sawn timber requirements. Further extension was not possible because land could not be acquired. After the introduction of provincial government the management and control of the plantation was handed to the East New Britain Provincial Government. There is confusion whether it is still owned by the National Government or not. (Similar confusion existed over ownership of the Bulolo Pine Plantation but was recently resolved by the National Government firmly asserting ownership).

Proper subcultural practices are not been followed and the plantation is now somewhat "run down". The balsa is regularly harvested for benefit of Teproy Timbers for export. Its marketing is unchecked and abuses have been

reported to the Commission. (This matter was not investigated because of constraints of time and staff.

B. ENCOURAGEMENT OF SMALL AND MEDIUM SCALE ON SHORE PROCESSING AND REPROCESSING INDUSTRIES WITH A HIGH DEGREE OF PNG OWNERSHIP AND PARTICIPATION BY PNG CITIZENS.

There are few small and medium scale processing and reprocessing industries and, far from being actively encouraged, it is not even easy to obtain statistics on these facilities from DOF.

Other than citizens being involved as employees in the timber processing industry, there is little sign of national ownership in the industry. The exceptions to this are as follows.

(a) Landowner Companies becoming involved in local processing

Examples include Djaul Development Corporation and Tasukolak Pty Ltd in New Ireland which have both very recently purchased logging equipment and small secondhand sawmills (IR No 4 Vol 2). Kei Besau Kampani Pty Ltd in Manus Island is proposing to be a joint venture partner in a veneer mill with SEAL Pty Ltd (IR No 5 App 4). There is also Lama Sawmills at Ialibu, Southern Highlands which has a small and fading resource and handles about 10 - 15 000 m³ p.a

(b) Wokabout Sawmills:

Many small local groups are now purchasing wokabout sawmills and endeavouring to produce sawn timber for village and local consumption.

These mills are fairly portable and are capable of sawing about one cubic metre of timber per day. They are now being produced in Lae and sell for about K5000 each.

The DOF does not seem to have any policy about wokabout sawmills yet, in the belief that their input is small and the equipment used in conjunction with them is not very damaging to the environment. Should they begin to proliferate however this situation will have to be reconsidered. At present many of them are being used outside the law, unless they are operating pursuant to officially issued Timber Authorities or unless they are selling produce only to "natives" within the meaning of the Forestry Act.

(c) Small to medium local sawmills operated by individuals or small companies or business groups.

These include:

- i) Lama Pty Ltd at Ialibu Southern Highlands which established a sawmill with New Zealand Aid Fund assistance. It is owned by local landowners and processes an input of approximately 10 000 m³ per year for domestic sales
- ii) Beechwood Pty Ltd This company claims to be substantially national owned and conducts a sawmill with an input capacity of approximately 10 000 - 15 000 m³ per annum for domestic sales. A large proportion of its timber is delivered to village owned break down mills by Beechwood for processing into flitches or baulk which is then trucked to the main mill for processing as sawn timber. The concept has worked well, to the satisfactions of all parties. It was initiated by the Department of Commerce (not Forests) and is

now a genuine self perpetuating nationally owned project which seems to be very much in line with the philosophy behind the "self help", "rural development", "small scale", "appropriate technology" aspects of the 1974 National Forestry Policy.

iii) Nakmai Company Pty Ltd after the collapse of the New Ireland Industries joint venture project involving Gaisho and the Landowner Company Nakmai the Landowner company appears to be in possession of the large, but for many years unused, Panamana Sawmill. Recently Groome (PNG) Pty Ltd leased the mill from Nakmai for K3000 per month and moved in its own sawmilling equipment. It is trucking in logs from elsewhere (as Gaisho cut out Nakmai LFA previously) and feeding them to the mill at an input rate of about 12 000 m³ per annum. The landowner company is involved only as lessor of the mill.

(iv) McDui is owned by automatic and naturalised citizens.

There have been a few former examples of national involvement in sawmills which have now ceased:

- i) After the war DOF sponsored sawmills at Lae and Kerevat to saw timber for postwar reconstruction and to train local sawmillers
- ii) On Buka Island between 1960 and the mid 1970s a small nationally owned mill known as the Hikalan Sawmill operated, processing about 200 m³ a year. It was self started and not promoted or supported by government.

- iii) Notako Business Group, North Solomons which operated a small forest mill

SUMMARY

As can readily be seen from the above list (which is a pretty full cover if not necessarily all inclusive) there has been no widespread and substantial involvement of nationals as owners in the sawmill industry producing for either the domestic or the export markets. There seems to have been no involvement in other forms of processing other than sawmills. (The situation of small reprocessing industries such as furniture making, wood carving etc. has not been examined but is known to be occurring infrequently and on a small scale).

What has been achieved by nationals has not been as a result of Forestry Policy administered by the Minister for Forests and the DOF. The larger and more successful ventures. (Lama and Beechwood) were promoted by New Zealand Government aid and the Department of Commerce. The other ventures seem to have commenced with no official involvement.

POLICY POSTULATE

- 11 INCREASE FOREIGN EARNINGS AND SUSTAINED ECONOMIC GROWTH BY PROMOTING LOG EXPORTS.

Until 1962 annual log exports had never exceeded 6 000 cubic metres. In that year they jumped from 4 800 m³ to 35,400 m³ and then climbed consistently to peak at 655,200 m³ in 1973/74 when there was a falling off and then a gradual rise to 472 500 in 1979. During that same period there was a fairly consistent increase in sawn timber

exports from 9 000 m3 in 1962 to 62,600 m3 in 1979. After the Revised National Forestry Policy was published in 1979 the change in production patterns and export figures has been most dramatic. Log exports rose continuously to reach 1,442,200 m3 in 1987 with plans to double the total again by 1991. Sawn timber has dropped from 62,600 m3 in 1979 to 2,700 m3 in 1988.

Revised Forestry Policy 1979 - guidelines:

The 1979 revision opened the door to increased log exports. No longer frowned upon, log exports were to be encouraged so as to boost PNG's foreign revenue earnings and to promote sustained economic growth in the timber industry and generally. It was not intended however to be a wide open encouragement to export logs. Guidelines were set by the 1979 policy revision which were aimed at maintaining a balance between log exports and local processing and to ensure that foreign investment was directed towards the high technology end of the timber industry and that national enterprises gained the main benefit from the comparatively simpler process of harvesting logs for export. Foreigners who wished to benefit from large scale log exports would have to provide substantial additional benefits for the people by also establishing large scale agricultural or reforestation projects or large scale integrated processing facilities. They would have to promote local training, business development and employment opportunities as well as paying export duty at 10 percent of FOB price, royalties and taxes. The measures to ensure that this happened were spelled out in guidelines in the 1979 policy revision.

The Revised National Forestry Policy 1979 is a clumsy document which seems to have been thrown together in a hurry and then published before the wording had been finalised. It is reproduced in full as a schedule to Appendix 2 of this Report. There are 16 guidelines of general application which were meant to control the allocation of log export quotas and then further guidelines applicable to four specific types of enterprise which were to be allowed to export logs. (These guidelines are fully discussed in IR No.6 Vol.1).

The rationale behind the guidelines displays a sound knowledge of the timber industry and the danger of allowing log exports to predominate over on shore processing. The guidelines were carefully formulated so that, if they were followed, most of the dangers of being overwhelmed by log exports could be avoided.

When these guidelines are listed, however, it becomes quite clear that the great majority of them have not been consistently applied and that allocation of export quotas have been made well outside the guidelines:

Guidelines of General Application

- A. Strict national government control over allocation of concessions and granting of export entitlements.

As previously discussed National Control has been weakly administered and has not been based upon proper planning or accurate knowledge of the resource. It has wavered under the influence of powerful lobby groups and has lurched from one allocation to the next. The only control

of exports has been importation of maximum log export good as in Permits and Reading agreements and the ability of the operators to extract logs to the generous maximum levels allowed.

B National government will specify guidelines for allocating concessions fairly between various areas and provinces.

No guidelines have been published and there is no National Forest Development Plan.

C. Monitor log export prices and market projections and fix total log export quotas.

The DOF and the FIC have kept records of disclosed export prices. In the last two years DOF Marketing Section has begun a serious study of international market prices in an endeavour to control Transfer Pricing. Total log export quotas have not been fixed on a national basis. The emphasis has been to seek to maximise log export quotas with scant regard to sustained yield forestry principles on a project, Provincial or National basis.

D. There will be a State Marketing Agent to sell some logs directly

A condition is to be inserted in each new or renewed Permit that up to 25% of the export allowance must be available for sale by or at the direction of the State Marketing Agent.

The enterprise will receive no less than the contract price less reasonable handling charges and marketing commission.

Eventually, after 7 years delay, the FIC took on this role as SMA. It did so without waiting for final NEC approval. It exercised the State's 25 percent option and conducted log sales on 15 shipments between mid 1986 and March 1987. In the process it made a substantial loss and its operations were flawed by inefficiency and illegality. Nevertheless it had the effect of substantially reducing transfer pricing and increasing the FOB price paid to PNG producers (IR NO 3).

Since the cessation of FIC marketing the DOF has exercised the State Option by acting as an agent rather than buying the logs. (See IR No 3).

E Restrict foreign investment to more capital intensive projects (involving woodchip and reforestation etc,) and give preference to PNG enterprises when allocating log export quotas for the less capital intensive projects.

Foreign investment has been allowed into all aspects of the timber industry and not merely into the capital intensive projects. Preference was given to two large Nationally owned Forest Development Corporations. These were Kumusi Timber Co. (see IR No 5 App 3) and Ulabo Timber Co. Neither has been successful and Kumusi was disaster (going into receivership within three years of commencement, with debts exceeding K3 million). Ulabo has limped on but is not successful.

Angus PNG Pty Ltd and Wawoi Guavi Timber Company received their original Permits in the fraudulent guise of being national companies. (IR No 2 and IR No 5 App 1) and there has been minimal national involvement in other timber enterprises.

There has been no effective export quota system and in the absence of such a system preference to local enterprises has been irrelevant.

F Log export entitlements will not be issued to operations being financed by a log buyer as part of a sole rights purchase agreement.

My inquiries have disclosed many instances where PNG producers are in fact selling predominantly and sometimes entirely to a buyer which has provided finance to the producer.

Some examples are:-

- . Gaisho (NG) was financing Fangalawa Plantations and acting as sole buyer for Fangalawa's produce from Ugana.
- . Sumitomo provided finance for Kumusi Timbers' contractors and enjoyed sole buying rights
- . Mitsubishi provided finance for United Timbers and enjoyed sole buying rights.
- . Three (possibly four) large Japanese Companies financed Gaisho (Japan) and Gaisho Japan financed Gaisho (NG). Between them the Japanese financiers and the parent company (Gaisho Japan) controlled all aspects of Gaisho (NG) marketing. The financiers were the main buyers
- . Nissho Iwai finances Stettin Bay Lumber Co (75% ownership increased later to 83%) and acts as sole buyer with very few exceptions.

These arrangements have greatly facilitated transfer pricing and other unfair marketing practices which I have reported upon in detail in IR No.6. Financial links with buyers has become more the rule than the exception.

G Forest Management controls-

- (a) firm control of volume of log exports;
- (b) approved forest management plan to be the base for government control;
- (c) standard environment protection clauses to be included in permits and agreements

- (a) I have found little evidence that individual operations are exceeding their total log export quota. In fact quotas are so high that they are usually under producing. There is little evidence that producers which fail to harvest their prescribed minimum cut are being penalised as provided for in their permit conditions. There are not overall control ceilings on log export volumes. The present aim is to increase levels of exports at a massive uncontrolled rate.
- (b) My comments on approved Forest working Plans as a control mechanism are already recorded at page 81. These FWPs have not been sufficiently detailed, rarely approved and almost never enforced.
- (c) Standard environmental protection clauses have been included in permits and agreements but, not being project specific, they are inadequate to protect the environment (see page.80). Compliance with these general provisions is not generally enforced.

H. Department of Forest and the Forest Industries Council to expand market promotion overseas

There has been very little market promotion overseas though it has been recommended by various commissioned consultants as a major aspect of policy to gain higher prices for both logs and processed timber. Market promotion requires a high degree of professionalism. (It is discussed in detail in IR NO 6 Vol.1).

I. The general rule is that the enterprise must construct the infrastructure it requires. This is negotiable and in some cases the government might assist by constructing facilities and charging for their use of doing so in return for a share of the equity.

This guideline seems to have been followed in almost all cases. Much of the infrastructure is, however, designed only to last for the duration of the (short term) project.

J. The government may negotiate the purchase of equity at par in potentially profitable enterprises.

The government has in fact purchased equity in SBLC, Open Bay, Kumusi, Ulabo and, through the Investment Corporation, it previously held a controlling interest in Madang Timbers. From these investments the government has received a bonus share issue in SBLC (raising its equity to K 1 million) which may one day make it a profitable investment. It has made a loss of K900 000 in addition to its original investment in Kumusi and made no profit from the other enterprises. It did not gain an effective say in corporate decisions by virtue of board representation in any of these enterprises.

K To assist the development of PNG enterprises associated with timber operations conditions are imposed on large operations harvesting in excess of 40 000 m3 per year over 10 year permit or longer.

Such enterprises must:-

- (a) adhere to a local business development programme to involve local enterprises such as tree felling, log extraction and supply of materials.
- (b) employ a business development officer to assist, and liaise with the Government on business development.

This guideline has been generally ignored. Lip service was paid to it in a few agreements. Only in the case of Vanimo Forest Products have detailed provisions been imposed upon a company to promote local business development. The company was not required to appoint a Business Development Officer but that position was created in the National Government Project team. It was never filled. (IR No 5 App 2).

The development of some local businesses has occurred in conjunction with the Vanimo project but on a minor scale only. It is generally not occurring in relation to other large or small projects.

L All conditions or revised conditions of agreement and permits will be enforced fully.

The enforcement of conditions has been notoriously weak as recorded in this report and the various interim reports.

The common experience has been that large enterprises have been allowed to blatantly avoid the conditions of their permits and project agreements with impunity. In the last resort the State has rarely been prepared to face the loss of revenue and political and landowner pressure involved in forcing an operator to close down. For example:

Wavoi Guavi Timber Co avoided almost all conditions on Block 1 and has still not completed the saw mill or carried out the natural regeneration trials required in Block 2. (IR No 5 App 1)

Open Bay Timber Co performed those infrastructure conditions which benefitted its operation such as the roads, bridges and township. Under its project agreement it failed to rebuild the (unused) sawmill which burned down but, instead, remitted the insurance money to its parent company; it totally failed to build its promised veneer mill, woodchip mill and kiln drier and for the last 16 years, it has entirely operated as a log export company. (It has commenced reforestation in a small way and its major reforestation obligation becomes due this year)

Vanimo Forest Products has still not commenced its major urban development project or its minor reforestation project (IR No 5 App 2)

Kumusi Timber Co was allowed to continue in receivership for over six years without fulfilling any of its infrastructure conditions (IR No 5 App 3)

New Ireland Otsuka held out for three years in open defiance of the government, refusing to fulfill its infrastructure obligations. It enjoyed the benefits of unfettered log exports for five years before the government finally closed it down. (IR No 6 Vol.4 App.6 Sched.2).

Nam Yang Timbers did build its chipmill but avoided its other major obligations. Having completed the mill it refused to operate it on the (probably true) basis that it would not be profitable. It continued on as a log exporter for several years before being closed down. (It has just been granted another permit in the same area).

Jant continues to clear-fell huge areas of natural forest to feed its chipmill but has not been able to fulfill its reforestation conditions because land has not been made available to it.

As well as failure to enforce major infrastructure conditions the Commission's reports detail numerous instances where other conditions are seriously in breach; such as conditions regarding logging practices, environmental protection, forest working plans, arrangements regarding letters of credit and marketing conditions. Not one enterprise investigated by the Commission has a satisfactory record of performing the conditions of its operation. These breaches are almost always tolerated by DOF and Forestry Ministers. Only Nam Yang, New Ireland Otsuka and Angus have been forced to closedown and this occurred only after years of operating contrary to permit and project agreement conditions and only when the enterprise was in such financial difficulty that its continued operation had become impossible.

M Training and localisation:

(a) Each negotiated timber concession will include a requirement that it will adhere to an approved training and localisation programme.

(b) A "training Grants Scheme" is discussed for possible future implementation.

This guideline has not resulted in strict insistence on detailed training programmes being submitted, approved and enforced by Forestry Inspectors. DOF has not given high priority to training and localisation and has been generally content if the Department of Labour and Employment guidelines were being met. Thus although VFP had a specific obligation to carry out an approved scheme of training and localisation as part of its project agreement it satisfied this obligation by simply submitting a series of organisation charts to the Department of Labour and Employment indicating, in relation to each establishment position, the year in which a national employee would begin to work alongside the incumbent expatriate and then the year in which it is proposed to localise.

As far as training is concerned VFP merely promised to send employees on training courses when available. Neither DOF nor the Department of Labour and Employment have systematically followed up to enforce this localisation programme. A study of the file shows several applications to extend localisation deadlines have been made by VFP. Despite this VFP has done more to localise than other companies. (IR No. 5 App. 2).

In this way four logging supervisors positions and the Planning section has been localised.

The training grants scheme proposed in the 1979 Policy Revision has not been implemented.

N Measures to protect log export revenues

(a) Strict control of volume of log exports by setting national priorities for the allocation of timber permits and log export quotas.

(b) "minimum guidelines prices" will be imposed;

(c) Marketing agreements and arrangements for sale of logs to be subject to government approval;

(d) Encourage domestic sales of processed timber but not by imposing tariffs or import quotas which would raise prices.

(a) Control according to National Priorities: The 1979 Revised Forestry Policy stated that a National Forestry Development Plan would be drawn up in consultation with provincial governments and with their approval and this would set the national priorities.

In fact a Plan was submitted with the NEC submission and was approved at the same time as the Revised Policy. It had not however been formulated in consultation with the provincial governments. Subsequent attempts to gain Provincial input and approval for a national plan came to nothing.

National priorities for the allocation of timber permits have been set by producing and updating a National Forestry Development Programme which lists proposed areas for allocation and sets a timetable. At least in recent years, the rationale behind the programme seems to be that every forest area with a commercial potential should be

checked out, surveyed, purchased and prepared for allocation at the earliest date which constraints of staff and funding will permit. The political direction has been to apply the accelerator pedal rather than the brakes and the current "boast" is that the level of log exports can be doubled before 1991.

Although an intention to contain harvesting within levels that will allow sustained yield forestry is often expressed, my inquiries show that there is no clear consensus in DOF as to what sustained yield forestry means and that there is insufficient knowledge of the national resource (or the resource of any one area) to enable it to be implemented effectively (See IR No 5 App 4 and the Schedule to IR No 4 Vol 1)

(b) **Minimum Export guidelines:** These have been imposed but far from controlling price fixing practices, the published MEP figures have been a great encouragement to transfer pricing as the figures are discounted and out of date. The MEP is commonly about 15 percent below true market price. (See IR No 6). It was for several years used as the maximum price producers felt obliged to disclose in PNG and the amount actually received above MEP was transferred offshore.

The position has improved since State Marketing involvement through DOF and FIC and with the altered system of ship by ship export licences (see IR No.6 Vol.1).

(c) **Approval of Marketing Agreements:** Various methods have been used to try and subject marketing agreements and arrangements to government approval (and see IR No.6 Vol.1):

- i) The terms of Permits and Project Agreements provide for arms length sales, fair market prices and specific directions to open the letter of credit in favour of the permit holder (not the contractor). Similar requirements are commonly included also in logging and marketing agreements between permit holder and contractors and these agreements require approval of the Secretary (DOF). Until very recently these conditions regarding marketing have been almost universally ignored.
- ii) The establishment of a State Marketing Agent (SMA), coupled with a requirement for timber enterprises to offer it 25 percent of produce and for the SMA to arrange sale at its option is another method of gaining marketing information and control over marketing.
- iii) One effective control mechanism available to the government is its power to refuse to grant an export licence to allow a log shipment to depart. This power is exercised by the Minister for Trade and Industry pursuant to the Exports (control and Valuation) Act Ch.108. If the Secretary DOF believes that a shipment is underpriced he can recommend to the Minister that he refuse to issue the export licence. Since the system of issuing individual licences for each shipment was introduced this has become an effective weapon, especially when used during the past year by the DOF Marketing Section (see IR No 3 and No 6).

Additionally the Minister for Forests has power to grant or withhold export permits which are also issued on an individual shipment basis and this is entirely within his own jurisdiction. It could be used to control marketing agreements between shippers and their buyers and to enforce other conditions (IR No.6 Vol.1)

Theoretically therefore DOF now has powers which can be effectively used to approve or disapprove marketing agreements. For a short period from mid - 1987 this was used to good effect. However, shortage of staff, facilities and incentives are now reducing DOF's effectiveness, as predicted in Interim Report No 3.

(d) Encouragement of Domestic Sales of Processed Timber: This has for many years been stated policy of government. The sad truth however is that it just has not happened. It was the aim that log exports would not be allowed from areas close to major domestic markets such as Port Moresby, Rabaul and Lae. Nevertheless ANG Timbers which was sawmilling near Port Moresby was starved of resources and its potential concession area was allocated to Goodwood Pty Ltd in record quick time (IR No.2 pp.2 App.39) Goodwood is now over one year behind in constructing its Sawmill and Port Moresby is now very short of sawn timber. Meanwhile Goodwood has spent the last two and half years exporting Port Moresby's intended sawn timber supply overseas as round logs.

MacDui Development, which took over the ANG Timbers sawmill has struggled to obtain a resource in reasonable proximity to sustain the mill and is unable to meet the domestic demand levels of the Port Moresby market.

Something similar happened in Rabaul when the Vudal area was allocated to Weco instead of being used as the resource area for Nohga sawmill.

Both these decisions were made by Forests Minister Diro in "irregular" circumstances. The Goodwood allocation was "given consideration" and then "pushed through" in a matter of 21 days after receipt of a one page proposal. This was on the last day before Mr Diro's sudden and unexpected departure from the Forestry portfolio and has never been satisfactorily explained. It seems the signature was put on the permit document one day after Mr Diro had been removed from the Forestry portfolio. The permit was actually issued before the cancellation of ANG Timber's permit over the same area.

The allocation to Weco was made after Mr Dixo had been persuaded to change his mind at the instigation of Mr Ward of Weco. Ward worked through Cowan of the FIC to influence (and probably to trick) Minister Diro. Under this influence Mr Diro revoked his previous decision to grant the concession to Timbersales, which required the timber to supply its sawmill, and appointed FIC chairman Maraleu to make an "objective" decision between Weco and Timbersales. Maraleu, who was paid adviser to Weco, decided in Weco's favour and the resource was then allocated to Weco by Minister Torato to be largely exported as round logs.

Recent allocations have demonstrated some degree of commitment to local processing but it is still being treated as a secondary aspect of primarily log export operations. Thus the recent Permit issued over the large Arawe concession provides that a 50 000 m³ (one shift) capacity sawmill must be constructed and operating by the end of the second year of the operations. This shows some concern for onshore processing but the processing conditions

(yet to be finalised) will inevitably mean that the reject logs will be directed to the sawmill and the best logs will be exported. No attempt was made to include further processing to use up reject logs and waste.

Even the new allocation to SBLC at Ania Fullerbourne adopts this approach and SBLC's commitment to onshore processing is not exploited by the new agreement. Under the agreement SBLC is actually permitted to reduce the volume it is presently processing during the first few years. Similarly it has not been required to introduce the further processing (such as a medium density fibre board mill) which I believe, on the evidence of its general manager, SBLC is ready to commence. (IR No.6 Vol.3 App.5)

0. Increase log export taxes to 10 percent of FOB. price for all non-processing log export operations

This policy was implemented. In large processing log export operations a discount on export duty has been allowed if the minimum processing requirement is met. This applies to Stettin Bay Lumber Co and Vanimo Forest Products Pty Ltd and is a major incentive for them to meet their minimum processing requirement.

On the other hand Wawai Guavi's conditions impose a log export quota reduction penalty for not fulfilling the processing requirement. This has had no effect because WGTC's export quota was raised well beyond its capacity to produce. Consequently its failure to construct the required sawmill has resulted only in a temporary reduction, on paper, of its inflated export quota.

As previously mentioned, a bureaucratic error cost the government hundreds of thousands of kina when the duty was levied on MEP rather than on FOB price as stipulated.

SUMMARY

The 1979 Policy was intended to control log exports so as to protect the domestic sawn timber market and to ensure that PNG producers and the Government received the best possible price for those logs which are to be exported.

The national control has been too weak, and has been subjected to too many improper influences, to effectively protect the supplies to our major domestic markets. It has also been unable to effectively stimulate the integrated processing enterprises which would reduce waste and encourage efficient onshore processing and which would ensure an adequate supply of sawn timber for domestic and export purposes. The concept of setting a "minimum export price" has been allowed to become the main mechanism setting the rate of transfer pricing. The policy of subjecting marketing agreements to government approval at various stages has not been applied effectively.

GUIDELINES FOR SPECIFIC ENTERPRISES

The four types of operation which are given special attention are set out in the White Paper under the following headings:

1. Proposals and Guidelines for the Formation and operation of Papua New Guinea Log Exporting Enterprises.
2. Guidelines for Enterprises involved in Timber Processing

3. Guidelines for Foreign Enterprises involved in Large Log Exporting operations and not processing within PNG;
4. Guidelines for Foreign Enterprises involved in limited log export/road construction contracts;

1. PROPOSALS AND GUIDELINES FOR THE INFORMATION AND OPERATION OF PAPUA NEW GUINEA LOG EXPORTING ENTERPRISES.

These enterprises came to be known as Forest Development Corporations. The intention behind the proposals was to assist the actual landowners to fully participate and share in the benefits of the timber operation occurring on their land. They were to receive government assistance in their formation and were to be granted rights to harvest and export logs free of most of the onerous conditions which were to be imposed upon "outsiders". The guidelines for these are:

- (1) Assist with finance and advice the formation of PNG owned log exporting enterprises. (Dept. of Commerce (Business Development) and Dept. of Forests to act jointly).
- (2) To spread the benefit more widely, share-holding in PNG log export enterprises will be held by one or a combination of the following groups-
 - . National Government
 - . Provincial Government
 - . People of the Forest Area.
- (3) PNG Log export enterprise to be managed for the first 10 years by an approved contract manager.
- (4) PNG Log export enterprise to be freed from "non profitable" infrastructure obligations.
- (5) Early profits to be used to repay loans.

(6) (a) Follow up land use plan (agriculture or reafforestation) to be drawn up before logging operation is approved and submitted with the log export proposal. But funding will be by national government and it will be managed separately from the log enterprise.

(b) A land use planning group to be set up within Department of Primary Industry to evaluate and monitor the entire follow up land use project.

(c) Land for it must be acquired prior to commencement of logging.

Only two Forest Development Corporations were established and neither was successful, Ulabo Timber Company Pty Ltd and Kumusi Timber Company Pty Ltd. Ulabo is not profitable because the resource granted to it was insufficient. Kumusi Timber Company Pty Ltd failed because of management problems, insufficient resource and because of poor planning and inaccessibility of the resources (See I.R. No.5 app.3). Several others were planned but never eventuated. Subsequently some companies sought to gain some preference in allocation of permit and less onerous conditions by posing as national companies (one of these was Angus PNG Pty Ltd, (IR. No.2) and others were Wavoi Guavi Timber Co (IR No.5 app.1) and Bruce Tsang's Companies (IR No.4 app.4). In fact they did not fall within the scope of this policy guideline.

After the failure with Kumusi and Ulabo this policy seems to have been abandoned.

2. INVESTMENT GUIDELINES FOR ENTERPRISES INVOLVED IN TIMBER PROCESSING

The White paper proposed the following guidelines for these enterprises:

1. Firms seeking to invest in timber processing will be assessed on the following criteria:
 - (a) experience with similar processing;
 - (b) record of profitable and efficient processing activities;
 - (c) experience in forest products marketing;
 - (d) financial capacity

2. Measures to encourage timber processing:
 - (a) allow more log exports if enterprise has poor access to domestic market for processed product or an inferior resources composition;
 - (b) taxation incentive (set out in some detail);
 - (c) possible reduction in royalties payable;
 - (d) non application of proposed 10% export tax if processing commitment is fulfilled;
 - (e) assistance in technical and managerial training of PNG employees;
 - (f) release from reforestation requirement
 - (g) failure to meet processing commitments may result in -
 - . loss of export tax rebate;
 - . reduction of log export quota
 - . cancellation of permit and recovery of damages;

3. Foreign enterprises may be allowed to combine log export and processing within the following guidelines:
 - (a) at least 30% of log harvest must be processed (higher for enterprises with good access to a domestic market or a good resource);
 - (b) processing schedules and planned expansion to be negotiated at the outset;
 - (c) no log exports near a domestic market if forest resources there are limited or in other places if forest resource is too limited to sustain a long run commercial log export operation.

Marketing guidelines for processing enterprises will be the same as for large log exporters set out in Part 4.

So far there have been very few companies attracted by the opportunity to commence a large on-shore processing facility. Mostly it has been a case of companies being attracted to commence a large log exporting enterprise and then being obliged by the government to, reluctantly, undertake a degree of local processing as part of the price of their log export quota. Jant Pty Ltd in the Gogol Forest near Madang is the only significant exception as it was attracted to commence chipmilling to supply its parent company in Japan, the Honhsu Pulp and Paper group. Until very recently it was not given a log export quota at all.

Vanimo Forests Products was attracted under this policy guideline and did establish a sawmill with a 30 000 m3 input capacity. It was also granted a log export quota of 200 000 m3 per annum and is rewarded for fulfilling its sawn timber quota by application of the export duty rebate and bonus log quota rules. With the aid of these incentives it meets its processing obligation in an inefficient and wasteful way but its main interest, most certainly, is on the log export side (IR No.5 App.2).

It is showing only reluctant interest in pursuing feasibility studies into further processing.

Stettin Bay Lumber Co commenced its present operation in 1982 in accordance with this guideline. Like VFP it shows only reluctant interest in further processing and reprocessing. Unlike VFP it has established extensive plantations. (See IR No 6 App 5 and p 165 of this report).

Wawpi Guavi Timber Co and Open Bay Timber Co have so far managed to avoid their processing conditions entirely or almost entirely (IR No 5 App 1 and IR No 6 Vol 4 App 6)

More recent allocations appear to be following the 30 percent of log export processing formula (Arawe and Ania Fullerbourn).

Other companies which formerly processed timber as the most significant aspect of their enterprise have, since 1974, substantially reduced the processing side in favour of increased log exports. The category includes Ambogo Sawmills, and Wewak/Madang Sawmill Company Pty Ltd.

The drop in the total volume of sawn timber being produced continued to fall from 21000 m3 in 1982 to 4000 m3 in 1987. The figures are a compelling statement about the failure of this aspect of government policy.

3. THE GUIDELINES FOR FOREIGN ENTERPRISES INVOLVED IN LARGE LOG EXPORT OPERATIONS AND NOT PROCESSING WITHIN PAPUA NEW GUINEA

The 1979 White Paper provided the following guidelines for large foreign log exporting enterprises;

- (1) *The basic premise is that such a concession should only be granted for operations which are combined with substantial additional activities such as agro-forestry projects or reforestation which require large amounts of capital or advanced technology.*

There are so many exceptions to this rule that it cannot be put forward anymore as Government policy. In most cases such conditions have either not been imposed, or have been imposed with "escape clauses" or merely as a feasibility study requirement. In other cases firm conditions to conduct such additional activities have simply been avoided. Many examples are dealt with in the various interim reports. They include Wawoi Guavi Timber Co, VFP, Kumusi, Angus, Goodwood and all the New Ireland companies (except DLAD which purchased some plantations to

satisfy its obligation to an agricultural project). SBLC is virtually the only company actually performing reasonably under this guideline.

- (2) The foreign enterprise must prove that it has enough experience, expertise, capital and marketing skill to handle all aspects of the proposed venture.

SBLC has satisfied this guideline with capital and skills in both the logging, sawmilling and reforestation aspects. VFP has capital and skills required for its operations.

Rimbunan Hijau undoubtedly has the capital and skills required for an integrated diverse operation and SEAL, recently approved as contractor on Manus Island, has the capital and skills required for the proposed Veneer Mill.

A long list could be made of companies who lacked capital and/or skills and it would include WGTC, Angus, Goodwood, OBTC and many others.

- (3) Such large scale of log export operations will be restricted to forest areas which:

- (a) have a large resource which will subsist until a reforestation plantation is ready for harvesting or until other follow up development is able to sustain economic activity; and

- (b) where the forest mix is unsuitable for processing, (this limitation is difficult to understand and, apparantly, not followed) and

- (c) where the forest is not required for a nearby domestic market for processed timber (such as Port Moresby, Lae, and Kavieng).

Guidelines (a) and (b) appear to be given no attention whatsoever. Although some attention has been given to protecting domestic sawn timber supplies, there are,

however, serious breaches regarding Port Moresby's needs and Rabaul's needs (Goodwood and Weco allocations respectively - see pages 191-192 above)

4. The large foreign log exporter (not processing) must undertake an activity which:-
- (a) integrates well with a logging operation; and
 - (b) will sustain economic activity in the timber area on a permanent basis; and
 - (c) together with logging requires a total investment of at least K5 million; and
 - (d) is included as a priority or open activity in the National Investment Priorities Schedule; and
 - (e) otherwise conforms to the policies of the National Government and the provincial government concerned.

The only large foreign exporters which are not processing are Wavoi Guavi Timber Co, Goodwood and Open Bay Timber Co. The first two were to process sawn timber but all are behind in completion of their sawmill. OBT built its mill which burned down, avoided its other processing obligations and has promised to build a chipmill in the future. None of them is undertaking any activity which complies with this guideline. All other foreign companies exporting logs are doing so on contract to a, so called, "national landowner company". By this means they avoid the guideline, as their puppet company, rather than themselves, becomes the exporter. None of these landowner companies are conducting the activities required under this guideline.

5. Failure to satisfactorily perform the associated projects within the given timetable may result in the imposition of monetary damages as well as curtailment of their permit.

The experience has been that foreign log exporters have always failed to satisfactorily perform the associated projects to the extent that they have been imposed. I know of no case where monetary damages have been imposed or a permit was curtailed for failure to undertake this type of required activity.

6. For all other matters large foreign log exporters will be subjected to the same conditions as are imposed on processing enterprises under Part 3 of the White Paper particularly regarding infrastructure, equity, PNG associated enterprise, and training and localisation.

The guideline has been discussed already.

7. Joint Ventures between a PNG log exporting enterprise and a foreign log exporter may be approved. The foreign company would hold a minority shareholding in such a venture

Such joint ventures occurred in Nakmai and Danfu (IR No 4 Vol. 2 App.6). Despite being the minority shareholder the foreign partner (Gaisho) exercised complete control of the operation and the transfer pricing. Other companies such as Wawoi Guavi Timber and Angus (PNG) were "sham" national companies which were in fact majority foreign owned.

When the large log export operations which have actually been established are measured against these guidelines the observer could be excused for believing that the guidelines were prepared for a different country. It became apparent during the course of this inquiry that virtually none of these guidelines are being consistently followed.

4 THE GUIDELINES FOR FOREIGN ENTERPRISES INVOLVED IN LIMITED LOG EXPORT/ROAD CONSTRUCTION CONTRACTS

The 1979 White Paper provided the following guidelines for log export/road construction enterprises:-

- (1) A log export permit may be granted to an enterprise in exchange for it constructing a priority road.
- (2) It must be capable of building the road to the required standard and within the given timetable.
- (3) Applications will be decided on a tender system and the enterprise requiring the least volume of log exports will be considered the lowest tenderer. But the contract may be allocated without putting to tender to an existing timber enterprise already working in the area.
- (4) The proposed road must be a clear priority road which would not normally be constructed as part of an existing timber operation or within the required time period or at less cost under a normal road construction contract.
- (5) The forest resource must be capable of sustaining the amount of logging required.
- (6) The term of the timber permit will normally be less than 5 years.
- (7) Export tax on logs will be 10% of F.O.B price and normal royalties will be paid.
- (8) No infrastructure or other associated conditions will normally be imposed.
- (9) All standard timber permit conditions will apply.

As a general rule enterprises which have been operating as log exporters and road constructors have completed the assigned roading, probably because certification to that effect is a condition precedent for granting the log export licence. It seems to work fairly well.

SUMMARY

The decision to encourage log exports had not been intended to result in the mad rush to get logs to the sea which has, increasingly, occurred. There was meant to be strict control over allocations to protect local processing, the domestic market and the future of the forest resource. The controls proved inadequate and the political will and bureaucratic efficiency and organisation were not sufficient. Foreign investment has been allowed to gain a position of nearly absolute dominance and some of the foreign timber companies have bribed, bought and tricked their way into an unholy partnership with whichever landowners, leaders, public servants and politicians were necessary for their immediate aim of getting access to, and marketing, logs.

There has been virtually no government sponsored market promotions, insufficient research and very little emphasis has been put on protecting the environment, the forests or the true economic and human needs of the landowners. Little benefit has flown to the landowners and even the government has been grossly underpaid by virtue of the wholesale and fraudulent transfer pricing which has occurred. This has cheated the government out of company and export duty to a staggering extent.

In general the timber companies have performed reasonably only the conditions which benefitted their own operations. Thus in many instances roads, bridges, townships and wharf facilities have been completed. Conditions regarding agricultural projects, reforestation, local business development and onshore processing have been performed rather reluctantly, long behind schedule, or

avoided altogether. Companies like Jant and SBLC (and in recent times OBTC), whose operations are based on long term processing, have tended to be more responsible in performing their obligations under project agreements.

POLICY POSTULATE

- 12 DESIGN TRAINING PROGRAMMES WHICH ARE RESPONSIVE TO MANPOWER NEEDS OF THE GOVERNMENT FORESTRY AND FOREST INDUSTRIES SECTORS.

There have been three levels of training in forestry; the four year degree course at the University of Technology, the three year diploma course at the Forestry College and various types of technical and inservice training at the Timber Institute Training College.

The performance has been seriously marred through lack of manpower planning. The syllabuses have been based on preparing graduates to fit into the forestry scene described in the 1974 policy document. This means they graduate with skills required for plantation management, reforestation, research and various types of processing and reprocessing techniques.

Many have found it hard to get a job in an industry which concentrates almost exclusively on logging for export and which prefers to import Asian skilled personnel.

POLICY POSTULATE

- 13 CONDUCT AND COORDINATE RESEARCH DESIGNED TO ACHIEVE NATIONAL FORESTRY POLICY REGARDING MANAGEMENT, UTILISATION AND CONSERVATION OF THE FORESTS RESOURCES

Research has been well funded and staffed in comparison with DOF's total budget and staff position. Thus about 20 percent of DOF budget was allocated for research in 1987 and about 50 percent of total staff.

Research priorities however have not been clear nor sufficiently related to overall forestry policy and requirements. A major reason for this is that expressed policy itself has wavered and is not closely related to actual forestry activities.

From the 1950s to 1985 the priority research emphasis was associated with plantation projects in the mistaken belief that the stated policy of promoting integrated processing operations on permanent forest estates would be implemented in fact. Had this occurred then research into forestry plantation species and management technique would have been appropriate. In fact however, as has been clearly shown, the defacto policy has been to encourage a massive increase in felling for export as logs. The research which was desperately needed to counter the destructive effects of this programme was research into sustainable yield management techniques, logging practices, natural regeneration of forests and post logging care and treatment. This approach was not adopted until 1985. The consequence is that forestry research has not really been designed to achieve the national forestry policy because of the difficulty of indentifying that policy and holding it in place.

The failure to formulate and follow a clear statement of policy has obviously thrown forestry education and research into confusion. It has had a similar effect upon forestry officers whose job is to enforce policy and it must similarly have confused timber operators - particularly those who actually wanted to "follow the rules". For those who were determined to act outside the rules anyway, policy uncertainty is the ideal environment in which to operate.

CURRENT NATIONAL FORESTRY POLICY

After studying all available policy documents, legislation and constitutional laws and after two years of studying forestry in action I remain at a loss as to how to define the current policy. It is easier by far to say what it is not, than what it is.

It is not the 1974 Policy even though it is still technically in place.

It is not the principles required by the Constitution. I say this because there is no apparent aim to preserve the forest resource for the benefit of future generations; it is not being controlled effectively in the national interest; there is no emphasis on PNG ways and PNG forms of economic and social organisation and no effective meaning is being given to the professed aim of decentralisation of political and economic structures.

It is not the 1979 Revised Policy. It follows that policy to the extent of encouraging an increase in log exports but none of the guidelines, which were designed to protect the country from the abuses which could flow from that course of action, are being followed.

Having failed to find a clear statement of existing forestry policy, I postulated thirteen broad policy principles from a study of a variety of documentary sources.

The thirteen broad policy principles which I postulated, and against which I analysed the current defacto situation, as disclosed from the Commission's inquiries, were drawn from policy documents such as the Constitution, the legislation, the 1974 Policy and 1979 Revision, NEC decisions (such as those approving the FIC as the State Marketing Agent and approving the 1987-1991 National Forest Development Programme) and various sectoral plans and policy statements included in budget papers which have received NEC approval.

Two years of detailed investigations have convinced me that none of those thirteen broad policy principles, or postulates, are reflected meaningfully in practice. With the exception of the eleventh postulate, that which aims at increasing the level of log exports, the government shows little or no sign of genuinely trying to base its actions on those postulates. With regard to log exports the government is certainly encouraging them but it is not applying the principles of restraint and control demanded by the 1979 Policy Revision.

When postulating the thirteen broad policy principles taken from various "official" documentary sources I limited myself to sources which had a sufficient degree of "authority".

I have deliberately omitted detailed reference to various draft policy statements which have been prepared in the Department of Forests but which have received neither Ministerial nor NEC endorsement.

There have however been reports on policy by consultants which have recommended revised policy and even submitted outlines of draft new forestry legislation. There have also been a series of draft revised policies prepared within DOF which never received Ministerial approval.

The main work by Consultants was done by Michael Gane of FAO and Richard Campbell in 1985. The first phase of their work produced a policy statement and an outline for a new Forestry act and in May and June 1985. The second phase involved the preparation of a draft Forestry Act in 1986 based upon the first phase report as amended by DOF. The work of Gane and Campbell was published by FAO, Rome in 1987.

I am aware that drafting instructions to establish a Timber Industries Board were prepared by the Wingti government just before it was ousted from power by the last vote of no confidence.

In June 1988 a committee in DOF worked upon and published a new draft policy which appears to have drawn upon some of the policy seminars organised by this Commission for part of its inspiration. It was not submitted to NEC and did not receive ministerial approval.

Under the new Minister for Forests, Mr Karl Stack, drafting instructions for a new Forestry Act were prepared and submitted to NEC for approval. Approval was given on 12 October 1988 for a Forest Bill to be drafted for presentation to the November session of the National Parliament.

The problem is that the question of forestry policy has still not been resolved. The drafting instructions merely draw heavily on Campbell's 1987 draft Forestry Act as its basis. They follow exactly the same format but portions have been deleted, especially sections which imposed checks and balances on the powers of the National Minister.

The provincial governments complain that they were not adequately consulted during policy formulation and not at all during preparation of the drafting instructions. A special Premier's Council Consultation Meeting on the 17 and 18 October 1988 expressed this concern and set up a Working Committee which met twice and then reported in January 1989. (Report of the Premiers Council Working Committee on Proposed Forestry Legislation January 1989). The report is very critical of the lack of consultation and of the drafting instructions. Industry also offered severe criticism of the drafting instruction and the lack of consultation and forced the Government to agree to a "breathing period" to allow discussion and comment from industry. The Bill is not yet prepared.

Drafting Instructions for Forestry Bill Oct 1988

The Drafting Instructions approved by NEC on 12 October 1988 are for a Bill which would abolish the current legislation and the system of acquisition by Timber Rights Purchase. This form of acquisition and the existing LFA

procedures are replaced by a contractual arrangement entered into between the State and a landowner company. In this way the landowners would retain legal title to the land but would contract to permit the State to acquire exclusive right to fell and remove their timber resource. It is difficult to see how this arrangement can be given simple legal effect as it assumes that the representative landowner company can lawfully acquire or claim rights to ownership of the land. To facilitate this the instructions specify that only 75% of residents are required to approve it.

Allocation of operating rights shall be by permit, licence or grant. These are issued by the Minister. While a tender procedure is envisaged it shall be possible for the Minister to waive the necessity for this. Some requirements are stated to be mandatory while others shall be optional. The optional requirements include the submission of a satisfactory Environmental Plan and proposals for onshore processing facilities and the proposed volume of log exports. I would consider these to be properly mandatory requirements in all cases.

The existing system of pre-registration is not formalised and information concerning the experience and financial capacity of a proposed operator is not required.

The role of Provincial Governments is acknowledged with some functions given to them exclusively and some stated to be concurrent. They can also assume some responsibilities of the National Government by delegation. The National Government is to take control of Provincial Forest Officers and may direct and discipline them.

While some clear emphasis is given to reforestation the principles of sustained yield management are not recognised. But a Forest Research Institute shall be established to collect relevant data and twenty percent of land shall be retained by the state for reforestation and agro-forest projects.

Royalties shall be fixed at 10 percent of FOB or market value and shall be paid to landowners. Provincial Governments shall receive a levy of K1 per cubic metre paid into a Follow-Up Land Use Fund. Levies known as the Forest Development Fund and the Forest Industry Fund shall be used to fund reforestation and the proposed Forest Industries Office respectively

The Forest Industries Office is given a broad range of responsibilities including the research and development of marketing and promotion; control over reforestation and agro-forestry projects, the issuing of export and import permits and the inspection and grading of forest products. This office shall be responsible to the Secretary of the Department of Forests.

The drafting instructions leave many delicate and key questions undetermined and it would be premature for me to describe the proposed Bill as representing the forestry policy of the National government in any way.

World Bank Report

A specialist World Bank team has recently completed the second of two fact finding visits investigating the forestry industry with a view to providing long term financial and technical assistance towards its development. With the approval of the Prime Minister I gave that team the benefit of the Commission's findings on certain matters.

From my discussions with members of that World Bank team I am aware that it is now preparing a report which will outline areas of policy reform and make policy recommendations - even to the extent of providing an outline of drafting instructions for the type of consolidated Forestry Bill which would support the policy the Bank proposes that PNG should adopt.

In these circumstances I have been content to limit my report strictly to the fact finding emphasis of the Commission's terms of reference. Although discussions were held with both Prime Minister Wingti and, subsequently, with Prime Minister Namaliu about the desirability of extending my terms of reference to request me to make recommendations on Forestry Policy this was never done. This may be just as well because a "Judicial Inquiry", conducted by a Judge with no technical expertise in Forestry, is probably not the most appropriate body to make recommendations on Forestry Policy.

This then is a factual report. I am asked to define what "the existing Government policy relating to forestry is" - particularly "relating to resource allocation, conditions of operations, marketing and pricing of timber". The only meaningful approach to this question is to define "defacto policy".

DEFACTO FORESTRY POLICY1 Resource Allocation

- (a) The policy is to retain power over resource allocation firmly in the hands of the National Minister for Forests and he exercises this power in his absolute discretion with no requirement or accepted practice of referring important allocations to NEC.

Although consultations with provincial governments may occur prior to allocation, they have no power of veto and little influence over the national minister if he has decided to allocate and feels he is supported by vocal landowner groups, backed up by a foreign timber company which is ready to start operating.

There is no clear statement of national forestry policy and no National Forestry Development Plan, worked up in conjunction with provincial governments, which sets the principles for deciding upon resource allocation. The Minister's discretion is, therefore, left dangerously unfettered.

There is a National Forestry Development Programme which sets out a schedule of areas for allocation and a timetable of "deadlines" which DOF is expected to achieve to keep the allocations on target.

The NFDP has not been prepared so as to implement clear national policies and priorities (because these are not known) nor has it been designed with meaningful participation by the provincial governments.

- (b) The Defacto Policy behind the National Forest Development Programme is to allocate as many resource areas as can be prepared for allocation within the life of the plan.

- (c) The overriding policy consideration is the need to increase national revenue and foreign earnings. This need overrides normal restraints such as staff availability.

Staff have been moved from other important tasks so as to boost the strength of those officers planning and preparing for further allocations. It has long been known that there is a desperate shortage of staff and funds for monitoring logging operations and for supervising the performance of permit conditions. The knowledge however has not forced a slow down in the rate of allocation. In the most recent budget, in fact, the monitoring section's budget has actually been reduced by almost 50 percent.

There is full knowledge of the fact that the conditions of existing permits and project agreements are not being enforced and that, as a consequence, substantial damage is being caused to the forests and the environment and substantial financial loss is being caused to government (through lost revenue) and to landowners. Nevertheless;

- (d) the defacto policy is to double the rate of allocation and to allocate more than four million further hectares of forest by 1991. The vast bulk of this timber is to be exported as round logs.
- (e) Realising that the basic data available on the quantity and quality of the remaining resource is very inaccurate and overly optimistic the defacto policy is to allocate and to take the risk that it may result in overcutting.
- (f) Though there is an often stated policy of sustainable yield management, that is in fact not the basis of allocation and permit conditions.
- (g) When there is an apparent conflict between the national interest in preserving the resource and an individual or group interest in exploiting for immediate cash reward the policy is to favour the individual or group right.

- (h) The defacto policy is to respond promptly and positively to pressure from local landowner companies for allocation of new areas by way of LFA or TRP even though the area is not scheduled for allocation in the NFDP - especially if the application is supported by the provincial government, Premier or prominent Ministers. If provincial government opinion is against the allocation which the Minister plans to make it tends to be overruled.

2 Conditions

(a) Actual Conditions:

It is policy and practice to write conditions into permits requiring;

- i) Construction of some infrastructure such as roads and bridges and, for larger projects, wharf facilities, a township and (possibly) a major processing plant.
- ii) The current tendency is to impose a condition to process 25 per cent of the allowable export quota through a sawmill though several years of straight log exporting are allowed before the condition takes effect.
- iii) It has been policy to sometimes impose conditions to assist in the development of an agriculture or similar project and/or promote local business development.
- iv) There has frequently been some requirement to stimulate natural regeneration in the forests or to plant up afforestation plantations.
- v) There has always been a policy to include general conditions relating to protection of the environment but rarely specific conditions. In recent months it appears to be the policy of the Minister for Environment and Conservation to insist upon the submission and approval of an Environmental Plan before the operation commences.

- vi) There has always been a policy to include conditions requiring the permit holder to seek fair market price by arms length sales.
- vii) There have always been conditions requiring good logging methods and follow up silvicultural care.
- viii) For larger projects it is common to require the permit holder (or contractor) to conduct feasibility studies into various desirable practices such as further processing, alternative energy sources and associated industries and activities such as agro-forestry and crocodile farms.

(b) Enforcement of Conditions

Enforcement of conditions has been notoriously weak. Although stated policy is to enforce all conditions strictly this is so patently not done that the policy should be restated:

- (i) Tolerate breaches of conditions if there is a chance of keeping the operation going. Cancel permits only as a last resource and meanwhile seek to accommodate the operator and renegotiate onerous conditions in order to maintain export duty and to safeguard the local job opportunities provided by the operation.
- (j) Do not undermine investor confidence by taking too hard a line on the export of illegal produce. Try and prevent illegal logging before it occurs, but, if it happens, grant the export licence and try and secure the proper payment of export duty and royalties later.

Reafforestation conditions have been generally avoided to such an extent that the policy should now be stated as;

- (k) Do not seek to force logging enterprises to reafforest except those which are undertaking a long term processing commitment (such as Jant, SBLC, and OBTC). Encourage their reafforestation programme by granting the right to export massive volumes of logs until the plantations mature.

A most recent trend should possibly be added as de facto policy

- (1) "substitute a reforestation levy of K1 per m3 for a requirement to establish reforestation plantations"

Whether the reforestation fund will actually be used for that purpose or merely be treated as a boost up for general revenue is not yet clear. DOF claims that it has established an authorised Reforestation Trust Fund, which seems a good idea.

Natural regeneration conditions, good silvicultural practices and good logging technique conditions have never been enforced. The conditions themselves are worded in a deliberately vague and hard-to-enforce sort of way and the DOF has still not decided what detailed logging requirements are appropriate and practical to include in a set of stricter conditions. Consequently a fair statement of existing de facto policy would be:

- (m) Tolerate damaging and unplanned logging practices in the interest of securing the benefits which flow to government and landowners from the operation. Exert whatever influence is practicable to discourage logging within 50 metres of actual flowing watercourses and on excessive slopes.

3 Marketing and pricing practices:

It is patently obvious, and has always been known to Governments, that the foreign companies which control the marketing of PNG logs as permit holders, contractors or log traders are blatantly ignoring the applicable marketing conditions. Letters of Credit are always and openly made out in favour of the foreign contractor even when the PNG permit holder is required to be the beneficiary of the letter of credit.

Operators have been allowed to sell at exactly Minimum Export Price even though that is known to be well below true market value.

Most PNG producers are selling to parent or related companies who are then reselling to the "true" buyers at a substantially higher price, with this price differential being retained out of PNG and not disclosed here.

Almost all foreign timber companies involved in logging and marketing have disclosed substantial losses for tax purposes and yet keep operating at a loss! The defacto policy should be stated as:

- (n) Be realistic as regards marketing and accept the inevitable that foreign companies will transfer a proportion of their profits off shore tax free and that it is difficult to detect and difficult to stop. Tolerate this practice in order to gain the benefits of export duty and royalty payments and a degree of foreign currency earnings. Accept the effect on the national economy of lost foreign currency earnings, lost revenue in the form of royalties income tax and export duty and the loss to landowner companies of their fair share of profits.

During the last two years there has been more government involvement in marketing in an endeavour to reduce the extent of transfer pricing. This has been attempted through exercise of the State Purchase Option and the activities of first FIC and now the DOF as State Marketing Agent. As a result the government has acquired more knowledge of the true market prices. Since the requirement to obtain an export licence (and an export permit) for each shipment was introduced the government also now has a stronger weapon to control market price by refusing to issue the licence if the shipment is underpriced.

Nevertheless, third country invoicing is still permitted, as are sales to parent and related companies and back to back letters of Credit. Companies which have been proved guilty of large scale transfer pricing before this Commission of Inquiry (and who are in all probability still doing it) have recently been granted new permits and approvals to operate as contractors for (defenceless) landowner companies. A recent variation to defacto policy should therefore be added:

- (o) Seek to reduce transfer pricing by involvement of government in the SMA and follow up proven breaches through rigid enforcement of taxation law by the Office of Taxation. Be prepared to accept that taxation assessments and penalties must be negotiated downwards to a realistic level which will allow the guilty company to keep operating and generating more revenue.

Foreign Investment

Because of the way foreign investment and foreign timber companies have been allowed to dominate the timber industry the defacto policy appears to be:

- (p) Encourage foreign investment in all aspects of the timber industry ensuring that royalties, export duty and import duties are paid in full. Tolerate a degree of transfer pricing as an inevitable consequence of this foreign involvement but seek to minimise it by competitive involvement in the market and the enforcement of the taxation laws. Strike a balance however so as not to stop production or frighten off foreign investors.
- (q) As far as is practicable in the circumstances, seek to persuade the foreign companies to provide a reasonable level of training and employment for PNG citizens but not to such an extent as will seriously interfere with the profitability of the foreign enterprise.

5 Resource Survey

My inquiries have disclosed so many instances where resource surveys were many years out of date (some dating back to the 1960s), were based on inadequate sampling and have been proved to be wildly inaccurate (by as much as one hundred percent) that I can put little or no value on the available data as a basis for the fine tuned planning required to estimate the value of a resource (as the basis for negotiations) or to work out the maximum cut which will permit sustainable yield forest management in any particular forest area.

Conducting accurate resource surveys is an expensive business requiring aerial survey and arduous ground patrols by skilled technical staff. This type of accurate survey is not being attempted.

The work being done is usually carried out, or sponsored or financed, by the foreign company seeking access to the resource and the results are heavily biased towards what that company wishes DOF to believe. Numerous examples are quoted in the interim reports where operations commenced with no knowledge of the resource (except that gained when the bulldozer was making snigging tracks) or where the resource data was completely wrong.

Knowing full well the inaccuracy and lack of resource data, the government has nevertheless been willing, in fact eager, to allocate the resource. It seems as if the defacto policy is almost:

- (x) If there is no resource knowledge about an area proposed for allocation then cut it down and find out.

Perhaps more attention would be paid to resource data if the forests were being allocated to companies investing in a long term integrated processing venture, as detailed knowledge of the available timbers would be required, and not just the volume but the major species as well. A company like SBLC most definitely would have acquired this information for itself before investing heavily in its proposed K75 million reforestation scheme.

It may well be different for pure log export operations and for such enterprises the defacto policy statement could probably be expressed;

- (s) For log exporting enterprises the policy is to accept fairly rough estimates of the extent and value of the resource as the enterprise will not involve heavy financial investment and if the resource cuts out sooner than anticipated the company can seek the allocation of another resource.

Such a trial and error policy would not be possible if sustainable yield forest management was truly the government's aim.

6 Onshore Processing

The disastrous decline in onshore processing shown above and discussed in detail in IR No 6 puts the lie to the 1974 Policy statement directing that all efforts would be made to increase the production and export of processed timber products. Since that date they have dropped off to almost nothing.

It is probably however still the defacto policy to:

- (t) Encourage large scale integrated onshore processing on permanent forest estates.

I say this because the government has persevered with SBLC and OBTC for many years. Failure to grant SBLC the firm legal base it requires and failure to enforce OBTC's long overdue permit conditions probably reflects inefficiency rather than lack of commitment to the concept. Failure to provide Jant with the required land for plantations and the required further resource however seems to indicate lack of commitment to that particular project.

The most recent trend is to require a fixed level of sawmilling to be carried out by log exporting companies to provide sawn timber for the domestic and overseas market. The way this is being required however ensures that the company will export its prime logs and saw only those rejected for export as defective .

This will result in a poor quality product and a wasteful sawmill as all defects will have to be cut out of the logs. In PNG such mills rarely have better than a 30 percent recovery ratio which means 70 percent of the saw logs are wasted. The government is not taking strenuous steps to insist on further processing to take up this level of waste (such as requiring construction of a medium density fibre board plant). For this reason an additional aspect of onshore processing defacto policy could be expressed:

- (u) *Encourage onshore sawmilling by log export enterprises for domestic and overseas markets but tolerate a second rate product and a high wastage rate.*

7. "Papua New Guinea Ways"

In 1974 there was a hope (perhaps an intention) that landowner groups would be enabled to benefit from timber operations using traditional forms of social organisation.

The fact that a few groups, who are involved in the timber industry in a minor way, are organised as registered business groups, rather than as more formal companies incorporated under the Companies Act, is about the only small step in this general direction. The landowner group in the current illegal Tabar operation which is acting as a "front" for Pacific Rim Pty Ltd is, for instance, a registered business group.

If there is any policy on the question of developing PNG forms of social and economic organisation I would say that the government would probably be opposed to it as a suitable vehicle for engaging in the timber industry in any sort of substantive way. A traditional group would be an acceptable basis for a grass cutting operation around VFP's compound for instance but no attempt has been made to recognise such groups as the entity to hold a permit or enter into a logging and marketing agreement.

8 Landowner benefits

There is a definite policy that landowners should receive benefits from the timber operation which is exploiting their own timber resource. It is not government policy however that they should receive the true value of the standing tree. Royalties are fixed at an absurdly low rate and landowners receive only a portion of that low amount (ranging from 25 to 75 percent).

Landowner companies stand to do better out of a deal if they are the permit holder or approved party to a LFA dealing. Government's performance in ensuring that the landowner companies are not cheated by foreign contractors has been poor and my inquiries have shown that time after time they have been signed up to very unfair agreements by

local lawyers acting for all parties and in acute conflict of interest situations. DOF has either approved those agreements, despite their unfairness, or refused approval but allowed the operation to commence anyway.

The defacto policy could be expressed:

- (v) Ensure that local landowners receive sufficient benefits to satisfy their low level of aspirations. Any benefits above that level which might be obtainable should flow to the national or provincial government on behalf of the people.

9 Decentralisation

This aspect was discussed in detail in the text above as regards functions, staff, consultation, powers and funds.

The overwhelming conclusion based on my inquiries is that:-

There is no effective policy or strategy which comes to grips with decentralisation. No policy expresses the way, or even the need, to find a proper balance between national and provincial legitimate interests in resource allocation, revenue collection, planning and supervisory and inspection functions.