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Resource Development in Papua New Guinea

Charles W Lepani, Papua New Guinea High Commissioner to Australia.

(Views expressed in this paper are those of the author and do not necessarily reflect the views of Government of PNG)

Chairman, Distinguished Captains of Industry and Friends,

I thank the organizers of this conference to showcase PNG's resource potential particularly in Oil and Gas sector.

My role this morning, is to outline some overall PNG policy framework to promote investment in resource development and to suggest some key concerns for noting, on issues of State ownership and financing of State equity, licensing for exploration and development of resources, and political risk issue.

The first issue I have been tasked to discuss is PNG's sovereignty and our bilateral relation with Australia.

In dispensing this issue, what remains for me to raise is the recent souring of relations when both our two governments were mortified by a fellow called Moti. Over the recent Asia Pacific Economic Cooperation (APEC) meeting, both our two Foreign Ministers have agreed to move forward with the Joint Ministerial Forum suspended on account of Moti Affair, for early next year.

I have said this before in another forum and I will keep saying it. PNG's greatest asset in Australia is the reservoir of goodwill amongst the Australian people for PNG despite the cooling off of relations between our two governments in the last twelve months. Indeed I cannot remember a time in the history of our bilateral relations, where there is such a disparity of goodwill between Australian people and their government when it comes to PNG. Increasing numbers of Kokoda track expeditions recently by Australians and our Canberra Mission's active engagement with Community Groups at Council levels, Rotary Clubs and Schools, continue to enhance this goodwill.

It has been a truism in the two decades after independence, to say that PNG and Australia have shared a unique relationship, underpinned by historical, geographic, economic and security ties. All these aspects of our

relationship are embodied in the Development Cooperation Treaty (DCT) of 1989 and later updated in 1999, and sub Treaties of the Defence Cooperation Treaty and Torres Strait Border Treaty. Australia's development assistance program in untied budget support form it was given in 70s and early 80s, has provided the substance for this uniqueness in the past. Changed modalities of providing aid from budget support to project tied aid and program-based aid over the last twenty years or so have seen greater control over, and involvement by Australia, in how its aid is distributed in PNG.

Over the last five years or so, very little reference is made of the "uniqueness" of our relationship at political circles at Waigani and Canberra. While it is not significant in general, it does, in my view, indicate the mood and the climate of change that is emerging between our two governments and how we respectively react and respond to these changes. The changes are well known but let me summarize them:

- The architecture of international, regional and national landscape, has changed from what it was 32 years ago when PNG gained its independence. Our respective policy and political responses to this change to promote our respective national and sovereign interests, will continue to determine the parameters and drivers for the future of our bilateral relations.
- Internationally, 9/11 has been a key factor in Australia's move to ensure some of its priorities in the development assistance it provides to PNG are respected and taken into account for its national security interest. It is the worst kept secret in Canberra, that Bush US administration had asked the Howard government to "take care" of its Pacific Islands neighbours to ensure terrorism, drug smuggling and money laundering do not enter the region and threaten Australia and US security interests.
- The approach Australia has adopted is an interventionist one of seeking regional cooperation with its Pacific Island neighbours under a Pacific Forum Agreement to intervene in Pacific neighbouring countries facing political turmoil. Such interventions include the Solomons riots, but in Tonga, New Zealand and Australia went on their own at the request of the Tongan government and with Fiji Australia attempted a veiled threat of intervention on the pretext of rescuing its citizens with an expeditionary force on stand-by in the waters of Fiji.
- In PNG, Australia's experience with Enhanced Cooperation Program (Policing Element) was short lived, on account of the Immunity issue for its AFP police operating in PNG. Again, there

is continued speculation on who initiated the ECP policing program. It is commonly agreed that the manner in which it was deployed could have been better handled. Even some sectors of Australian government, normally associated with Australia's foreign aid and foreign policy were largely left out of the program planning phases.

- From PNG perspective, the Supreme Court has ruled on the constitutionality of the immunity issue. PNG has now instituted its own review of the total ECP Program. At the minimum, ECP should be brought under the umbrella of the DCT.
- Australia has taken the step over the last five years in particular, to pay careful attention, to how its aid funding to PNG is being used. With this move comes the commensurate and necessary step for Australia to monitor and partake in policy decisions we make affecting our budget, and indeed our macro management policies in general. In early this year, the Development Cooperation Strategy negotiated and agreed to by the officials of our countries at Alotau, gives substance to this ever increasing engagement of Australia in our policy formulation processes and resource allocation.
- PNG has expressed its displeasure and at times made this known in no uncertain terms at Senior Officials level and at the Joint Ministerial Forum level that under the hubris of continued development aid and joint aid programming, Australia is unilaterally making decisions on aspects of its development assistance to PNG and on intruding into PNG's exclusive sovereign right to decide on policies for development and the resources allocated to support these policies.
- If recent pronouncements from Canberra are any indication of the future conduct of our bilateral ties particularly with respect to its development assistance to PNG, PNG should expect more of the same and not less.
- The perennial issue of governance continues to be on the radar screen and efforts by Treasury and Finance ECP contingent with their PNG colleagues in these agencies within PNG government are bringing a modicum of comfort for Canberra. There are other priorities for spending Australia's aid resources which fall in line with ours which include, health, education, infrastructure, law and justice and HIV/AIDS.
- In the past up to 85% of funding on priorities, was borne by the development assistance funding sources, most of which came from Australia's aid program. The last Somare government began the

process of reclaiming priority funding by increasing spending from around 20% on each of our priorities to 50%. While it did not attract much political attention, it is a very significant initiative symbolically, to begin the process of reclaiming our sovereignty and absolute right to determine our future in our policy decisions. PNG cannot say we are sovereign and economically independent when others pay for much of our development needs.

On resource development policies, let me state at the outset that PNG has a well developed and balanced framework of policies based on past experience with some quite adventurous and brave initial benchmark fiscal regimes in mining sector in particular. I refer here to the capital gains tax in the renegotiation of Bougainville Copper Agreement, the Ok Tedi talks which allowed for an amicable exit of Kennekot the lessons of which are current and have become more relevant for PNG today than ever before in the case of commercializing our Gas resource.

The Bougainville mine itself has left an indelible mark on PNG's track record of policy successes and failures. Policy and legislative successes in recognizing the sovereignty of PNG to own resources for the nation's development, to develop major resource projects for revenue generation only with no employment creation and local value adding as objectives.

The failures lie in not recognizing that how you distribute this wealth and who gets this wealth is just as crucial in the Bougainville case and indeed is as relevant a policy legacy today as it was then when the first explosion to sabotage the mine infrastructure was set off. We all know now in hindsight how a complacent government of the day to attend to renegotiating the Mine Agreement was one of the immediate precipitating underlying causes for the failures, and how royalties paid to leaders of landowners without concurrent arrangements to take account of share for future generations of landowner did contribute to the failure, and how concerns by landowners for environment degradation were taken with a grain of salt also added salt to the festering wound.

All these landowner generated issues have contributed to a very robust policy today for recognizing the unique role landownership or strictly speaking, land custodianship plays in mineral and oil gas resource developments in PNG. In many ways it is a unique policy that state can devolve its sovereign power and authority to a part of its whole. This policy outcome gives rise to the perceived problem of having a third party to the negotiating table, the investor would prefer to deal on a one stop shop basis, with the State only on licencing, equity, and fiscal regime.

The Development Forum approach to dealing with landowner issues has been supplemented by the existence of Mineral Resources Group of Companies (MRDC) as manager of State and landowner equity interests fairly and squarely puts the landowners of any resource project on an almost equal footing with the State and sits them on the table as equal partners to other stakeholders in negotiations. The separation in landowner interest from the State and maturity in landowner role and participation is recognized by government of PNG recently when it set up its own resource management company in Petromin leaving MRDC to manage landowner mining, petroleum and gas interests.

There may be an opportunity here for State to review its fiscal regime on equity participation or move to production sharing. In light of its key concern for public reducing debt a possible move to production sharing may address this fiscal issue of concern. Equity participation has been advocated and continues to exist not only for national participation and ownership policy but also some investors have actively sought government participation by equity for sovereign risk concerns. Government needs to weigh these competing public policy issues in light of fiscal imperatives and risks and liabilities to public balance sheet.

While on issues of sovereign risk, it is not for me to question the gurus and market analysts and investment bankers of their wisdom on this matter. However, may I say this that it still befuddles me for PNG risk been worse than some West African, Asian and East European economies and political risks are rated better than PNG's. It reminds me of piranhas swimming in the river and with appetite for and eating these risks floating by from everywhere in the world except when they come across PNG risks, Oops! Sorry, not today thank you!!

Most of you know the developments taking place in Asia Pacific Economic Cooperation (APEC). At this year's APEC Finance Ministers' Meeting at Coolumb, Queensland, the deepening and expansion of capital markets in APEC economies was a very significant issue discussed and US has offered its expertise in this area to provide Technical Assistance to move issue forward. PNG is a member of APEC and while its capital is insignificant compared to the larger economies, there are areas where real and concrete steps can be taken with International Financial Institutions (IFIs) and donors with private sector to set up facilities to initiate financing and capital markets for smaller economies in the region.

Last but not the least, I want to discuss the more vexing question of investors sitting on proven resources for too long without moving either

to develop them or relinquishing them back to the State so it can seek other interested parties to develop the resources. I know too well the commercial imperatives of large resource projects. But while \$US 6 billion may seem small to some large partners whose Market Cap sits at \$US340 billion, for PNG it is a project of national importance. Moving milestones with concurrent project scaling up from a humble pipeline to Townsville, then extending it to Gladstone then to Moomba where it met its Waterloo, to link with an ambitious national grid of distribution begs the question? Do the producers know what they are doing or are they taking PNG for a run up the garden path? Having come to a dead end on PNG-Australia Gas Pipeline Project, can the same investor's be trusted to again do the right thing commercially for PNG?

I leave you to ponder these issues seriously.

Thank you.