



# ISSUES PAPER

March 2014

Issues Paper # 07

**Prof. Satish Chand** is Professor of Finance, University of New South Wales at Canberra, Australian Defense Academy.

S.Chand@adfa.edu.au

**Dr. Justin Ondopa** is Senior Research Fellow, Property Sector Development Research and Project Program at the National Research Institute.

jondopa@nri.org.pg

**Ms. Logea Nao** is currently studying at the Australian National University.

Inguba12@gmail.com

## Use of Land Leases as Collateral for Accessing Formal Sector Finance in Papua New Guinea<sup>1</sup>

### Abstract

The 97 percent of the total land area of Papua New Guinea (PNG) is under customary title. This land cannot be used as collateral to access finance from banks and the rest of the commercial sector.

This paper presents strategies to make leases granted on land that is held under customary title to be bankable. A key challenge in making leases to become bankable is to ensure the authenticity of leases granted by the Department of Lands and Physical Planning (DLPP).

Ten specific recommendations are made to make land leases bankable.

**The National Research Institute**  
P. O. Box 5854 Boroko, NCD  
Papua New Guinea  
Tel: (675) 326 0061  
Fax: (675) 326 0213  
Email: [nri@nri.org.pg](mailto:nri@nri.org.pg)

Website: [www.nri.org.pg](http://www.nri.org.pg)

<sup>1</sup>This research has been co-sponsored by the National Research Institute and the PNG Commercial Bankers Association. We are grateful to the individuals named in Table A1 who assisted in providing the data for this research. Views expressed in this paper and errors in it are those of the authors only. This paper does not constitute either legal or financial advice.



**1. Introduction**

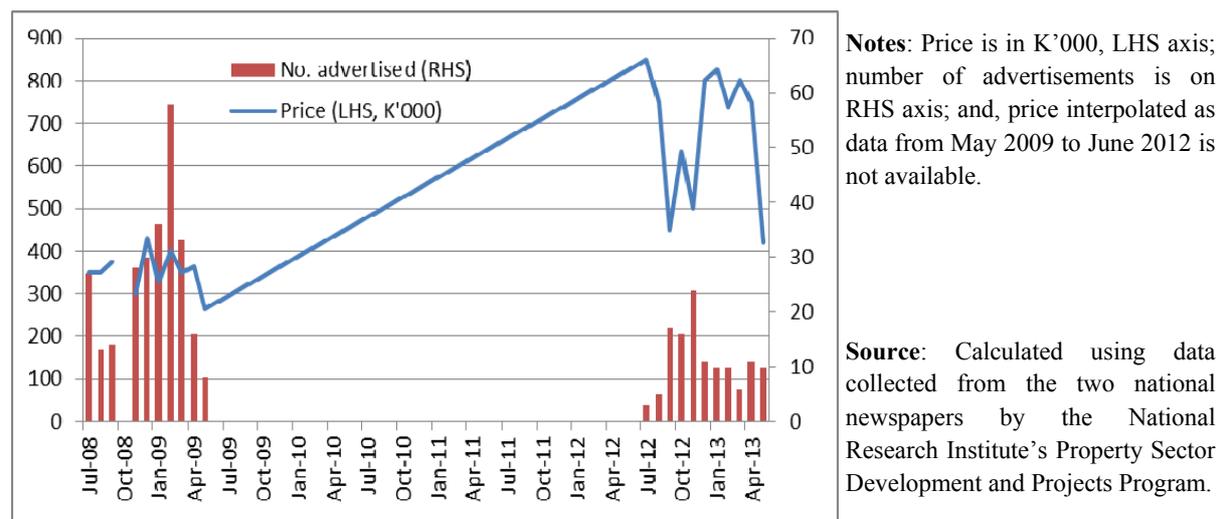
Land held under customary title in Papua New Guinea is not bankable. In other words, customary-owned land, comprising a total of 97 percent of the total land area of some 462,840 km<sup>2</sup>, cannot be used as collateral to access finance from commercial banks. This land, in the words of De Soto, is ‘dead capital’ (De Soto, 2000). The lack of a secure title, according to De Soto, impedes access to formal finance by the poor and this in turn lowers the level of investment and the rate of growth in income. Several scholars have argued that secure rights to property can raise the levels of investment through several channels, all of which then leads to growth in income (Besley, 1995).

Land titling provides a mechanism for availing security of the rights to real (i.e. immovable) property. This is necessary, albeit not sufficient, to allow the titled property to be used as collateral to secure investment finance from the formal sector (Christensen, *et al.*, 2006). The title on its own, however, is insufficient to access credit since lenders, and commercial banks particularly, will not risk depositors’ funds unless and until they are certain of a return. Thus legally-defined title together with efficient enforcement mechanisms is critical to reducing the risk of property lending by the commercial sector. Such risks are a large component of the transactions costs for lenders.

Enforcement of property rights requires that these rights are collectively respected and publicly protected. Only then will transaction costs between the borrower and the lender be low enough to permit widespread financial intermediation for the real estate industry (Feder, 1985). The bulk of property lending in PNG is confined to the urban sectors (comprising the provincial centres and towns) and to those individuals and corporations who have a secure title and a demonstrated record of the capacity to service a loan. Clearly, the above comprises a small minority of the population.

The vast majority of the population live on land held under customary title. For many households, this is the only asset they have. Thus, access to land on a long-term and secure basis accompanied with access to credit from the formal sector has the potential to boost building of houses around the major urban centres. The National Capital District (NCD) is a glaring example of the above: house prices and rental rates have been rising rapidly over the past several years together with growth of squatter settlements (Chand and Yala, 2012). Figure 1 illustrates median prices of residences in Gerehu, a suburb of the NCD with majority owner-occupied residences, more than doubled between 2008 and 2013.<sup>2</sup>

**Figure 1: Median house prices and number advertised, Gerehu**



<sup>2</sup> Figure 1 shows that advertised nominal house prices in Gerehu increased by 236 percent between July 2008 and January 2013, and have since been trending down. The number of advertisements in the two national newspapers for house sales in Gerehu peaked at 58 in February, 2009.

The inability to use land held under customary title to expand the supply of real estate and the inability to access credit using the land as collateral has impeded expansion of the formal real estate sector on vacant land within the peripheries of the major cities and urban centres of PNG. Similarly, the Small and Medium Enterprises (SMEs) have complained about the problems in using land as collateral to access finance from the commercial banks.<sup>3</sup>

Locally led and domestically crafted land reforms that are underway in PNG were designed to provide secure and long-term leases to land held under customary title such that the above could encourage investment and growth of income. These reforms build on the foundations of long-standing informal systems to provide land owned by traditional clan groups for private enterprise on a long and secure terms through the formal systems (Yala, 2010). Crucially, the landowning groups (clans) have the option of using two newly enacted legislations to consensually avail their customary-owned land for development on long and secure terms.

These reforms were designed to deliver benefits to the landowner, the investor, and the public more generally. The landowners earn income by availing their vacant land for development on a long-term and secure basis. The investors benefit from having their latent demand for land being satisfied. Spin-off activity in construction, hardware, and other ancillary services boost employment and economic activity as a whole. The public gains from increased investment and the associated growth in income. By being a strictly positive sum game for each of the stakeholders, the risks of land conflict from the reforms are minimised (Deininger and Castagnini, 2006).<sup>4</sup>

An objective of the reform is to make land held under customary title bankable. If successful, the reform underway has the potential to make a significant contribution to development. However, international evidence of land reforms being successful in facilitating access to finance from the formal sector is mixed at best (Kerekes and Williamson, 2010; Schargrodsky and Galiani, 2010). Could the land reforms underway in PNG be any different? We hope so!

Two new laws; namely the *Land Groups Incorporation (Amendment) Act 2000*, and the *Land Registration (Amendment) Act 2009*, were gazetted on 20 February 2012, and came into operation from 1 March 2012.<sup>5</sup> The *Land Groups Incorporation (Amendment) Act 2009* provides the legislative framework for customary land owners to incorporate as legal entities and then register their land with a view to leasing the unused portions, following proper cadastral mapping, to the private sector. The land thus availed can be leased through the *Land Registration (Amendment) Act 2009* for a term of up to 99 years. The latter of the above-mentioned statutes allows mortgages to be created and used as security (paragraph 62), permitting transfer of mortgage (paragraph 66), and sale of property by the mortgagee (paragraph 68) on default (as defined in paragraph 67). Furthermore, Section 74 allows the mortgagee to enter and take possession of land following default in payment of any secured credit by the mortgagor.

The law does not allow land held under customary title be used as collateral.<sup>6</sup> Even if it did (which incidentally is not argued here), they will not on their own be sufficient to make the land to become bankable. The task for this paper is to provide reasons why customary-owned land cannot be used as collateral, and what could be done to make this land 'bankable'. The latter is important in light of the fact that the Government of PNG (GoPNG) has espoused a policy of expanding supply of real estate.

<sup>3</sup> See an article titled, 'Land-for-business woes', on page 36 of *The National* dated 26 September 2013.

<sup>4</sup> Proposed land reforms in the lead up to the national elections of 2002 witnessed large street protests in Port Moresby that was fermented by 'political entrepreneurs' and which led to the fatal shooting of four UPNG students.

<sup>5</sup> Published as *Papua New Guinea National Gazette* No. G64, Government Printer, Port Moresby.

<sup>6</sup> Section 19(c) of the *Land Registration (Amendment) Act 2009* prohibits "transfer of allodial title in clan land". See also Section 98 of the *Land Registration Act 1981* and Section 19 of the *Land Group Incorporation Act 1974*.

The review of housing and real estate industry in 2010 by the Independent Consumer and Competition Commission makes the following recommendations:

- (i) “freeing up the supply of State land; and encouraging the ‘bringing to market’ of customary land; to address scarcity of ‘raw’ land wherever it exists; and,
- (ii) improving title registration, record-keeping and title transfer procedures to ensure the security of land as collateral” (ICCC, 2010:p.7 – emphasis added).

The question addressed in this paper is as to whether the leases, rather than the underlying land title, can be collateralised so as to access finance from the commercial sector. Data was collected through a semi-structured interview, ethics clearance for which was secured from The National Research Institute and The University of New South Wales. The goals of this research were to: (a) document the extant practice of property lending by the commercial banks; (b) identify constraints to and challenges of using land leases as collateral; and, (c) propose policy options to facilitate access to finance by lessees.

The key findings from this research can be summarised as follows: Land held under customary title remains ‘dead capital’; that is, it is not being used as collateral to raise finance from the formal sector. Three reasons were given for the above. First, the lenders were not conversant with the new laws. Second, there is a thin secondary market in land leases thus making leases illiquid. Finally, insecurity over the property rights to leases is a major hurdle to commercial property lending. Disputes over ownership rights, presence of duplicate titles to the same piece of land, weak capacity to enforce contracts, and restrictions on transferability of leases impede lending by commercial banks to the bulk of the population.

Compounding the above problems are deficiencies in land administration (mal-administration) including issue of dubious titles to competing parties, exercise of ministerial discretion in issuing leases on State land that have subsequently been rescinded by the courts, and large losses incurred by lenders that have severely curtailed lending for real estate development as a whole. The World Bank’s ‘Ease of Doing Business’ ranks PNG 104 of a total of 185 countries, but the sub-ranks in terms of ‘Resolving insolvency’ and ‘Enforcing contracts’ are 125, and 166 respectively (data for 2013). Banks report extreme difficulties in foreclosing on a loan securitised with a land lease. The cost of extending credit in PNG, consequently, is high.

The rest of the paper is structured as follows: Section 2 describes the methodology and provides the findings, Section 3 presents the recommendations, and Conclusion brings the paper to a close.

## **2. Research methodology and findings**

This section provides a summary of the methodology employed for data collection and the key findings. The latter is further sub-divided into 2 sections; the first dealing with the bankability of State leases and the problems with the above. The second considers bankability, or the lack thereof, of leases held on land under customary title.

Data on bankability of land leases was collected in the last week of August 2013 via a semi-structured survey from the formal financial sector comprising the three commercial banks (i.e. ANZ, BSP, and Westpac), Credit Corporation, and Kina Finance Corporation. Discussions were also held with officials from the Department of Treasury and Brian Aldrich of AKT Associates. The questionnaire used and the individuals consulted is provided as Appendix A1 and A2.

Properties with freehold and leasehold title within the National Capital District, Lae, Mt Hagen, and Kokopo are used as collateral to extend credit by all three commercial banks. Leases are generally preferred to freehold title as non-citizens are allowed to hold the former but not freehold title (see Section 54(c) of the *Constitution of the Independent State of Papua New Guinea*).

Table 1 provides a summary of the conditions for accessing finance from the five formal sector providers of credit. There is little divergence in the process of obtaining loan finance, and the terms on which such credit is provided differs little between the credit providers. The process used in extending credit by the two foreign banks is identical to that used by their parents in Australia. The loan term ranges from 7 years (for Credit Corporation) to 25 years (for ANZ Banking Corporation); equity of 20 percent is required with the exception for Credit Corporation where loans of up to the full value of the property may be accessed for a highly credible client; interest rates are largely product driven, and as of August 2013 ranged from 7.75 percent (special housing loan from Kina Finance) to 11.71 percent (indicator lending rate for Westpac Banking Corporation) per annum; serviceability threshold of a ceiling of 35 percent of salary (ANZ Banking Corporation); and, clear title to the collateral is essential albeit not sufficient for accessing credit.

**Table 1: Summary of Loan Conditions**

Institution	Term of loan	Determinant for value of loan	Interest rate	Collateral required
BSP	Commercial – 15 years (preferred 10 years) Residential – 25 years & borrower <60 years of age	Credit security process	Product-driven	1. Genuine title 2. Financial capability/ Ability to service the loan 3. Risk analysis – property value, equity, and borrower credit history.
WESTPAC	15 years maximum	Credit security process	Indicator Lending Rate is 11.71% (-2) Private Corporate Rate is 8.25% (+1)	1. 20% equity 2. Valuation 3. Genuine title 4. Financial capability/ Ability to service 5. Risk analysis
CREDIT CORPORATION	7-10 years (absolute maximum of 10 years)	Credit security process: 70-30%; 80-20%; 100%	Indicator Lending Rate is 12.5%, margin (+-1)	1. Character check/ Relationship 2. Financial capability/ Ability to service 3. Genuine title 4. Property valuation
ANZ	25 years	Credit security process: 80% of property value; less than 35% of the applicant's salary	9-9.5% (market rate)	1. Financial capability/ Ability to service 2. Genuine title 3. Risk analysis
KINA FINANCE	Maximum term of 20 years (average of 10 years)	Client-need, ultimately through credit security process	7.75% (special housing loan)	1. Financial capability/ Ability to service 2. Assessment of security 3. Genuine title 4. Risk analysis (including ability for Kina Finance to repossess collateral)

**Source:** Authors' compilation from survey data.

The capacity to service the loan and the adequacy of collateral in securing the loan is considered paramount by the formal sector lenders. On serviceability, the banks use credit history of their clients in judging the capacity to repay the loan thus minimising the need to repossess collateral. All credit providers emphasised the fact that they were conservative in making judgements on serviceability, but the larger risk was with being able to exercise their rights of repossessing and selling the collateral in the event of default on repayments. The largest risks were in terms of establishing genuineness of the title to the collateral.

Establishing the authenticity of any given title was extremely problematic given the widespread cases of fraud. The cases of duplicate titles for a given piece of land were pointed out as being common practice. It

was also pointed out that encumbrances on a given title were erased within the National Department of Lands and Physical Planning (DLPP), in clear breach of law. Lenders discovered titles to be bogus only when executing mortgagee sale. The above practices devalue titles, raise the risk of any transactions in immovable property, and raise the cost of extending credit in PNG as a whole.

The legislated process in issuing leases and their transfers for State-land as mandated under the *Land Act 1996* are given in the form of a flow chart (see Figure 2). The application for a title involves lodging an application to the DLPP on a prescribed form (see Appendix 3), together with the mandated fee of between K10 for a Special Agricultural Business Lease (SABL) to K500 for an Urban Development Lease (UDL). Illegal facilitation fee paid to DLPP staff are reported to range from a couple of thousand Kina to a case where K100,000 was reported as being paid for a lease over land at Jacksons Airport. While the process that is followed within the Department is opaque, we were told that the lodged application is screened for authenticity following which clearance from other departments on the use of the land under application is sought. The collected information is then handed over to the Land Board for a decision, and in ‘exceptional circumstances’ to the Minister for Lands and Physical Planning for a decision instead.<sup>7</sup>

All credit providers complained of the long delays in getting the necessary searches and transfers of titles through the DLPP; each pointed out that these delays were due to a combination of deliberate action to stop the transaction and incompetence on the part of the staff in the Department; and, one pointed to a ‘completely dysfunctional DLPP’. One credit-provider informed that payment of K1,000 was demanded to locate the right file, which otherwise was locked in a room of files with the key held by a staff member who was away and ‘very sick’. The case of one transaction that involved the transfer of a lease by the DLPP reportedly took seven years! Executing mortgagee sales following court orders were equally problematic as the Police seldom assisted in evicting occupants of the property and the threat of violence was omnipresent during such evictions. Lending in the Highlands provinces, for example, took into account the limited capacity to repossess collateral in the event of a default in repayments on the loan.

On being asked as to how the credit providers circumvent the problems within DLPP, one informed of the use of ‘wantoks’ while another had outsourced the process of transferring leases to a law firm that charged a fee, depending on the complexity of the case, in the vicinity of K7,000 (approximately A\$3,000) per transaction. Settlements, we were informed, took anything between six to 18 months. The above are in stark contrast to the norms in Australia where law firms charge, again depending on the complexity of the transaction, approximately A\$1000 and property settlement takes place within a month of initiation.

*Leases on customary land are not used as collateral*

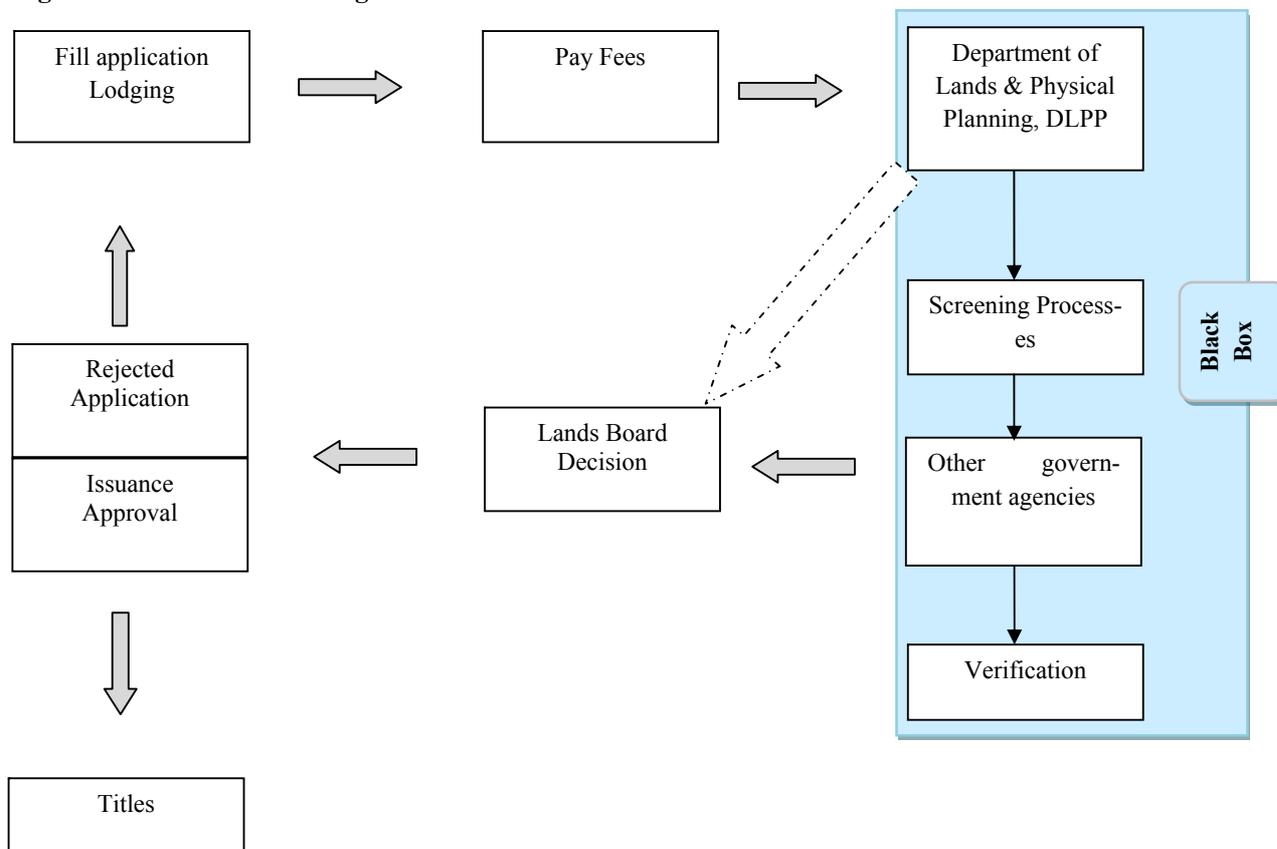
The issues raised above relate to alienated land and those under State lease. The supply of such land within the vicinity of the major urban centres has been exhausted. While physical space within the urban fringe is available, every credit provider pointed out that they did not accept land under customary title as collateral. The lone exception was a case where a loan was provided on a *Special Agricultural Business Lease* (SABL) as collateral. The lender subsequently got ‘burnt’, thus was no longer active in this market.<sup>8</sup> The above-mentioned case is common knowledge amongst credit providers who shun the use of leases on land under customary title as collateral. Consequently, a large fraction of the population is denied access to credit from the formal sector. There was, according to one senior bank staff interviewed, room for increased lending to owner occupied homes brought to the market at affordable prices to serve the nationals (in contrast to the expatriate population where demand had reached a plateau). The bank, according to this

<sup>7</sup> What constitutes an exception so as to allow for Ministerial discretion is not stipulated.

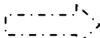
<sup>8</sup> The details of this transaction have been withheld as doing so will reveal the identity of the credit provider.

informant, “would be eager to grow their markets in this segment if land with secured tenures and legal titles for ownership were made available as collateral for acquisition funding”.

**Figure 2: Process of obtaining a title over a State-lease**



**Legend**

-  - Legislated steps in obtaining property title.
-  - Reported process within DLPP.
-  - The DLPP is termed a ‘black box’ as the process of issuing titles is less than fully transparent.
-  - Denotes that the processes are less than fully transparent to an outsider.

**Source: Authors’ compilation from information collected via interviews of stakeholders.**

The case of a bank staff, relayed to us by his manager, brings home the problems of accessing finance for the majority of the population who live on ‘their’ land. The staff member, a senior and long-term employee of the bank, requires credit to improve his dwellings. His bank (and employer) wants to lend for two specific reasons: first, the borrower (who is known to the bank) has the capacity to service the loan; and, second, it would be the ‘right thing to do by the employee’. The loan, we were told, could not be extended because the employee did not have adequate collateral. The staff member has built his home on land belonging to his clan. While a landowner himself, the land is not bankable. It is dead capital.

While it is impractical to use land under customary title as collateral, could the 99-year leases on such land be used instead? Clearly not yet!<sup>9</sup> Data collected via the survey revealed that the formal-sector providers of credit were not fully cognisant on the recent land reforms that allowed registration and leasing of land under customary title on long-term and secure basis. Even if they were, one informant pointed out that they would lend only if a secondary market in these leases developed to the stage where the lender could be confident that mortgagee sales could be possible. Thus, the potential for use of land leases as collateral are minimal unless a large and liquid market in land leases takes hold. Such an eventuality, even in the best of circumstances, will take time.

There is, as Justice Gibbs Salika notes in his judgement of 28 September 2013 on a land dispute, “a general lack of understanding of our people when entering into arrangements to purchase land from the State, traditional landowners and also from registered owners of property” (WS 664, 2012; paragraph 4 on page 4). The Judge reported that the first defendant sold a portion of land worth K45,000 to the plaintiff without having a proper title to the land. The above case illustrates the problems in the use of titles as evidence of the rights to property and the associated risks in using land title as collateral for extending credit.<sup>10</sup>

#### *Problems of valuing property*

Use of property as collateral to extend credit demands accurate valuations. This has proved problematic due to the lack of qualified valuers and the absence of data on property prices to help with valuations. Thus, lenders have taken a conservative approach to valuing real estate. The infancy of the real estate sector and absence of sales data on the transactions that do take place has placed hurdles in valuing property.

### **3. Recommendations**

- i. Establish a committee comprising representatives from the formal sector lenders, landowning clans within the NCD, Bank of PNG, DLPP including the Office of the Valuer General, and The Treasury under the National Land Development Program (NLDP) to explore means of making land leases bankable.
- ii. Workshops to be held to inform the formal sector credit providers and the PNG Real Estate Industry Association of the new legislations permitting leasing of land held under customary title on 99-year leases for building of real estate.
- iii. Data on prices at which properties are exchanged from the Office of the Valuer General and rental rates to be collected and placed on an electronic database that is readily accessible to the public on an ongoing and real-time basis.<sup>11</sup> Such information will facilitate better valuations of property and greater transparency in the broad trends in the real estate sector.<sup>12</sup>
- iv. Consideration to be given to funding and formalising the property price and rental rate tracking system established by the National Housing Policy Implementation Taskforce (NHPIT). Data on prices and rental rates by size, type, and suburb of property to be publicly made available on the website as is currently done by ‘*Allhomes.com.au*’ in Australia.<sup>13</sup>
- v. Benchmarks on time and Kina cost of registering and transferring property to be set and monitored on a half-annual basis. The benchmarks could include the settlement period and legal costs of property settlement. The prevailing Australian norms could be used as a guide for these benchmarks.

<sup>9</sup> Residential land leases in Fiji are sold through newspaper advertisements each weekend. As an example, *The Fiji Times* of 14 September 2013 advertised “Vacant residential Lot for sale 99-year residential lease within Lautoka city boundary area 801m2” at: <http://classifieds.fijitimes.com/ad.aspx?aid=316809>.

<sup>10</sup> The case was reported on page 5 of *The National* of 30 September 2013 in an article titled ‘Salika: Have title to land’.

<sup>11</sup> Poland successfully introduced a new caseload management system for the land and mortgage registries and digitised the records of the registries (see World-Bank 2012. *Doing business 2013: smarter regulations for small and medium-size enterprises*, World Bank Publications.)

<sup>12</sup> The NRI had collected monthly data on prices and rental rates for advertised properties in the two national newspapers from August 2011 to January 2012 (see Nao and Ain, 2012. “Information paper for the NHPIT”); this could be continued into the indefinite future with dedicated resources for the above.

<sup>13</sup> An example can be seen at: <http://www.allhomes.com.au/ah/other/sale-residential/advanced-search/view>

- vi. The Land Registry within DLPP to be charged with the sole responsibility of: (a) providing online and real-time searches of titles; (b) registering leases and titles; and, (c) being responsible for issuing all titles and leases. Existing legislation provides for the above-enumerated. Part III, Division 1 of *The Land Groups Incorporation (Amendment) Act 2009* stipulates procedure for preparation and issue of certificates of title, including the maximum penalty of K2,000 for unauthorised removal of a certificate of title from the custody of the Registrar. Paragraph 11 of the above-mentioned legislation states that the certificate of title, when duly registered, “is conclusive evidence, in relation to the land it describes, that the person named in the certificate of title (i) as seized of an estate in land; or (ii) as taking or otherwise entitled to an estate or interest in the land”; and, Section 125 states transmission of title by custom.<sup>14</sup>
- vii. Consideration be given to raising fee for registration and transfer of leases so as to reflect the actual costs incurred by DLPP in undertaking these assignments.
- viii. Consideration may be given to indexing leases and titles by geography and debtors name with both of the above made accessible online and in real time.<sup>15</sup>
- ix. Serious consideration be given to making titles and leases issued by the Lands Registry indefeasible; that is, the right in the property are protected from being annulled due to error or omission from the DLPP.<sup>16</sup>
- x. Consideration be given to raising the maximum penalty for breach of processes within DLPP. Staff of the NLDP-Registry could be made criminally liable for issuing duff titles and duplicate leases so as to protect the State from abuse within the DLPP. Systems would have to be designed to ensure that these rules are strictly enforced.

Further research may be necessary to implement recommendations (vi), (vii), and (viii). The above will entail a detailed investigation into the existing process within DLPP pertaining to issuing of (multiple) leases with a view to remedying the failures. The last two of the 10 recommendations enumerated above would be the most difficult to implement but equally the most important if land leases were to be made bankable. A title or lease to a piece of land is worthless unless the rights to the asset are enforceable. Dubious leases and dodgy land titles are as valuable as counterfeit currencies, and using dubious titles would be akin to using counterfeit currency that is indistinguishable from the genuine ones to purchase goods and services. The difference between counterfeit currencies and dubious titles in circulation in PNG is that the latter is issued by the legitimate authority; that is, the Lands Registry within DLPP. It is hard to imagine BPNG issuing counterfeit Kina, so why the same is possible in another agency of the State is puzzling to say the least. The dubious titles issued by the Lands Registry are in appearance identical to the genuine titles, thus distinguishing between the two is simply impossible. These duplicate titles create uncertainty on the authenticity of any title deed, raising the risks of using any title as collateral. Given the above, we are not surprised that banks take a highly conservative approach to using land titles as collateral. And the costs incurred in authenticating a title is borne both by the lender and the borrower.

The critical question is as to *how to stop the production of dubious titles*. The solution, at least on paper, is simple. The Lands Registry in the DLPP has a monopoly on the issue of land titles. This is no different to the BPNG having a monopoly on issuing Kina. Thus, incentives need to be created within the Lands Registry to ensure that dubious titles are not issued. Recommendation (x) enumerated make it a criminal

<sup>14</sup> Note that the *Land Act 1996* stipulates the process to be followed in obtaining leases on State land; the Secretary for DLPP has the sole authority to execute State Leases (Section 72(2)) with the Registrar of Titles and the Lessee being the only persons allowed to hold a copy each of the registered certificates (see Sections 8 and 9 of the *Land Registration Act*).

<sup>15</sup> This Registry will be similar to that created by the ‘*Personal Property Security Act 2011*’ to: “make provision for the creation, attachment, perfection, prioritisation, and enforcement of security interests in certain property, and to provide for related transactions and other interests necessary to give notice of the status of property to buyers and prospective creditors”. Interests in ‘real property’, including land leases, are excluded from the Act (Section 11(c)). Section 76 of this Act establishes a ‘Personal Security Registry’ to: “receive, index, store and retrieve notices delivered by secured parties and execution creditors” (Section 76(1a)).

<sup>16</sup> The Constitutional Law Reform Commission (2007) notes indefeasibility of duly registered customary land (see page 38 of the report).

offence to issue dubious titles; a penalty no different to what a staff member of BPNG would incur if he/she issued Kina without authority.

#### 4. Conclusion

The bulk of the land in PNG is not bankable. This includes the 97 percent of the total land area that is held under customary title plus alienated land and those under State leases which are located outside of the four major urban centres of Port Moresby, Lae, Mount Hagen, and Kokopo. The three commercial banks, and their formal sector counterparts, take a conservative stance towards extending depositors funds to borrowers who use title to land as collateral. Such a stance is necessary in maintaining the trust of depositors in their banks.

The key considerations in extending credit from the formal sector are: (i) serviceability of the loan; (ii) genuineness of the title; and, (iii) risk of default. Credit providers repossess collateral as the last resort to recovering their loans, and weigh out the risks entailed upfront at the processing stage of the loan in reselling repossessed properties in a context where markets may be illiquid and enforcement of the rights to an immovable property weak. Property lending in PNG has high risks thus the portfolio of loans is restricted to secure clients and around regions where the banks have physical presence. Increasing access to bank finance, thus requires reductions in these risks.

Ten specific recommendations have been made to making land leases/titles bankable. Commercial banks accept land titles and leases as collateral, but these are currently restricted to State and freehold land within the major urban centres and to trusted clients. Land under customary title cannot be used as collateral. While the recent reforms allow issuing of 99-year leases on land held under customary title, the leases are not as yet bankable. The reasons for the above include a lack of awareness of the recent land reforms that permit granting of such leases, the absence of a mature secondary market in leases, and the severe problems of establishing authenticity of these leases.

A major risk to use of title to real property as collateral is establishing the authenticity of the title. The circulation of dubious titles that is indistinguishable from their genuine counterpart makes land titles as a whole of minimal value.<sup>17</sup> The above is akin to having counterfeit Kina circulating in the economy that is indistinguishable from the real currency. Such an eventuality would freeze all trade in Kina. Land titles are worth thousands of Kina, thus the risks of being duped with a dud title is a lot greater than holding a counterfeit currency of the highest denomination. It is thus remarkable that any lending on land titles takes place given the circulation of dubious certificates.

Finally, the challenge of making land leases bankable is daunting. In the case of land under customary title, which is completely un-bankable now, the land owning clans respecting the rights of the lessee and the State underwriting the claim to these rights is critical to making such leases bankable. Progress on this front is likely to be in tiny steps. Thus, any incremental progress made in making the most valuable of the land leases bankable has the potential to deepen the mortgage market, induce greater supply of housing, and have a healthy spill-over effect onto the rest of the economy.

---

<sup>17</sup>One informed commentator has dubbed these ‘bullshit’ titles; their monetary worth is aptly described in the assigned label.

**Reference**

- Besley, T., 1995. 'Property-Rights and Investment Incentives — Theory and Evidence from Ghana', *Journal of Political Economy*, **103**:903–937.
- Chand, S. & Yala, C., 2012. 'Institutions for improving access to land for settler-housing: Evidence from Papua New Guinea', *Land Use Policy*, **29**:143–153.
- Christensen, J., Pattillo, C. & Gulde, A.M., 2006. Bankable Assets: Africa faces many obstacles in developing financial systems. Available: <https://openknowledge.worldbank.org/handle/10986/9601> [Accessed 5 September 2013].
- De Soto, H., 2000. **Mystery of capital: why capitalism triumphs in the West and fails everywhere else**. New York, USA: Basic books.
- Deininger, K. & Castagnini, R. 2006. 'Incidence and impact of land conflict in Uganda', *Journal of Economic Behavior & Organization*, **60**:321–345.
- Feder, G., 1985. The relation between farm size and farm productivity: The role of family labor, supervision and credit constraints, *Journal of Development Economics*, **18**:297–313.
- Independent Consumer and Competition Commission (ICCC), 2010. PNG housing and real estate industry review, Port Moresby.
- Kerekes, C.B. & Williamson, C.R., 2010. 'Propertyless in Peru, Even with a Government Land Title', *American Journal of Economics and Sociology*, **69**:1011–1033.
- Schargrodsky, E. & Galiani, S., 2010. 'Property rights for the poor: Effects of land titling', *Journal of Public Economics*, **94**:700–729.
- World-Bank, 2013. **Doing business 2013: smarter regulations for small and medium-size enterprises**. Washington DC.: World Bank Publications.
- Yala, C., 2010. **The Genesis of the Papua New Guinea Land Reform Program**. Port Moresby: The National Research Institute.

**Appendix A1: Questions to the commercial banks****SECTION 1: NUMBER AND VALUE OF MORTGAGES HELD**

Do you provide mortgage finance? If so, then proceed to the next questions.

How many mortgages do you currently hold?

What is the average size of these mortgages?

What is the geographic distribution (Port Moresby, Lae, rural PNG, urban PNG, etc) of these mortgages?

**SECTION 2: PROCESS OF OBTAINING MORTGAGE FINANCE**

Please briefly describe the process of obtaining mortgage finance.

What are the decision criteria for approving a loan?

How is the value of the loan determined?

How is the repayment period determined?

How is the interest rate to be charged determined?

**SECTION 3: REGULATION AND POLICIES**

What are the internal policies of your institution affecting mortgage lending?

What are the external policies affecting mortgage lending?

What are the (internal and external) impediments to growth of mortgage lending?

What could be done to grow the mortgage market in PNG?

**SECTION 4: LAND REFORM**

Are you aware of land reforms being undertaken in PNG? If yes then proceed to the next questions.

How have the land reforms affected bank lending (for purchase of real estate)?

What can be done as part of the land reform to further develop the mortgage market?

**SECTION 5: OTHER INFORMATION**

Is there anything else that you would like to add to the discussion we have had thus far?

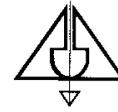
## Appendix A2: Schedule of interviews

	<u>Date/Time</u>	<u>Person interviewed</u>	<u>Institution</u>
1.	Tuesday 27 August (02:00pm-02:40pm)	Mr. Haroon Ali <i>Group Chief Risk Officer</i>	Bank of South Pacific
2.		Mr. Dave Wenham <i>Relationship Manager</i>	Bank of South Pacific
3.		Mr. George Barratt <i>Head of Lending Support Unit</i>	Bank of South Pacific
4.		Mr. Tom Wallace <i>Acting Chief Credit Officer</i>	Bank of South Pacific
5.	Wednesday 28 August (11:30am-12:10pm)	Mr. David Kui <i>Principal Economist</i>	Department of Treasury
6.		Mr. Moses Zazon <i>Senior Economist</i>	Department of Treasury
7.		Mr. Ian Nicholas <i>Advisor (Strongim Gavman Program)</i>	Department of Treasury
8.	Wednesday 28 August (01:35pm-02:15pm)	Mr. Donald Hallam <i>Acting Managing Director (Head of Corporate and Commercial Banking)</i>	Westpac
9.	Thursday 29 August (02:00pm-02:40pm)	Mr. Peter Burland <i>Business Development Manager</i>	Credit Corporation
10.	Friday 30 August (02:10pm-02:50pm)	Mr. John Crouch <i>Chief Risk Officer (North West Pacific Region)</i>	ANZ
11.	Friday 06 September (02:00pm-02:40pm)	Mr. Michael Van Dorssen <i>General Manager</i>	Kina Finance
12.		Ms. Kila Tau <i>Manager, Operations</i>	Kina Finance
13.		Ms. Manilah Apawa <i>Legal Officer</i>	Kina Finance

Appendix 3: Application Form for Lease on State Land



DEPARTMENT OF LANDS AND PHYSICAL PLANNING



Land Act 1996

**APPLICATION OR TENDER FORM**

(Cheque or attachment to be pinned to the Form)

Advertisement Number (if any) \_\_\_\_\_

A. (1) Application (Name in Full) \_\_\_\_\_

(2) Occupation \_\_\_\_\_

(3) Address \_\_\_\_\_

\_\_\_\_\_ Phone: \_\_\_\_\_

B. Type of Lease applied for \_\_\_\_\_

C. Proposed Purpose, Improvements and other Details (Stating Value of Improvements)

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

D. Description of Land (use only if not in response to an advertisement) \_\_\_\_\_

\_\_\_\_\_  
\_\_\_\_\_

(Sketch plan to be provided on an attachment).

E. Tender of Land Available Preference (additional preference on attachment if necessary).

Preference	Description (Lot and Section or Portion Number)	Amount Offered	Town	Province
------------	--	-------------------	------	----------

1<sup>st</sup> \_\_\_\_\_

2<sup>nd</sup> \_\_\_\_\_

3<sup>rd</sup> \_\_\_\_\_

**OFFICE USE ONLY**

FILE:.....  
 Receipt No:..... Signature of Applicant  
 Amount:..... Date:.....  
 Date:.....

(over)

**NOTE:**

**A. APPLICANT.**

Applicants or Tenderers should note-

1. Full name (block letters), occupation and personal postal address;
2. If a Company, the proper Registered Company name and address of the Company representative.
3. If more than one person, the tenancy desired and, if tenancy in common, the division of shares.

Applicants or Tenderers should note-

4. That a lease cannot be held in a name registered under the Business Names Act only; and
5. That in the case of death in joint tenancy, the deceased partner's interest vests in the surviving partner and, in the case of tenancy in common, the deceased partner's interest vests in his/her estate.

**B. TYPE OF LEASE.**

Leases provided for are Business, Pastoral, Agricultural, Mission, Special Purposes and Urban Development Leases. With the exception of Urban Development Leases, State lease may be granted for a maximum period of 99 years. Urban Development Leases, have a maximum duration of 5 years. Any application of town land, the purpose of the lease must be in accordance with the zoning as declared under the Town Planning Act.

**C. PROPOSED PURPOSES, IMPROVEMENTS, ETC.**

The applicant or Tenderer should provide fullest details (on attachment if necessary) of and for the lease including information on;

1. Financial status or prospects;
2. Details of other land holdings in PNG including, approximately the value of improvements to these holdings;
3. Approximate value and type of proposed improvements to the land applied for;
4. Experience and abilities to develop the land; and
5. Any other details which would support the application.

**D. DESCRIPTION OF LAND.**

To be used only if NOT in response to an advertisement. A brief description giving the area and locality is required. A sketch plan should be provided on a attachment. Where possible the land parcel should be identified on a map published by the Lands Department. In the case of Tenders or an advertisement of land available for leasing the description is to be inserted in the column provided under the heading "Tender or Land Available Preference".

In the case of Tenders or an advertisement of land available for leasing the description is to be inserted in the column provided under the heading "Tender or Land Available Preference".

**E. TENDER OR LAND AVAILABLE PREFERENCE.**

The Preference should be clearly indicated. In cases where there are more than Three (3) preferences the additional preferences may be shown on attachment. The "Description" should the Allotment and Section number or the Portion number as shown in the Gazette. The "Amount Offered" column need only be completed in the case of tenders.

**F. TENDERERS.**

Tenderers should take particular note that a tender for an amount less than the reserve price (being 60% of the unimproved value of the land) is invalid and shall not be considered. The successful tenderer will be required to pay the full amount of the tender.

**G. URBAN DEVELOPMENT LEASES (UDL).**

In addition to the requirements of the relevant sections above, an applicant or tenderer for an Urban Development Lease shall submit;

- (1) A preliminary proposal for the Urban Development Lease (UDL)
- (2) A preliminary sketch plan of the proposed Urban Development Lease (UDL)
- (3) Provisional proposals for subdivision surveys and installation of roads and drainage.

**H. FEES:**

- (1) All applications or tenders must be accompanied by a Registration of Application Fee. These are follows;
- |   |         |                                      |        |
|---|---------|--------------------------------------|--------|
| (i) Urban Development Lease                   | K500.00 | vi) Mission Leases                   | K20.00 |
| (ii) Residential High Covenant                | K50.00  | (vii) Agricultural Leases            | K20.00 |
| (iii) Residential Low/Medium Covenant         | K25.00  | (viii) Pastoral Leases               | K20.00 |
| (iv) Business/Commercial/Special Purposes     | K100.00 | (ix) Special Agricultural & Business |        |
| (v) Leases over settlement land (Urban/Rural) | K20.00  | Lease                                | K10.00 |

(2) Following the grant of the lease, an addition fee of K50.00 (preparation of lease fee), (and if surveyed, the survey fee as prescribed and, in the case of tender the amount of the tender shall be payable within two (2) months from the date of grantie, from the date of gazettal of the recommended lease holder in the PNG National Gazette.

(3) If not surveyed, the payment of survey fee may be deferred until survey.

**NOTE:**

If more than one block is required an additional Application Fee for each additional block must be paid.

**1. GENERAL.**

- (i) All applications must be lodged with the Secretary of Lands & Physical Planning.
- (ii) All applications without the required fee will be considered as informal.
- (iii) All applications will be considered by the Land Board at a date which will be notified to the application and in the National Gazette

## ABOUT THE AUTHORS

Satish Chand is Professor of Finance in the School of Business at the University of New South Wales Canberra. His research interests include labour migration, land reform, and the challenges of development in communities torn by conflict. For the past three years, Satish has been researching the rebound in the economy of Bougainville and how this rebound is helping sustain peace following the decade long conflict.

Dr. Justin Ondopa has a Bachelors degree in Land Studies from the PNG University of Technology, and a Masters in Resource Management and a Ph.D in Resource Ecology from Hiroshima University in Japan. He has worked with the University of Papua New Guinea, and in the hydrocarbon and NGO industry, and has extensive experience on Papua New Guinea and Pacific environment and resource management issues.

Ms. Logea Nao has a Bachelors degree in Economics from the University of Papua New Guinea. Logea was Project Officer at NRI within the Economics Policy Research Program (from October 2010 to April 2012); the Property Sector Development Research and Project Program (from May 2012 to July 2013); and then the National Land Development Program from July to November, 2013. Logea is currently undertaking postgraduate studies at the Australian National University in Canberra.

*The views expressed in this paper are entirely the authors' own and do not in any way or form reflect the views of the National Research Institute.*

## ABOUT THE NRI

The **National Research Institute** or NRI, is an Independent Statutory Authority established by the Government to carry out research into economic and social development issues affecting Papua New Guinea (PNG), and to generate debate and discussions leading to development of appropriate policy interventions.

Current research activities revolve around these development pillars, in line with *PNG Vision 2050* and PNG's Development Priorities:

1. Institutional Strengthening Pillar
  - Improving Basic Service Delivery (Sub-national Governance and Community Development).
  - Improving Governance Research Program.
2. People Pillar
  - Universal Basic Education Research Program.
  - Population Research Program.
3. Wealth Creation Pillar
  - Property Sector Development Research and Projects Program.
  - Economic Policy Research Program.

The NRI Issues Paper is designed to be more responsive to changing policy debates and discussions, and the need to make an informed intervention in policy discussions in a timely manner.

All NRI Issues Papers are available on our website, [www.nri.org.pg](http://www.nri.org.pg).

NATIONAL RESEARCH INSTITUTE—INQUIRE | INFORM | INFLUENCE