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SPOTLIGHT

THE DEFICIENCIES IN THE
COMPANIES ACT (1997) OF PAPUA
NEW GUINEA:
DOES IT PROMOTE EQUITABLE
DISTRIBUTION OF BENEFITS AMONG
LANDOWNERS?

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Key Points

- Deficiencies in the Companies Act (1997) have a negative effect on the management of landowner companies and distribution of landowner benefits.
- Deficiencies such as the absence of a company constitution and the selection of shareholders and directors greatly affect the flow of benefits from landowner companies to impacted landowner communities.
- Policy interventions such as reviewing the Companies Act, restructuring the current company structure, making company constitution a mandatory requirement, and accepting incorporated business groups as shareholders, ensure benefits are fairly distributed among landowner communities.
- Investment Promotion Authority (IPA) is the administrator of the Companies Act and regulator of landowner companies.
- In 2010, IPA investigated Ahi Holdings Limited, a landowner company, for mismanagement allegations.

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THE DEFICIENCIES IN THE COMPANIES ACT (1997) OF PAPUA NEW GUINEA

By Thomas Wangi

A study into customary landowner companies by Sanida et al. (2015) revealed a major anomaly in the operations of the Companies Act 1997 which is administered by the Investment Promotion Authority. The anomaly is that the Companies Act allows for landowner companies to have proxy shareholders who are not customary landowners, and representing the landowner communities at large. The proxy shareholders in turn elect the landowner company's directors. This practice creates a situation where the proxy shareholders with only a few landowner directors benefit while the majority of the landowner communities are excluded from the benefit sharing process.

The study by Sanida et al. (2015) reaffirms the government's land reform initiative aimed at improving equitable distribution of benefits among landowners who voluntarily register their land for development in Papua New Guinea (PNG). The study's aim was to improve the existing Act's policies to enhance IPA's role in providing a better equitable benefit sharing process to landowner communities. The research drew policy lessons from the Ahi Holdings case study, including especially policies relating to landowner companies within PNG, and called for a review of the Companies Act (1997).

The study's findings revealed that Section 42 of the Act states that any persons who are not members of the landowner groups can become independent shareholders and directors. As a result, the independent shareholders and directors pursue their own interests ahead of customary landowners interests. For example, the independent directors of Ahi Holdings Limited mismanaged the company for self-benefit, leaving aside the interests of the majority of the landowners.

To promote equitable distribution of benefits among entire landowner groups, the study recommended that IPA review the Act, remove proxy or independent shareholders and directors, allow for incorporate business groups to become shareholders and directors, and make company constitution a mandatory requirement for registration.

The operations of the Companies Act

IPA is the regulatory authority responsible for the administration of key business laws such as the Companies Act (1997) in PNG. The Act regulates the incorporation of companies, responsibilities of companies, shareholders and directors, dissolution of companies, and restoration of companies. The Act was amended in 2014 to improve corporate governance practices and ease regulatory burdens upon companies to do business. The Act also regulates the operations of landowner companies and manages landowner issues in PNG.

The study dealing with customary landowner companies by Sanida et al. (2015) highlighted several issues including the inefficient management and distribution of benefits resulting in poor welfare outcomes in the affected landowner community. Section 42 of the Companies Act deals with landowner issues relating to representatives whom landowners select as trustee shareholders and directors to form and manage a company. The customary landowners mobilise their resources, register the company with IPA and go into business with the support of the trustees. However, many landowner representatives do not understand the Act and its requirements, and as such the landowner companies are mismanaged. Deficiencies in the Act greatly affect the flow of financial and development benefits to genuine landowners.

The landowners conduct shareholders meetings in their villages when landowner representatives mismanage a company. The landowners then lodge new registration forms with IPA to appoint new shareholders and directors. Under the Act, only the shareholders can remove and appoint directors through a legally constituted shareholders meeting. As a result, the original shareholders and directors continue to hold office until a proper shareholders meeting is held.

The customary landowners report all mismanagement issues to IPA for formal investigations. IPA then conducts investigations under the Companies Act to determine allegations of mismanagement, to not only secure directors compliance but also for the benefit of genuine landowners. Unfortunately, investigations tend to be time consuming and frustrating as most landowner companies do not have fixed registered offices and contact addresses and most company directors are not known to IPA.

After the investigation, IPA advises the customary landowners to convince at least one or some shareholders and directors to call a special shareholders meeting in accordance with Section 102 of the Act or apply to the Court under Section 104 of the Act. If all fail even after the existing shareholders and directors are duly informed, then IPA proceeds to deregister the company. IPA can also apply to the court under Section 426 of the Act to disqualify the directors from holding office, and make interim arrangements until new trustees are elected or a new company is registered.

Case study of Ahi Holdings Limited

The Ahi Holding Limited (AHL) was a landowner company in Lae, Morobe Province, that was involved in the stevedoring business through Riback Stevedores Limited (RSL). AHL owned 51 percent of the shares in RSL, a joint venture business with Steamships Limited who owned 49 percent. The landowner company was formed in 1994 by six Ahi villages: Butibam, Hengali, Kamkumung, Yanga, Wagang, and Yalu and was registered with IPA in 1995.

AHL had six shareholders who were also directors representing the six Ahi villages. The landowners elected the shareholders for indefinite terms. The shareholders then among themselves, appointed a Board Chairman and a Managing Director. The shareholders only met when dividend payments were made by Steamships.

The financial flows to AHL were significant for many years as per the shareholding agreement with Steamships Limited but very limited evidence of tangible infrastructure or financial benefits were seen in the villages. The Ahi landowners claimed that the shareholders grossly mismanaged the company for their own interest and benefits were not equitably shared or spent in the best interest of landowners.

In 2009, the landowners registered AHL's mismanagement issue with IPA, leading to an investigation in 2010 as per Sections 400-407 of the Act. The investigation revealed that despite the substantial amount of benefits paid to AHL, there was little improvement in the welfare outcomes in the six Ahi villages. IPA recommended that the six villages conduct meetings to appoint new company shareholders. However, the meetings did not eventuate, and IPA filed legal proceedings to disqualify all the directors in any landowner companies including AHL. In the proceeding, IPA also took out interim restraining orders at the Waigani National Court, preventing the AHL directors from performing their duties.

Despite IPA's actions the Ahi landowners failed to appoint new shareholders. In 2013, IPA deregistered AHL and advised the Ahi landowners to create a new trustee company. Subsequently, the customary landowners established the Ahi

Investments Limited (AIL) which was registered with IPA in May 2015. The new company, like its predecessor, has six directors representing the six villages, however, the Registrar of Companies is the sole shareholder. The Registrar keeps 100 percent of the shares in a trust account until AIL has an approved company structure to manage its shares. This is a control measure taken by IPA to prevent abuse of landowner benefits. The Registrar will use Sections 372 and 373 of the Act to transfer the shares of AHL to AIL when AIL's company structure becomes operational.

The Ahi case study highlights several issues that commonly exist in landowner companies, and affect the welfare of many landowner communities.

Policy lessons from the Ahi Case study

Appoint shareholders in the village: The election of trustee shareholders should be conducted in the village and the selected trustee shareholders should execute a trust deed to represent landowners. The terms of the deed should determine how and when the trustee should be replaced as a shareholder and the term of office of the shareholder should also be stated in the deed.

Accept business groups as shareholders: The landowners should incorporate business groups to hold shares in trustee companies. In doing so, the chairperson of the business group will automatically be a trustee shareholder of the company, and appoint the board of directors. No individual persons should be accepted as shareholders.

Remove independent directors: The proxy directors should be removed from the company structure and replaced with landowner groups as shareholders and directors. The independent directors are seen as barriers to the flow of benefits to genuine landowners living in villages, as the proxy directors collude with few landowner trustees to protect their own interest.

Conduct workshops to understand the Companies Act requirements: Landowner companies should engage IPA officers to conduct workshops to educate the shareholders and directors of landowner companies of the Act and its requirements. This will ensure that the shareholders and directors understand and apply the Act's requirements and processes appropriately in the operations of the landowner company.

Does the Companies Act promote equitable distribution of benefits among landowners?

The customary landowners are engaged in spinoff business activities in resource and other project areas through registered companies and businesses. The business activities

are designed to benefit all members of the landowner groups. However, studies by Johnson (2012) and Sanida et al. (2015) on mining activities in Porgera and Hidden Valley respectively revealed that benefit sharing processes were ineffective, and benefits were not equitably shared among landowner communities. Only a few people benefit by relying on the laws, leaving the majority of the genuine beneficiaries out.

The key factors that adversely affect the flow of financial and other benefits are:

- **Deficiencies in the Companies Act:** Section 42 of the Act facilitates opportunities for any person who is not a member of a landowner group to participate in the decision making and benefit sharing process. The Act does not clearly stipulate the involvement of indigenous people in any landowner business, prompting outsiders to take advantage of the situation.
- **Existing company structure:** The current company structure allows for independent directors who are not landowners to be on the board of directors. The nomination of an independent director is not clearly stipulated in the laws. Any person can pursue his or her own agenda, diverting benefits away from the normal benefit sharing process. According to the Registrar of Companies (IPA, 2016), business and shareholder structures of many landowner companies change regularly (i.e. monthly, quarterly or yearly). Different landowner factions nominate their own trustee shareholders for the same company, making it difficult for IPA to manage the changes in the company structure. Additionally, the structure of company shareholding varies; including individuals, families, clans, or incorporated land groups (ILGs).
- **Lack of company constitution:** The company constitution serves as a legal guide for the landowner company and its operations. However, many landowner companies operate without a constitution. As such, company constitution should be a mandatory requirement for any landowner company to register with IPA. The constitution should clearly define the nature of business, identity of shareholders and directors, requirements of shareholders and directors, duties of shareholders and directors, relationship between shareholders and directors, relationship between landowners and directors, nomination of shareholders and directors, benefit sharing processes, office locations, and contact addresses.
- **Election of shareholders and directors:** The persons whom the landowners trust and vote as shareholders let them down in the benefit sharing process. According

to *The National* (2016), Porebada landowners were denied equal access to benefits through their landowner company, Porebada Holdings Limited. Several landowner companies have independent directors as trustees on the board, but how they are selected and the term of office for shareholders are not clearly stipulated in the company constitution.

Policy interventions for promoting equitable distribution of benefits

The Ahi case study and other studies on landowner businesses have shown that only a minority of landowners received benefits. Despite the large number of landowner companies operating in partnership with developers of major resource projects in PNG, much of the landowner communities still live in poverty with basic services such as roads, clinics, and schools in deteriorating conditions.

The Government through IPA has a responsibility to review the Companies Act, and develop appropriate guidelines to better manage the flow of benefits from landowner businesses. This can be achieved by:

- **Reviewing the Companies Act:** The Act needs to be fully reviewed to accommodate the interests of landowners who are missing out from the benefit sharing process of their landowner companies and businesses. The amended Companies Act 2014 gives more power to the Registrar of Companies to issue administrative guidelines to companies. However, proxy shareholders and directors will still remain until Section 42 of the Act is fully reviewed.
- **Redesign trustee type company structure:** The current company structure enables individuals who are not members of the customary landowner groups to become independent directors of landowner companies. Redesigning the company structure will allow only customary landowners to be shareholders and directors with strictness. The board under the new structure makes decisions in favour of landowners, and benefits are expected to be equally shared among the impacted communities.
- **Make constitution a mandatory requirement:** A company that registers with IPA must provide a constitution as an administrative mandatory requirement. The constitution guides the operations of the company, protects the welfare of the shareholders and directors, and promotes fairness in the distribution of benefits among the impacted communities. All stakeholders of the company must perform according to the constitution, and be

penalised for any wrong doings as stipulated in the constitution. IPA shall reject a company that fails to provide a constitution during lodging of application.

- Accept ILGs and business groups as shareholders: Some shareholders are elected by the landowners in the villages while others are nominated outside of the landowner communities. There are also directors who are nominated as trust appointees who have no customary link to the landowner groups. The individuals elected by the communities protect their own interests in the benefit sharing process, making the entire landowner communities suffer. Therefore, IPA should accept ILGs and business groups as shareholders to ensure the equitable distribution of benefits to landowner communities. The company constitution should clearly define the election process of the shareholders and directors.

Conclusion

This paper shows that deficiencies in the Companies Act have negative implications on the management of landowner companies and distribution of benefits to landowner communities.

The Ahi case study found that six shareholders who were also directors of the company had pursued their own interests, leaving the majority of the landowners out of the benefit sharing process. This emphasises the need for policy interventions to review the Act and improve the management and equitable distribution of benefits to landowner communities.

The review of the Act will facilitate the removal of independent directors and allow for incorporated business groups to become shareholders and directors. IPA should also enforce company constitution as a mandatory requirement for landowner communities to register their companies.

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