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Structural Deficiencies in the Frameworks Defining and Facilitating the Management of Landowner Benefit Streams: Lessons from the Porgera and Hidden Valley Mining Projects

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Introduction

On the eve of the much awaited Papua New Guinea (PNG) Liquefied Natural Gas (LNG) windfall, this article revisits one key question – Why is that the existing resource project benefit sharing arrangements not impacting the welfare of the project impact communities? Finding an answer to this question is critical because lessons from this can be useful for shaping the impact that the anticipated PNG LNG bonanza and other projects could have on the lives of the project impact communities and the nation as a whole.

Project impact communities include customary landowners, local-level governments (LLGs), and provincial governments in host provinces. Unlike the Mining sector, the PNG LNG project covers a vast area, categorised into production, pipeline and processing plant communities, LLGs, and provincial governments. Hence, the PNG LNG project is more complex and has a wider footprint. However, lessons for the efficient management of financial flows to the project impact communities are applicable in all sectors.

The National Research Institute (NRI) with its objective of ensuring that the exploitation of PNG's natural resources has a lasting and positive impact on the lives of the project impact communities and the nation at large, has undertaken a set of research projects. One set of research is focused at the national level, especially focusing on the need for the creation of the PNG Sovereign Wealth Fund (SWF). This article focuses on the impact of resource extraction projects at the project impact community level.

Our main emphasis is that, the proceeds from the extraction of these resources should have permanent and irreversible positive impact at the individual, family, community and national level. The average citizen should be able to enjoy the kind of lifestyle taken for granted in a modern society because the exploitation of these resources has made it possible. This is the vision we want the political leaders, landowners, and the broader community to embrace.

We therefore, through these different studies, aim to explore ways to support the National Government champion reforms that will ensure

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that the PNG LNG windfall and other windfalls do have a positive impact on the welfare of the affected communities, local government areas, the provinces, and the nation as a whole. Hence, this article draws from two recent reports, lessons useful for improving the institutional structures that oversee the management of the benefits stream flows.

The Case Studies

This article draws findings from two cases studies: the Porgera Gold Mine and the Hidden Valley Mine in the Enga and Morobe Provinces, respectively. These studies shed light on the benefits sharing, management, and distribution process by unpacking the agreements that underpin the project developments.

Porgera Gold Mine

In 2011, the NRI undertook a study into the landowner benefits from the Porgera Gold Mine (Johnson, P, 2012. *Lode Shedding: A Case Study of the Economic Benefits to the Landowners, the Provincial Government and the State, from the Porgera Gold Mine: Background and Financial Flows from the Mine*). The study aimed to address a broader question of why PNG is resource-rich yet its citizens remain poor. The specific objectives of the study were to:

- track the financial benefit streams of the Porgera Gold Mine;
- analyse some of the important frameworks put in place to achieve outcomes sought by the developer, landowners, provincial, and national governments; and
- examine the linkages between the Memorandum of Agreement (MOA), financial benefits from the mine, institutional structures, and development outcomes.

The study examined the:

- content of the original Porgera agreements and their implementation;
- chain of agreements to see if goals had been achieved;
- type and size of benefits and their distribution; and
- areas where revenues have been spent and how effective they were.

The main findings are that the project developer (Porgera Joint Venture) clearly indicated that payments made to landowner entities, consistent with the mining agreement, and the benefits to landowners, whilst substantial, are not clear, and opaque. Only a few people benefit whilst the majority suffer. However, attempts to interview and get more information on how these funds were used were not successful.

The study makes the overall conclusion that without greater transparency in how finances from resource development are managed and distributed, PNG will remain resource rich and its people remain poor. Recommendations were made for better management of these funds, through structures such as a SWF model. This is to cater for both intra (current generation) and intergenerational (future generation) equity. The objective is to ensure that both the present and future generations benefit from the proceeds of these investments.

Hidden Valley Mine

The Hidden Valley Mine study was commissioned by the Bulolo Joint District Planning and Budget Priorities Committee (Sanida, O., Mako, A., and Yala, C, 2015. *A Review and Assessment of the Benefit-Sharing Arrangements for Large-Scale Mining Activities in Wau-Bulolo, Papua New Guinea*). The analysis focused on comparing the expectations under the 2009 Memorandum of Agreement (MOA) and actual outcomes, in order to ascertain whether:

- the MOA terms were followed, in terms of the benefits flows; and
- the benefit sharing mechanism was appropriate.

The study found that the project developer (Hidden Valley Joint Venture) like its counterpart in Porgera (Porgera Joint Venture), has channelled all the financial and development benefits (royalties, compensation, etc), as per the MOA to the various recipients. With regards to the second question, the benefit sharing mechanism was not appropriate. There were serious structural flows with the design of the institutions that receive and manage the benefits flows. In fact the Hidden Valley study indicates that landowner benefits are not equitably shared nor spent in the best interests of a majority of landowners. Recommendations are made again on better management systems of landowner benefits.

The findings from both studies indicate that:

- financial flows to the landowning communities are consistent with the project development agreements;
- financial flows to the landowning communities are significant, and
- landowner benefits are not equitably shared nor spent in the best interests of a majority of landowners.

Both studies make recommendations to improve the management and equitable distributions of landowner benefits.

Structural Design Issues

A detailed analysis of the frameworks that manage landowner benefits depicts that:

- institutions that define and manage landowner benefits, that is, the landowner associations and landowner companies have serious deficiencies in their structural design, hence undermining sound governance and prudent management;
- management of the benefits flows; that is, both the financial and development flows, suffer from high coordination and high transaction costs because the funds are managed or distributed through many different channels and agencies; and
- funds are sparingly distributed across a variety of channels, thereby losing economies of scale.

These structural deficiencies create an environment that is conducive for rampant rent-seeking by those entrusted to manage the benefits flows, raise transaction costs, and encourages poor coordination and inefficient management systems and processes. Hence, despite the large financial flows, the expected welfare benefit outcomes are not achieved. The policy challenge is to address the weaknesses in the structural design of the framework for facilitating and managing landowners' benefits flows.

Lessons for Policy

These findings need to be seen in the context of current debates at the national level. An emerging issue is the push by some to have more landowner equity in resource development projects, as they argue that they do not get enough of their share of the benefits. Perhaps the problem lies, as we suggest, in the structure of the benefits sharing mechanisms.

Focusing at the landowning community level, the benefits are not being shared and/or spent for the benefit of landowners and surrounding communities. The key issues fuelling these arguments are that the:

- the bulk of the landowners do not see the benefits. It is obvious from our two studies that only a few people are benefiting whilst the larger majority do not see nor know about this;
- Provincial and Local-level Governments may not be spending the monies for projects as agreed to, in the localities for the benefit of landowners and surrounding communities; and
- the National Government may not be remitting funds to Provincial Governments and other entities to spend on areas agreed to, for the benefit of communities living in the vicinity of the mining areas. Also some projects agreed to, for delivery to project sites by the National Government through Public Investment Projects (PIP) such as in Porgera have not been adhered to.

The National Government has a responsibility to review and improve on providing appropriate institutional frameworks for better management of

landowner benefits so that they genuinely benefit from the resources being extracted from their land. Moreover, this will help minimise the risks posed by landowners to the investment community.

At the national level, there is an euphoria about the potential positive impact from the anticipated PNG LNG Bonanza. There is also a silent but strong view that the PNG LNG Bonanza might disappear into thin air, leaving behind an impoverished and dysfunctional country. The findings from these two case studies provide useful lessons for policy that will assist in sound policy analysis and debate. This in turn, would lead to reforms that will help improve on the systems and processes that ensures that frameworks are sound and channelling the benefits stream to improving the livelihood of all, especially the project impact communities.

A New Structure and Process

The Porgera study recommended that a SWF structure be adopted for managing the landowning benefits streams. The Hidden Valley study provided a simplified structure that divides the benefits flow from the resources sector to the host communities into two streams – Financial and Development:

- **Financial Benefits Pool:** This pools financial flows (royalties, business spin-offs and Hidden Valley Mine benefits) into one pool which can be divided into three funds:
 - ◆ long-term (40%) – The fund addresses the intergenerational issue. This fund is saved and invested for long-term. Investments can be within country or out of the country. The income generated from this can be used at a certain point in future to benefit the future/younger generation.
 - ◆ human capital formation (40%) – The fund is for health (insurance scheme), education scheme (scholarship), and better housing for all beneficiaries. These three are critical for the development of a person. Good housing, education and health are fundamental for the development of a transformed and educated population. For instance, a child born into a landowning family, at the start of a mine, will be able to grow up in a good house, have access to quality health service and will be educated by the time the child turns 21.
 - ◆ cash (20%) – This is the remaining component which is to be given out either as direct cash or shopping vouchers to meet current consumption needs.

The institutional basis for managing the Financial Benefits Pool is the Incorporated Land Group (ILG) incorporated under the *Land*

Groups Incorporation (Amendment) Act (1974), currently being implemented through the auspices of the National Land Development Program. The ILG is a better institutional structure considering its management and governance structure than the landowner-based associations. Further, reforms are needed to promote efficient management of landowner companies. There exist significant weaknesses in the existing *Companies Act* which need to be reviewed with the view to improving the management and operation of landowner companies.

- **Development Benefits Pool:** The proposal is to have all development funds (special support grants, tax credit schemes, and donor funded projects) pooled into one and used for development through a *Special Purpose Vehicle (SPV)* that has four distinct institutions:
 - ◆ the State – The State should have one person representing the national, provincial and local-level government interests;
 - ◆ Developer – project developer;
 - ◆ Community—a community representative representing the interests of all the mine-affected communities, including customary landowners; and
 - ◆ Independent Development Financier – one representing other funding agencies such as donors who have an interest in supporting development in such communities.

(Note that compensation payments are not included in the two pools because they are “victim” specific payments, which cannot be regulated, as far as distribution is concerned).

The four institutional representatives play an oversight role over the SPV. The SPV must be tasked to procure and oversee the development of the requisite infrastructure, which will permanently transform the mining affected communities. This may include the development of a viable township, where possible.

Conclusion

This article affirms that the financial and development flows from the existing resource development projects are substantial and consistent with the resource development agreements. However, there are structural weaknesses in the framework that manages these

benefits streams. The weaknesses appear to be universal and that the PNG LNG project and other projects may have the same inherent weaknesses.

Suggestions are made for a better framework which will improve on these weaknesses and improve the distribution mechanism for the effective sharing and management of landowner benefits in the resources sector.

Lessons were drawn from two case studies: Porgera Gold Mine and Hidden Valley Mine, focusing largely on the benefits flow to the landowning communities. Both case studies demonstrated that the current mechanisms for sharing and managing the benefits flows from the mining activities are weak. A two-funds benefits stream management pool is proposed – financial and development – with well-defined institutional structures that ensures efficient management of the benefits flow. The ILG is promoted as the grassroots foundational institution for managing the Financial Benefits Pool stream. The SPV is proposed for the management of the Development Benefits Pool stream. Institutional weaknesses in the *Companies Act* which is undermining efficient management of landowner companies have also been highlighted. The key argument is that, with proper management structures, the benefits flows to the landowners from resource developments can be used to achieve optimum benefit for the present and future generations.

The National Government has a responsibility to review and improve on providing appropriate institutional frameworks for better management of landowner benefits so that they genuinely benefit from the resources being extracted from their land. This is also an important avenue to minimise the risks posed by landowners to the investment community.

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