



# ‘Black gold or excrement of the devil’?<sup>1</sup>

## The externalities of oil production in Papua New Guinea

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Southern Highlands Province in Papua New Guinea has received hundreds of millions of kina from oil exports. However, it has failed to translate this windfall into long-term benefits for its people, resulting in the prevalence of ‘poverty amidst wealth’. The paper considers this outcome a consequence of poor public policy choices and weak governance, rent seeking, corruption, and lawlessness, and puts forward alternative policies.

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This article examines why the Southern Highlands Province, the only province in Papua New Guinea in which oil and gas reserves have been found in commercial quantities, has so spectacularly mismanaged its share of the oil revenues. In a major statement to parliament on the economic situation of Southern Highlands Province, the Minister for Inter-Government Relations, Sir Peter Barter, noted recently that the province’s ability to manage this windfall effectively has so far been a complete failure.<sup>2</sup>

The article details the types of revenues received from oil production since 1992 and considers how Southern Highlands Province has been utilising these monies, resulting in its current state where it is deemed to be on the brink of collapse.<sup>3</sup> It is argued that this

situation has arisen mainly because of principal-agent problems, rent-seeking behaviour, and corruption associated with the use of oil revenues in the province. Some suggestions are provided for the government of Southern Highlands Province and the national government to manage oil revenues better so that they can steer away from what is here termed the ‘PNG disease’.<sup>4</sup>

### **Brief overview of oil development in Papua New Guinea**

Oil and gas exploration has been undertaken in Papua New Guinea since 1911 and small and uneconomic oil and gas fields were found in the 1950s and 1960s (Rickwood



1990). Development of the petroleum industry in Papua New Guinea can be mainly attributed to the discovery of the Kutubu oil fields in the late 1980s. The Kutubu project, which came on line on 28 October 1991, was the first commercial project to produce hydrocarbon exports. On 27 June 1992 the first shipment of Kutubu's 'light sweet crude' was exported via the offshore marine terminal (the Kumul Platform) in the Gulf of Papua. This milestone achievement marked the beginning of the receipt of oil revenues by the national government as well as the host province of the oil fields, the Southern Highlands Province.

After the discovery and development of the Kutubu oil fields, further exploration work resulted in the discovery of the South East (SE) Gobe oil field in 1991, which '...was followed by further exploration wells, first on the SE Gobe structure and then on related structures' (AusAID 1998:198). The Gobe project began producing oil in April 1998 from two separate oil fields under two separate licences which, for purposes of operational ease, were unified as a single petroleum project. Exploration outside the Kutubu and Gobe areas in 1995 and 1996 resulted in the discovery of the Paua and Moran structures. The Moran project commenced commercial production under an extended well testing program in February 1998.<sup>5</sup> Moran became a licensed commercial operation in February 2001 when the national government granted it a petroleum development licence (PDL) and recognised Moran as Papua New Guinea's third oil field. Papua New Guinea now has four main petroleum-producing fields: Hides gas field and the Kutubu, Gobe and Moran oil fields.

For the purposes of this discussion only oil revenues derived from the sale of oil from the Kutubu, Gobe and Moran oil projects and either directly or indirectly channeled into the Southern Highlands provincial

administration as well as various local-level governments within Southern Highlands Province, are relevant and considered in terms of their use and/or misuse. The period considered spans nine years from 1992 to 2001.

### **Oil revenues accruing to the Southern Highlands Province**

There are two broad categories of oil benefits accruing to Southern Highlands Province. The first is direct monetary or cash benefits paid directly to landowners, local-level governments, and the Southern Highlands provincial government. Payments to landowners include royalties, equity dividends, land compensation payments, land rental payments, and Memorandum of Agreement (MOA) grants and business development grants. MOA grants are usually awarded to local (landowner) business contractors for the implementation of prescribed infrastructure projects within local communities, such as classrooms, aid-posts and feeder roads. Such contracts are supposedly awarded after a bidding process administered by the Southern Highlands Provincial Supply and Tenders Board.

Cash benefits are also received by the Southern Highlands provincial government and local-level governments whose administrative jurisdictions overlap or are within close proximity to the licence area of a petroleum project. As well as their allotted shares of royalties and equity dividends, based on what is stipulated under the MOAs for each petroleum project, the provincial and local-level governments also receive Special Support Grants (SSGs) and Infrastructure Grants. For instance, in the case of the Kutubu oil project, the provincial government receives SSGs and Infrastructure Grants awarded under the clauses of the Kutubu MOA, based on the former Petroleum



Act, but now repealed. Both of these grants are supposed to be used for developmental projects within the project area as well as in other parts of Southern Highlands Province. Under the Moran Petroleum Project benefit arrangements, the SSG has been replaced by a Development Levy, as stipulated under the new Oil and Gas Act 1998 (amended 2001), which is only paid to the Southern Highlands provincial government. Royalties are disbursed on a monthly basis while equity dividends are paid quarterly to the recipients, be they landowners, local-level governments or the Southern Highlands provincial government.<sup>6</sup>

The second broad category of benefits accruing to the Southern Highlands Province consists of non-cash benefits or benefits-in-kind, which are received by individuals and groups. Non-cash benefits received by individuals, usually landowners, include employment opportunities, on-the-job training, and scholarships for short to long-term educational, vocational and other training opportunities, especially in higher learning institutions. Benefits-in-kind awarded to groups include the direct awarding of business contracts to landowner companies, financial loan guarantees to commercial banks on behalf of new landowner business ventures, and MOA grants to landowner companies for expenditure related to infrastructure implementation. The main benefits-in-kind accruing to the Southern Highlands provincial government include the Tax Credit Scheme infrastructure projects. Both the MOA grants and the Tax Credit Scheme are intended to facilitate the provision of basic infrastructure and social services such as roads, bridges, schools, aid posts and health centres in the project area and in other needy areas within the Southern Highlands Province, as per their district and provincial development plans.

#### **Actual oil revenues received by the Southern Highlands Province, 1992–2001**

Table 1 provides a summary of oil revenues received by the Southern Highlands Province between 1992 and 2001. Item A shows total benefits paid to the national government over the same period, amounting to around K2.5 billion. This total is made up of five components of which 88 per cent is petroleum income tax; 7 per cent is salary and wages tax across all oil projects; 3 per cent is stamp duty and import taxes across all projects; 1.9 per cent is equity dividends paid from projects in which the State holds equity; and 0.1 per cent is from business withholding tax applicable only to the Kutubu oil project (under Petroleum Development License 2). This tax revenue is paid into the national government's consolidated revenue. A portion of consolidated revenue is allocated to the Southern Highlands provincial government as its share of the annual provincial budgetary allocations. In order to show clearly the oil monies received directly by the Southern Highlands Province, the total national government oil receipts of K2.5 billion are deducted from the total oil revenue (Table 1).

The K158 million paid as direct landowner cash benefits comprises four components. The largest, the equity dividends component, is 55.4 per cent of the total. The equity benefit is only derived from the Kutubu and Gobe projects in which the landowners have 2 per cent equity holdings. In the case of the Kutubu project, even landowners who live outside the area of Project Development License 2 but along the export pipeline route also benefit from this 2 per cent equity. The next largest component is net royalty payments paid to landowner customary groups defined as Incorporated Land Groups. This amounts to 41 per cent of the total. Land compensation payments<sup>7</sup> are only 2.9 per cent of the total. These are



**Table 1 Summary of benefits received by the Southern Highlands Province from oil production, 1992–2001 (million kina)**

| Item                                                                | Category of benefits received                                          | kina (million) |
|---------------------------------------------------------------------|------------------------------------------------------------------------|----------------|
| A                                                                   | National Government revenue <sup>a</sup>                               | 2,487          |
| B                                                                   | Direct landowner cash benefits <sup>b</sup>                            | 158            |
| C                                                                   | Landowner and district non-cash benefits <sup>c</sup>                  | 401            |
| D                                                                   | Provincial Government and Local-Level Government benefits <sup>d</sup> | 182            |
| Total benefits                                                      |                                                                        | 3,228          |
| Less taxes paid to consolidated revenue                             |                                                                        | 2,487          |
| Total benefits received by Southern Highlands Provincial Government |                                                                        | 741            |

<sup>a</sup> Paid into the national government's consolidated revenue.

<sup>b</sup> Paid as cash to landowners.

<sup>c</sup> These benefits are in-kind—jobs and training, business contracts, loan guarantees, infrastructure projects, school scholarships, and so on.

<sup>d</sup> Some money from the national government's consolidated revenue is distributed to the provincial government under the annual provincial budgetary appropriations.

**Source:** Papua New Guinea, 2001. *Summary of Consolidated Benefits*, Department of Petroleum and Energy, Government of Papua New Guinea, Port Moresby.

payments made to all project area landowners whose lands are adversely affected by the oil development, in terms of environmental damage, such as limestone quarrying, and damage to food gardens and economic trees. The final component of direct cash benefits to landowners is land rental payments from all three oil projects. This is a mere 0.7 per cent of the total.

Item C in Table 1 comprises total landowner and district non-cash benefits. Of this, the largest share of 40.1 per cent has been in the form of landowner business contracts awarded by the project operators. This is followed by Tax Credit Scheme project expenditures, accounting for 26.7 per cent of the total. Salaries and wages paid to Papua New Guineans through their employment in the projects as well as monies spent on their training make up the third largest component with 25.2 per cent. Scholarships for higher education and training as well as financial

loan guarantees to commercial banks for new landowner companies venturing into first-time businesses follow with 3.7 per cent each.<sup>8</sup> Last, MOA grants for social infrastructure projects amounted to only 0.6 per cent of the total. These benefits not only accrue to project area landowners but also to groups of people who do not necessarily own traditional land within a Petroleum Development License demarcation but who live within the vicinity of the oil project or within the administrative boundaries of the districts which an oil project overlays.

Provincial and local-level government benefits comprise six components. Royalties paid to the provincial government accounted for 46 per cent (K182 million) of the total amount. SSGs and/or Development Levies made up 26 per cent of the total; whilst equity dividends received by the provincial government, particularly from the Kutubu Project, accounted for 16 per cent. MOA



grants to the province and the local-level governments, as stipulated under the relevant clauses of the Kutubu and Gobe MOAs, constituted 7 per cent of the total; whilst total Infrastructure Grants amounted to only 4 per cent. Finally, royalties paid to the local-level governments, mainly from the Moran project, were a mere one per cent of the total.

Undoubtedly, the total amount of K741 million received by the province in one form or another is a windfall by any standard, especially when it is over and above the province's annual budgetary appropriations from the national government.

#### **Evidence of maladministration, misappropriation and corruption**

Whilst evidence that oil revenues are being squandered is not easily accessible due to poor record-keeping in various government offices, as well as the secrecy inevitably involved in dubious dealings, there are a few government reports that point towards such practices. One such report was compiled in May 2003 by the Department of Provincial and Local Government Affairs (Papua New Guinea 2003).

Stories pertaining to poor use of oil revenues, corruption, mismanagement and misuse are frequently reported in the media, especially the two daily newspapers, the *Post-Courier* and *The National*. The print media plays a pivotal role in keeping the public abreast of what is happening in Southern Highlands Province. Newspaper stories, feature articles or columns and letters, deemed as anecdotal evidence, are indicators of the level of complaints, disappointments and frustrations voiced by many sectors of the community against the Southern Highlands provincial government over its mismanagement and misapplication of oil revenues.

Based on the nature and frequency of complaints and the extent of reporting of

stories about the mismanagement, misappropriation and corruption related to the Southern Highlands provincial government's use of oil revenues, it is possible to draw some conclusions about the government's performance.

#### **An official report describing misuse of oil revenues**

The 2003 report by the Department of Provincial and Local Government Affairs was commissioned after complaints were received by the Minister for Inter-Government Relations relating to allegations of misappropriation, abuse of office and illegal diversion of funds by those responsible for the management of the Kutubu Special Purpose Authority (KSPA), the body which receives 30 per cent of all SSGs and Infrastructure Grants (Table 1) accruing to the province from the Kutubu Petroleum Project.

The report revealed that Infrastructure Grants and SSGs had not been properly accounted for and that planned projects for the Kutubu project area had not been implemented despite funds being expended for them. Further, physical inspection of most projects claimed to have been funded and implemented by the Kutubu Development Authority revealed that the projects did not exist; in other words, even when Infrastructure Grants were expended, they were not used for their intended purposes (see also Koyama 2004:27).<sup>9</sup> In most instances, funds were diverted to unbudgeted activities by political leaders, provincial administrators and the chairman of the KSPA (Papua New Guinea 2003:3–4; Koyama 2004:27–8). These are vivid examples of the principal-agent problems prevalent in Southern Highlands Province. Furthermore, in most of these cases, the use of grants did not conform to any financial standard or guidelines; many of the payments were not accompanied by documentary evidence to substantiate them (Papua New Guinea 2003:13, 16). The report



also disclosed that although the provincial administration had been managing SSGs since the early 1990s, there was 'little or nothing in terms of tangible social and economic development in the Kutubu Project area' (Papua New Guinea 2003:15).

Among the many recommendations in the report, the most notable were those that strongly recommended referral to the Police Fraud Squad for further investigation and possible prosecution of persons implicated in allegations of impropriety and malfeasance within the Southern Highlands provincial government, particularly those who were responsible for administering the Infrastructure Grants and SSGs (Papua New Guinea 2003:14, 17).

The report catalogues very clear examples of principal-agent problems, rent-seeking behaviour and corruption directly related to the management of oil revenues that are entrenched in Southern Highlands Province. These problems appear to be strangling the transparent use of oil revenues for the social and economic needs of the province.

#### **A brief review of newspaper reports describing corruption and misuse of oil revenues**

Other examples of principal-agent problems and rent-seeking behaviour manifested in the maladministration, misappropriation and outright theft of oil revenues are often reported in stories and letters to the editor in Papua New Guinea's two daily papers. For the purpose of emphasising the problems highlighted in the above-mentioned report and providing additional evidence in support of the contention that oil revenues are being misappropriated, a few of these news stories and letters are discussed below.

A *Post-Courier* article, 'Call to Suspend Southern Highlands Province Government' (22 October 2004:7) reported that Paul Tegi, the Director of a non-government organisation,

PNG Rural Development, announced that the people of Southern Highlands Province were calling on the National Executive Council to suspend their provincial government immediately following an allegation of misappropriation of more than K1.7 million. Mr Tegi produced evidence by way of affidavits to show that monies were paid to individuals and non-existent projects and that people in the province were helping themselves to provincial treasury funds for 'ghost services' rendered to the provincial government.

In one of his series of articles in *The National* on the plight of Southern Highlands Province amidst the chaos created by a breakdown of law and order, absence of good leadership and 'systemic and systematic corruption'<sup>10</sup> perpetrated by irresponsible civil servants, Kevin Pamba reminisced about the 'good old days' when the Southern Highlands Provincial Works Department was under the management of the 12 Civil Engineers Works Unit of the Australian Army. The columnist lamented that it was then when most of the roads, bridges and building infrastructure of Southern Highlands Province were built and maintained. With their departure at the end of 1999, things went from bad to worse. He attributed this to the lack of discipline and commitment by civil servants in the province and its overall poor governance. The article 'Australian officials could assist Southern Highlands Province recover' (*The National*, 31 August 2004:17), suggested that the national government consider sending Australian personnel under the Enhanced Cooperation Package to Southern Highlands Province to restore discipline and commitment as a foundation for good governance to flourish again within the Southern Highlands provincial government bureaucracy.

In another article, 'Can Yawari live up to his promise?' (*The National*, 26 October 2004:10), Mr Pamba bemoaned the fact that



many business houses were deserting the Southern Highlands Province. Hence, it was obvious that the tag 'resource rich province' was becoming a misnomer. He observed that while the immediate residents of the petroleum projects may have enjoyed some benefits, the rest of the province had failed to see the materialisation of oil revenues in tangible outcomes. Mr Pamba pondered over what life would be like, post oil and gas, especially in the absence of a clear policy and a distinct post oil and gas abandonment plan in place. This, as he pointed out, is a major problem, especially when the province is being inundated with 'false claims' and other improprieties and malfeasances relating to management of its public treasury, coupled with the evidence of 'carpetbaggers' and 'spivs' roaming the province.

The *Post-Courier* article, 'Southern Highlands in turmoil. Services kept from people' (5 August 2004:11–12), was a summarised version of a Ministerial Statement by the Minister for Inter-Government Relations, stating that the delivery of basic services collapsed where resources are being misapplied and misused and that the maintenance of law and good order is a significant problem in Southern Highlands Province. A clear example of this is the publicly touted 'free education' policy, which had resulted in the premature closure of many schools due to their non-receipt of basic school supplies on time. The Minister recommended that the national government be made aware of the chaotic situation in Southern Highlands Province and immediate steps be taken to redress it through investigations by the Police Fraud Squad, the Department of Finance and the Auditor General's office into the many cases of misapplication of public funds with a view towards possible prosecution of alleged perpetrators.

Concerning the publicly lauded 'free education' policy by the Governor for Southern Highlands Province, the Minister

for Education pointed out that it would cost an additional K10 million on top of the budgeted K9.5 million to have all schools in Southern Highlands Province operate successfully until the end of the 2004 academic year. This was disclosed after many schools had prematurely ended their school year when much needed supplies, such as food rations, books, and school equipment, failed to reach them on time. This news item was reported in *The National* (10 August 2004:6) with the title, 'K10m shortfall for Southern Highlands Province schools'.

The problem with peace and good order was further highlighted in a front-page story 'Southern Highlands Province guns scare. Business leader warns of violence, bloodshed' (*The National*, 18 August 2004:1–2), when the Chairman of the Gobe Leadership Committee revealed that there is a proliferation of high-powered guns in the Southern Highlands Province and further alleged that most were bought by project area landowners using oil monies. Alarmed by this development, the Gobe landowner leader described the situation as a disaster waiting to happen, especially when the Department of Petroleum and Energy and the oil resource developers were reluctant to take any action.

In reiterating the call for investigation and prosecution of alleged suspects of corruption, Frank Senge Kolma in his article, 'Southern Highlands Province on the brink. Government fears collapse of province, takes tough administrative measures' (*The Weekend National*, 13–15 August 2004:1–2), reported that whilst deliberating on the likelihood of declaring Southern Highlands Province a state of emergency, Cabinet decided that one of the outstanding tasks was to conduct a thorough investigation leading to possible prosecution of alleged perpetrators featured in the many documented cases of fraud, misappropriation and graft within the Southern Highlands provincial government and local-level governments.



Many letters to the editors of the *Post-Courier* and *The National* resonate with the same cry for investigations into the alleged misuse and corrupt practices surrounding public funds within the echelons of the Southern Highlands provincial and district administrations. In a letter headed, 'Officers drain Southern Highlands Province treasury', (*The National*, 15 January 2004:22), Titus H. of Port Moresby alleged that when Southern Highlands' provincial government financial functions were transferred to the National Department of Finance in Port Moresby,<sup>11</sup> amounts ranging from K3,000 to K50,000 were paid to Southern Highlands provincial 'government service providers' and contractors, most of them being Port Moresby residents. This prompted the letterwriter to plead for the vigilant administration and stringent control of Southern Highlands Province funds.

Guy Gibson's letter 'Southern Highlands Province must be suspended' (*The National*, 21 October 2004:14) was intended to garner public support to have Southern Highlands provincial government suspended. The most profound reasons cited were poor government administration, especially in the use of public funds to pay 'false claims' submitted by fraudulent service providers, who had orchestrated highly irregular and questionable financial claims for 'ghost services' rendered to the Southern Highlands provincial government.

Likewise, in another letter by Yana Apunae of Lae, entitled 'Too many unresolved cases in Southern Highlands Province' (*The National*, 14 October 2004:14), the writer laments the many unresolved cases of 'theft of public funds and corruption' that had never appeared before the courts and alleged that such outcomes resulted from political interventions. Mr Apunae cited eight cases of corrupt practices that required immediate investigation.

The current situation, where politics operates along ethnic lines, and social and economic development initiatives are polarised along similar lines, is a result of certain individuals and/or groups employing their tribal, financial and political clout to leverage a grapple-hold on the millions of kina in oil revenues accruing to Southern Highlands Province annually.

Generally, what may be termed the 'PNG disease' appears as a consequence of a weak policy environment, poor governance and corruption, which have clearly manifested themselves in Southern Highlands Province, where we have 'pirates in power' benefiting from kickbacks and other forms of embezzlement of public funds, nepotism or cronyism, ethnocentrism (*wantok*-ism), and all forms of bribery and corruption. These have contributed towards negative economic growth and other staggering malign results. This situation has also been described in Koyama (2004:24–28) which catalogues various forms of principal-agent problems, rent-seeking and corruption amongst leaders and members of incorporated land groups that regularly receive oil revenues on behalf of individual project area landowners of the three oil projects in Southern Highlands Province.

Windybank and Manning (2003:2) have made similar observations regarding the wasteful utilisation of resource rents in Papua New Guinea. They argue that abundant mineral resources, including gold, copper and substantial oil and gas reserves, created windfall incomes but these have ended up in waste and corruption. Such rent-seeking behaviour is responsible for the rise of a 'small political élite' and overblown government bureaucracies at the expense of infrastructure development and the diversification of the economy.

The latest report of the Economic Analytical Unit of the Australian Government's



Department of Foreign Affairs and Trade, *Papua New Guinea: the road ahead*, expresses similar sentiments. The report states that while Papua New Guinea is endowed with vast natural resources, these have not been translated into better living standards and that economic growth is characterised by a boom and bust cycle. It also states that ingredients of 'poor governance, lawlessness, political instability, poor fiscal management and inadequate physical infrastructure and utilities' (Australia 2004:xv) have all been added to the menu, resulting in an unpalatable broth of economic and social decline.

### **A prescription for 'PNG disease' and the 'curse of oil'**

Nonetheless, there is still a glimmer of hope as one realises that the PNG disease is not HIV/AIDS!<sup>12</sup> With proper antidotes, the PNG disease is curable and there remain many opportunities to turn the curse of oil into a blessing. Following are some antidotes for PNG disease and the so-called curse of oil.

- Distributing oil revenues directly to the people as in the case of the State of Alaska and the Canadian province of Alberta. This would mean making oil revenues less available to 'pirates in power'. It must be noted that in both cases, it is the interest earned from oil funds that is distributed and not direct oil revenues, such as royalties.
- Ensuring that the Department of Petroleum and Energy's Social Mapping and Landowner Identification Regulation is urgently endorsed by Cabinet to allow for proper identification of true landowners while curtailing fictitious landowners who are usually prone towards rent-seeking behaviour.

Moreover, ensuring that negotiations during Development Forums and other forums are not conducted under duress and that the State is not coerced into agreements favouring rent-seekers. One such measure immediately available to the State is to invoke Section 174 of the Oil and Gas Act, which places a limit on project benefits accruing to landowners, local-level governments and provincial governments.

- Ensuring that the distribution of oil revenues, at the national and provincial level, to the people of Southern Highlands Province is supported by institutions and mechanisms that are accountable and transparent in all their facets, with checks and balance mechanisms at all stages of collection, management and disbursement of revenues. This should be done both at the national and provincial level. If the insertion of accountable and transparent mechanisms proves to be difficult at the provincial and local government levels, then the national government should seriously consider whether it is in Papua New Guinea's best interest in the long term to continue with the current three-tier decentralised government system which, in the case of Southern Highlands Province, has resulted in a rent-seeking and corruption-prone bureaucracy. In most of its activities the provincial government has demonstrated that it is not subservient to the interests of the people of Southern Highlands Province but serves the whims of its politicians and bureaucrats. The question of whether a three-tier government structure is good for Papua New Guinea or whether it mainly serves to provide opportunities for rent-seeking and corruption and hence for the PNG



disease to thrive should be re-visited and thoroughly debated.

- Ensuring that Papua New Guinea joins the 'Publish What You Pay Campaign'.<sup>13</sup> This campaign is being promoted in Africa by churches and civil society groups who are calling on governments and oil companies to be more transparent in their operations and financial dealings. Civil society groups and ordinary citizens are then able to utilise whatever political space is available to them to attempt to hold their governments to account (Gary and Karl 2003:5–7). The national government should formulate a 'publish what you pay policy' to ensure transparency and accountability of resource rents accruing to landowners and the three-tier government structure.
- Fighting corruption at all levels of government. Whilst there are legal sanctions against corruption in its myriad forms, it is the glaring lack of enforcement that needs improvement. A few exemplary prosecutions of corruption would restore some legitimacy to government, as it is obvious that government's policing and judicial activities in this area appear to be 'barking but cannot really bite'. Some immediate measures would be to protect whistle blowers through legislation and make public disclosure of the assets of public figures mandatory. Furthermore, public assets acquired corruptly should be recovered by the State. These measures are imperative, as it is now common knowledge that the PNG economy is bedeviled by widespread corruption.
- Improving governance through developing widespread understanding of laws and ethical and moral values. Awareness campaigns should be carried out to inform people of the difference between traditional obligations (the 'big-man' system and its pressures and implications) and obligations towards the State and private business, in terms of their relevant laws, regulations and industry codes of conduct and ethical standards.
- Channeling oil revenues into the non-oil export sector, mainly the agricultural sector in line with the government's new 'green revolution' initiative. It is in this sector that Papua New Guinea has a comparative advantage (Duncan 2000:41). Oil revenues should also be channelled into sustainable fisheries, forestry and tourism activities, especially eco-tourism. The effective reactivation of the non-oil export sector will culminate in a broader tax base for government as well as increased employment opportunities.
- Channelling oil revenues into maintaining existing infrastructure and possibly building new roads, bridges, airstrips, wharves, schools, rural water supplies and communication and electrification projects in lieu of cash handouts to project area individuals. Such measures have been adopted by the Canadian province of Ontario for its oil revenues (Koyama 2004:30; Ojameruaye 2004:9). Improved infrastructure would facilitate the implementation of the 'green revolution' policy by opening up markets as part of the national government's export-driven economic recovery strategy.<sup>14</sup>
- Curtailing excessive and frivolous spending during periods of high oil prices and borrowing or 'austerity measures' during periods of low oil prices. This should minimise distortions and dampen unnecessary fluctuations



or oil price related volatility. One way to do this is to have 'permanent' or fixed income expectations from which spending is drawn. Budgets should be drawn up from a 'surprise free' oil price assumption. Excess revenue from oil can be placed in a stabilisation account managed by reputable commercial fund managers and ideally kept offshore in government securities and equities. If we have learnt anything from the experience of the PNG Mineral Resources Stabilisation Fund we know this is imperative. Government can then draw money from such an account into its annual budgets from time to time or use these savings to retire public debt (Duncan 2004:138; Stiglitz 2004:172).

- Finally, but not least, ensuring that government policies and expenditure should be pro-poor in order to reduce poverty. Government has to put 'its money where its mouth is' to help the poor. Government programs in this area should ensure that they are not hijacked by people with vested interests or those who are bent on cornering funds that are supposed to be spent on the poor to enrich the already rich.

## Conclusion

This paper has considered the problems of the 'curse' of oil and what is here termed the PNG disease with its accompanying collateral manifestations from a narrow (Southern Highlands Province) perspective as well as from a broad perspective (Papua New Guinea). To overcome the PNG disease and to steer away from the curse of oil, a holistic approach is required by the three tiers of government, individuals, civil society and the private sector working in collaboration in the adoption of the above

antidotes and others that may be deemed necessary. The problems are more political and social than economic and so the curse and disease can be overcome only if government has the political will to overcome them at a time when the disease is prevalent but probably not yet in a malignant form.

## Notes

- <sup>1</sup> A quote from Juan Pablo Alfonzo cited in Gary and Karl (2003:19).
- <sup>2</sup> Deteriorating health services, community schools, elementary schools and vocational schools are a source of major concern in the Southern Highlands Province. Crime is rising and police are often powerless. Underlying this decline of services is wide-scale misappropriation, maladministration, a dysfunctional public service, collapse of local-level government, and breaches of sound governance at provincial level. Proliferation of weapons is a related concern. These include high-powered weapons in the hands of certain individuals and their supporters and intimidation of the public and rival groups. Potential consequences for the Southern Highlands are horrendous. The Southern Highlands will continue the downward spiral of services, peace, infrastructure and commerce (*Post-Courier*, 5 August 2004:11).
- <sup>3</sup> 'Southern Highlands Province on the brink: Government fears collapse of province, takes tough administrative measures', *The National*, 13–15 August 2004:1–2.
- <sup>4</sup> The term 'PNG disease' in this context specifically refers to the negative experiences (negative externalities) of the Southern Highlands Province as a consequence of the management and utilisation of resource rents from petroleum projects. Hence, the term should not be taken out of context to draw parallels with experiences in the use of agriculture, mining, forestry and fisheries resources, and their resource rents, in other parts of Papua New Guinea. For instance, resource rents from the Porgera Gold mine



- accruing to the Enga Provincial Government appear to have been prudently managed.
- <sup>5</sup> The extended well testing program was conducted whilst the Moran field was still under a petroleum prospecting licence (PPL) during the exploration phase.
- <sup>6</sup> The scheduling of payments is dependent on the administrative capacity of the Department of Petroleum and Energy (royalties) and the Mineral Resources Development Company (equity dividends).
- <sup>7</sup> Compensation payments are calculated from the rates dictated by the Valuer General's compensation assessment schedule.
- <sup>8</sup> A short discussion on the failure of most of these types of businesses can be seen in Koyama (2004:26–8).
- <sup>9</sup> The Kutubu Development Authority was the predecessor to the Kutubu Special Purpose Authority.
- <sup>10</sup> The author first heard this description of corruption used by Sir Mekere Morauta during an interview with a reporter in a SBS documentary about corruption in Papua New Guinea in the mid 1990s. Systemic, because corruption has invaded the whole process of policy and decision-making and, systematic, because it is organised and highly sophisticated (Windybank and Manning 2003:4).
- <sup>11</sup> The Southern Highlands provincial government financial functions were transferred to the National Department of Finance in Waigani as a consequence of alleged misapplication of public funds when financial responsibility was formerly vested with the Southern Highlands provincial government.
- <sup>12</sup> A parallel can also be drawn in the case of HIV / AIDS between Papua New Guinea and Sub-Saharan Africa, in terms of its prevalence and spread. The similarity between HIV / AIDS and the 'PNG disease' is that both may be considered as developmental epidemics, as their prevalence has varying adverse implications for the economy and its development aspirations.
- <sup>13</sup> See <http://www.publishwhatyoupay.org>
- <sup>14</sup> In its 2005 Development Budget, the government has identified four key Impact Programs: Transport Infrastructure Rehabilitation and Maintenance; Export Promotion and Income

Earning Opportunities; Public Sector Reform and Governance; and Access to Basic Education and Health. The government is allocating 63 per cent of a total of K280 million in its Development Budget towards infrastructure maintenance (priority area one) whilst 37 per cent is shared amongst the other three areas. A large proportion of the K176 million (63 per cent) allocated for infrastructure maintenance will be used for the newly introduced District Roads Improvement Program (*Post-Courier*, 'PNG Government 2005 Budget Report', 17 November 2004:1–5).

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