PNG FORESTRY REVIEW TEAM

AUDITING FORESTRY PROJECTS CURRENTLY "IN PROCESS" FOR COMPLIANCE WITH THE REQUIREMENTS OF THE POLICY, THE FORESTRY ACT AND OTHER REGULATIONS AND GUIDELINES

To: Government of Papua New Guinea
C/- The Interagency Forestry Review Committee
Office of the Chief Secretary to Government

From: Review Team

Date: 5 March 2001

Re: **INDIVIDUAL PROJECT REVIEW REPORT NUMBER 30**

HEKIKO (GULF PROVINCE)

AUDIT CONCLUSIONS AND RECOMMENDATIONS:

RESOURCE AND PLANNING ISSUES:

The sustained timber yield principle has been complied with. The project is not in compliance with the Act in that it is not listed in the National Forest Plan for development. Sensible operational procedures have not been complied with in that there has not been any field volumetric inventory. A very significant proportion (38%) of the forest is classified by the Office of Environment and Conservation as "fragile". The estimated sustainable annual cut is not sufficient to support a conventional stand alone log export project (or a financially efficient logging operation if "fragile" forests are excluded from logging). The right of the PNGFA to implement conservation set asides as provided for in the Forest Management Agreement (and the consequences there-of) has not been bought forward into the Project Agreement.

LEGAL COMPLIANCE:

The decision to base the project on the Turama Block 1 Forest Management Agreement was ill-advised. Subsequent attempts to regularise the Forest Management Agreement documentation was not handled with competence. In other respects due process has generally been observed.

LANDOWNER ISSUES:

Awareness raising in the project area was conducted by a number of agencies resulting in confusion and too little specific information relating to the forestry project. ILGs have fractured into family groups resisting significant efforts by the PNGFA to rectify the situation. The situation with regard to the Forest Management Agreement is confused since there is no specific agreement for the Gulf portion of the Hekiko project area. There is no evidence of landowner involvement in the Development Options Study, the Project Guidelines or the Project Agreement.

RECOMMENDATIONS (INCLUDING CORRECTIVE MEASURES IF REQUIRED):

- That the actions taken to terminate the Project Agreement are appropriate and should be pursued without delay.

- That the PNGFA and Office of Environment and Conservation negotiate a position regarding the harvesting of Fragile Forests for inclusion in the Logging Code of Practice.

- That the request by some ILGs to become part of the Turama project should be considered and acted upon, after legal advice has been obtained.

If a decision is made to further pursue this project then:

- That the legal status of the Integrated Conservation and Development Project agreement between the State and an NGO be determined and it's impact on a potential forestry project clarified.

- That the PNGFA undertake proper volumetric inventory.

- That the PNGFA update the National Forest Plan.

- That the PNGFA ensure a firm contractual basis for the project by the execution of an appropriate Forest Management Agreement.

- That the PNGFA take advantage of the social mapping and ILG incorporation work undertaken in the area by the Chevron Oil company.

- That there be continued efforts to fully involve landowners in informed decision making.

Note: The individual project reports summarise the findings of the Review Team regarding material compliance issues, and present project specific recommendations for the consideration of the Interagency Forestry Review Committee. Separate reports produced at the end of the review process set out in more detail the audit procedures applied, and comments and recommendations regarding existing policies, legal requirements and project development processes.

REVIEW REPORT

SUMMARY PROJECT DETAILS:

Project type:	Forest Management Agreement / Timber Permit
Processing stage:	Formation of Incorporated Land Groups (ILGs) completed. Forest Management Agreement executed. Development Options Study completed. Project Guidelines completed. Developer selected (Yeungs Group Enterprises Ltd) and Project Agreement executed. Environmental Plan submitted but rejected (twice). Recommendation to the Board to terminate the Project Agreement.
Gross FMA area:	196,000 ha
Gross loggable area:	65,000 ha (a)
Net sustainable timber yield:	Not able to be calculated as no inventory undertaken within the project area – background notes are presented in Appendix 1. Project Guidelines set out a sustainable yield estimate of 35,000 m3/a.

(a) Based on data from the PNGFA FIMS database.

A. FORESTRY AND PLANNING ASPECTS

1. SECTORAL PLANNING AND CONTROL	
PROVINCIAL FOREST PLAN • PNGFA Board endorsed Provincial Forestry Plan exists: • Is the Provincial Forestry Plan current: • Is the Project listed in the Provincial Forestry Plan: NATIONAL FOREST PLAN • Is the Project listed in the National Forest Plan as required under s54 of the Act:	Yes No – expired January 2000 No No

2. PROJECT DEFINITION IN FMA DOCUMENT	**Note**: There is no FMA document for the Gulf portion of Hekiko. The PNGFA assumes that the area has been acquired under the Turama Block 1 FMA Part 1. The project area is defined in Turama Block 1 FMA Part 2.
• Is the gross loggable area properly defined:	Unclear. The map in the Turama Block 1 FMA (Part 2) indicates a gross loggable area 63,000 ha based on the application of the logging exclusion areas defined in the PNG Code of Logging Practice 1996. The map in the draft Hekiko (Southern Highlands) FMA indicates a gross loggable area of 61,000 ha for the Gulf Province portion. The FIMS data indicates a gross loggable area of 65,000 ha. Applying the standard 15% reduction factor indicates a net loggable area of about 54,000 ha. The Environment Plan produced for Yeungs Group notes a gross operable area of 66,000 ha, but treats this as if it is net. The project area is subject to an Integrated Conservation and Development Project

	agreement between the State and an NGO. As this is not gazetted, it's status is unclear.
• Has the total gross merchantable volume been properly estimated:	No. There was no inventory in this project area (see notes presented in Appendix 1). PNGFA have inappropriately applied data from an inventory undertaken in the Southern Highlands portion of the Hekiko area. The Environment Plan produced for Yeungs Group presents data for a 0.05% sample undertaken by the developer which indicated a gross volume of 33.6 m3/ha.
• Has the net merchantable volume been properly estimated:	No. The volume data used to estimate the net volume is considered unreliable (see notes presented in Appendix 1). The Development Options Study indicates a net harvestable volume of 1.2 million m3. This is later raised to 1.9 million m3 in a paper to the PNGFA Board based on a small area addition. The Environment Plan produced for the Yeungs Group indicates 2.2 million m3, but is based on gross area – corrected for this the figure would be 1.9 million m3.
• Have "Fragile Forest Areas" (OEC definition) been considered:	No, because there is no agreed position regarding fragile forest areas. An estimated 38% of the gross loggable area of the Hekiko (Gulf portion) project is classified as Fragile Forest.
• Have environmentally sensitive areas been considered:	Yes. Large scale Gazetted conservation areas are excluded from the FMA area. Small scale Gazetted conservation areas are identified and excluded from the gross loggable area. The Logging Code prohibits logging in defined environmentally sensitive areas which are excluded when the gross loggable area is defined.
• Have conservation set asides been appropriately implemented:	No. Whilst the standard FMA document reserves the right for the PNGFA to exclude up to 10% of the gross loggable area from logging for conservation purposes, this right (and its potential consequences) has not been carried forward into the Project Guidelines or the Project Agreement.

3. **ESTIMATE OF SUSTAINABLE CUT**	
• Has the sustainable annual cut been properly calculated:	Questionable given the doubts regarding the volume per hectare estimate. The Project Guidelines indicate 35,000 m3/a. The Board recommended a reduction to 24,000 m3/a. The Project Agreement permits 53,000 m3/a subject to a "re-survey" (see notes presented in Appendix 1). If the area classified as Fragile Forest is excluded then the estimated sustainable cut will be reduced by about 38%. In the Environmental Plan prepared for the Yeungs Group the company proposes to cut 63,000 m3/a for the first 10 years and 23,000 m3/a there-after.
• Is the estimated sustainable yield sufficient to support a financially efficient logging investment (min 30,000 m3/a):	Uncertain but probably yes.
• Is the estimated sustainable yield sufficient to support a stand-alone log export operation (min 70,000 m3/a guideline set by PNGFA Board):	No

4. **CONSISTENCY BETWEEN DOCUMENTS**	
• Is the area and volume data consistent between the FMA, the Development Options Study, the Project Guidelines and the Project Guidelines:	The resource data underlying this project is questionable. No inventory work was undertaken. There is no FMA document. The DOS and Project Guidelines are consistent. The Project Agreement sets out a significantly increased allowable annual cut subject to "re-survey". The Environmental Plan prepared for the Yeungs Group proposes a cut higher for the first 10 years than that set out in the Project Guidelines, or that set out in the Project Agreement.

• Any other material inconsistencies regarding the resource:	None found.

5. ANY OTHER MATERIAL NON-COMPLIANCE REGARDING THE RESOURCE	
• The standard cutting cycle assumed in the sustainable annual cut calculation.	The National Forest Policy specifies a 40 year cutting cycle. In practice a 35 year cycle is applied. No explanation is available.

RECOMMENDATIONS REGARDING FORESTRY ASPECTS:

1. SECTORAL PLANNING AND CONTROL

- That the PNGFA update the National Forest Plan.

- That the PNGFA pro-actively assist the Gulf Provincial Government update their Provincial Forest Plan (s49), and facilitate the inclusion of the updated Provincial Forest Development Programme (s49(2)(b)) into the National Forest Development Programme (s47(2)(c)(ii)) as required under the National Forest Policy (Part II (3)(b)) as the basis for the PNGFA's acquisition and allocation programme.

- That the PNG Government direct the OEC and the PNGFA to determine a formal position on whether Fragile Forest Areas (OEC definition) may be logged, and incorporate the agreed position into the Logging Code.

2. PROJECT DEFINITION

- That the PNGFA begin again with this project by undertaking volumetric field inventory within the project area to provide sound volume information for project planning.

3. ESTIMATE OF THE SUSTAINABLE CUT

- That the PNGFA calculate a sustainable cut estimate based on sound volumetric inventory as the basis for considering project development options.

4. ANY OTHER MATERIAL NON-COMPLIANCE REGARDING THE RESOURCE

- That the PNGFA either base their sustainable cut calculations on a 40 year cutting cycle (as required under the National Forest Policy) or provide justification for adopting a 35 year cutting cycle.

B . LEGAL COMPLIANCE

SUMMARY OF LEGAL COMPLIANCE:

- Basing this project on the adjoining project area's Forest Management Agreement is entirely inappropriate. The subsequent attempts to add two more Forest Management Agreements to Turama Block 1 (as intended amendments of the original agreement) was not done in a competent manner.

- The allocation of the project to Yeungs Group Ltd raises a number of concerns. It is a company with a paid up capital of K 2.00 and with no experience in the forestry sector. It provided no financial information and identified no markets. It had been involved with purported landowner representatives for many years in ways that tend to compromise due process.

A full compliance checklist and some additional notes are presented in Appendix 2.

RECOMMENDATIONS REGARDING LEGAL ASPECTS:

1. That if the project is to proceed then it must be put on a sound contractual footing. The wishes of certain ILG's to join the adjoining Turama Extension project must be considered and properly actioned.

2. The recent action by the PNGFA to terminate the Project Agreement is entirely appropriate and should be pursued without delay, after proper legal advice has been obtained.

C. LANDOWNER ISSUES

RESOURCE ACQUISITION	
1. Landowner Awareness	
The Review Team was looking for evidence of an awareness package containing information explaining the purpose, benefits and otherwise to be expected from the project. This could include general conditions that could be used for all prospective projects.	The Gulf Province portion of the Hekiko timber resources were originally part of Turama Block 1 FMA. A Landowner Company (LANCO) Keko Resources was formed representing Fogamaiu to Bosavi, being the Southern Highlands portion of the resource. The SH landowners, represented by ICRAF, declined to be involved until resource inventory was conducted and bio-diversity areas defined. In April 1997 Dihau Resource Investments Ltd was formed to represent people from Siawiti in the Gulf Province.

2. Landowner Mobilisation	
Landowners are required to be mobilised by means of the Land Groups Incorporation Act. The Review Team was looking to find evidence of full participation by landowners in the ILG process particularly with regard to: • **Recognition that the resources are owned by individual land groups and not collectives of land groups** • **The formation of representative bodies for project consultations and negotiations.**	In 1996 Keko Resources Ltd state that there were 45 landholding clans in SHP. Benjamin Wabua claimed to "represent" the Gulf Hekiko landowners. The ILGs along the Kutubu oil export pipeline were originally done by oil company Chevron. Later the PNGFA became involved and facilitated additional ILGs for forestry purposes. No reconciliation was done and there is almost certain overlap between the ILGs. Following the original incorporation ILGs have inappropriately broken into family groups who have been able to become registered as an ILG as a result of a lack of any scrutiny on the part of the office of the Registrar of Titles. The PNGFA has conducted an extensive review of the ILGs from Turama Block 1 FMA which is purported to include the Gulf portion of Hekiko. The review is a strongly critical in-house assessment of the process of setting up ILGs under the Land Groups Incorporation Act for the purposes of forestry projects.
3. Forest Management Agreement	
Must Specify: • **Monetary benefits for the customary group** • **Area in agreement by map** • **PFMC certificate as to** - **authenticity of the tenure of the customary land** - **willingness of customary owners to enter into FMA** • **Review level of consultation with landowners**	PFMC signed the Schedule 6 certificate re tenure and willingness to sign agreement. Gulf landowners themselves drew up an alternative FMA and had it signed. This was not recognised by NFS which stated that the area was covered by the Turama Block 1 FMA. There is no FMA specific to the Gulf portion of the Hekiko project.

RESOURCE ALLOCATION	
1. Development Options Study	
The Review Team was looking to see if the Development Options Study: • **Catered for landowner concerns and aspirations and if** • **All options presented for the resource development had a realistic chance of being pursued.**	The DOS is a rather superficial documentation of the project area. It takes no account of the WWF scientific work, nor the fact that the oil pipeline and its access track runs right through the project area. The Landowner wish list is routine indicating little or no consultation with landowners. The project area already has benefited from provision of infrastructure by the Kutubu Oil project and some landowners are involved with the Gobe Oil project.
2. Project Guidelines	
Draft guidelines must be discussed and developed in consultation with the resource owners.	There is no mention of specific landowner expectations in the guidelines.
3. Project Agreement	
Authority is required to involve landowners in selection of the "developer" and in negotiation of the Project Agreements according to the terms of the FMA.	Project Agreement negotiated. No specific reference to landowner benefits other than an obligation to build an unspecified facility each year in accordance with the Provincial Government Plan. There is no evidence of landowner consultation in this process.
4. Environmental Plan	
EP is produced by the preferred developer according to the prescription of the Environmental Planning Act. Evidence of consultation with landowners is important.	EP presented to OEC twice and rejected both times.

Some additional notes are presented in Appendix 3.

CONCLUSIONS REGARDING LANDOWNER ASPECTS:

- Landowners have been exposed to a great deal of contact from developers, LANCOs, NGOs and Chevron field officers for some years but this contact has been uneven in different parts of the project area and it is not clear that adequate information has been made available relating to the specific project proposed.

- The ILGs in this area have suffered from several areas of confusion:

    - The prior Chevron ILGs which covered part of the area were overlaid with new ILGs covering the same people for the purposes of the FMA.
    - The original ILGs have fractured into family groups creating confusion and potential inequality in benefit distribution.
    - Claims keep surfacing that ILGs have been left out of the process.
    - The frequent movements of ILGs from the Hekiko FMA to the Turama FMA and vice versa makes it very difficult for NFS to monitor and manage the ILGs.

- These problems have resulted in three FMA documents none of which is specific to the Hekiko (Gulf) land area.

- NFS undertook a review of the ILGs in the Turama FMAs but concluded that the effort was in vain given that "landowners were not telling the truth". Family ILGs were still being proposed during the vetting process.

- This project illustrates a complete breakdown of the use of the Land Groups Incorporation Act that an agency like NFS cannot rectify on its own.

RECOMMENDATIONS REGARDING LANDOWNER ASPECTS:

1. That the Government must address the breakdown in the use of ILGs as it affects all forestry projects as well as mining and petroleum projects.

2. That Social Mapping of the project area should precede land group incorporation.

3. That given Chevron Niugini Ltd has conducted a considerable amount of social mapping for this area, that this particular project be retrofitted by a combined effort by Government, Chevron and the PNGFA.

APPENDIX 1 : COMMENTS ON THE RESOURCE ESTIMATES

Chain Of Events and Resource Data:

March 1988 – TP 2-12 Turama granted on the western side of Gulf Province to Turama Forest Industries Ltd (under their former name Long Term Trading Ltd). Twenty year term, unsustainable cut.

March 1991 – Then Department of Forests inventory exercise in the area to the east of TP 2-12. A total of 21 x 0.2 ha plots (or a total 4.2 hectare sample). The gross volume of sawlogs is estimated to be 34.075 m3/ha. The precise location of the field work is not known. This is a minute sample which is later applied to a gross loggable area of 136,400 ha, indicating a 0.003% sample.

1994/95 – PNGFA facilitates the setting up of Incorporated Land Groups and signs a Forest Management Agreement over a large area immediately to the east of TP 2-12. The area is labelled as FMA Block 1 (of three) of the West Gulf Province Timber Supply Area. The rights to all the timber in this area are indicated to Turama Forest Industries Ltd as a supply area for a processing facility they are planning in response to Minister Neville's direction that all log exporters should do so. The gross area of Block 1 is 539,400 ha, and the estimated net loggable area is 136,400 ha (as shown on the map in the FMA document). The Timber Supply Area concept is later discontinued on instruction from the National Executive Council on the basis that it does not provide for any landowner input into the decision as to who will harvest their timber. It is agreed that Turama Forest Industries will proceed to develop the area under a Timber Permit issued under the then new Forestry Act 1991.

The FMA document is incomplete in that Schedule 4 "Estimated Volume Of Timber" is not completed. Whilst a gross volume per hectare of 34.075 m3/ha is set out, there is no loggable area data or an estimate of the total loggable volume. The gross volume per hectare figure is identical to that determined by the minute inventory undertaken in 1991.

1995/96 – Reaction against the FMA by politicians on the basis that it includes the Gulf Province part of an area referred to as Hekiko, where a competing developer has indicated his plans to set up a forestry project. The Hekiko area also includes part of the Southern Highlands Province (which is not covered by the Turama Block 1 FMA). The PNGFA prepare a second FMA for the Turama Block 1 area (finally approved by the Minister in 1998), which purports to exclude the Hekiko area. The map in this document indicates that the "excluded" Hekiko area is 195,727 ha, of which the net loggable component is 63,197 ha. It also indicates that the "revised" Turama Block 1 FMA area is now 337,073 ha including a net loggable area of 169,159 ha. Schedule 4 "Estimated Volume Of Timber" sets out a net loggable volume of 23.843 m3/ha (being a gross volume of 34.075 m3/ha adjusted by a standard volume reduction factor of 30% to allow for defects). The gross volume per hectare figure is identical to that determined by the minute inventory undertaken in 1991.

November 1995 – Hekiko Forest Products Pty Ltd (90% owned by Yeungs Group Enterprises Ltd) submits a proposal covering both portions of the Hekiko project area. It is based on an unsustainable proposed cut of 416,000 m3/a for 20 years. The report presents the results of inventory work undertaken by the company based on 79 plots totalling 15.8 hectares. The indicated gross volume per hectare is 63 m3. Applying the standard gross to net reduction factor of 30% indicates a net volume of 44 m3/ha. The company's proposal is based on a net volume of 48 m3/ha, which is subsequently reduced by a further 25% as an "allowance for sampling error and defects" indicating the company's expectation of harvesting on average 36 m3/ha. This inventory information does not appear to have been further used, either by the company or the PNGFA.

The company set out the same resource information in an Environmental Plan prepared at the same time (November 1995).

1996 – Based on the concept of developing both the Southern Highlands and Gulf Province portion of the Hekiko area as a single project, the PNGFA undertake inventory work in the Southern Highlands portion. The gross area of this portion is 429,400 ha, and the estimated gross loggable area is 131,240 ha. Some 1428 0.1 hectare plots are measured within the gross loggable area (0.109% sample). Gross sawlog density (50 cm diameter at breast height or above buttress or greater) is estimated to be 80.494 m3/ha.

September 1996 – PNGFA produce an inventory report setting out the resources of the Hekiko area. The gross loggable area in the Southern Highlands and Gulf Province portions are stated to be 54,870 ha and 61,400 ha respectively. A non-standard area reduction factor of 30% is applied to estimate the net loggable areas which are 38,409 ha and 42,980 ha respectively, and add to 81,389 ha. The standard reduction is 15%.

To estimate the loggable volume, the net loggable area is multiplied by a gross volume per hectare estimate of 40.246 m3/ha. On this basis the loggable volume estimate for the Southern Highlands portion is 1.545 million m3, and that for the Gulf portion is 1.729 million m3. The text of the report sets out sustainable yield estimates based on a 35 year rotation - 44,000 m3/a for the Southern Highlands portion and 49,000 m3/ha for the Gulf portion.

In commenting on the forest inventory the text of the Inventory Report states that "The original results of the forest inventory indicate that there is a stocking of 80.492 m3 per hectare of sawlogs …… Due to factors related to the collection of samples the results were reduced by 50% to arrive at a conservative estimate which are …….. 40.246 m3/ha for sawlog". The gross volume per hectare figure (80.492 m3/ha) is that derived from the inventory undertaken in the Southern Highlands portion of Hekiko earlier in 1996. As well as having been reduced by 50%, the data has thus been applied to all of the Hekiko area, including the Gulf portion. PNGFA uncertainty regarding the resource is further illustrated by the statement that "There have been suggestions that the above [sustainable cut] figures should be reduced by a further 30% as experience from adjacent areas show that the volume that is extractable is lower than that of the inventory".

Applying the standard gross to net volume reduction factor of 30% to the above gross volume per hectare estimates results in sustainable yield estimates of 31,000 m3/a for the Southern Highlands portion, and 35,000 m3/a for the Gulf Province portion.

About 1996 – In order to develop Hekiko area as a single project, the PNGFA proceed to acquire the Southern Highlands portion under an FMA. The PNGFA consider that they have already acquired the Gulf portion under the earlier Turama Block1 FMA. A draft FMA for the Southern Highlands portion was prepared. Schedule 4 "Estimated Volume of Timber” shows a volume per hectare figure of 40.25 m3, which is that indicated in their September 1996 forest inventory report. A hand written note sets out the instruction to “please apply reduction to m3/ha as well as the area” indicating that the 40.25 m3/ha is to be treated as a gross volume per hectare figure, and that the sustainable yield estimate is to be based on 28.18 m3/ha after the application of the standard 30% gross to net volume reduction factor. This would be 35,000 m3/a as calculated above.

1996 – At some point it was decided that developing Hekiko as a single Trans-Province project was not politically acceptable and the PNGFA proceeded to progress the Gulf portion as a stand alone project. A Development Options Study was prepared. This sets out the same estimate of the net loggable area as that presented in the September 1996 forest inventory report (42,980 ha), and applies the gross volume estimate of 40.246 m3/ha also sourced from that report. The standard 30% gross to net reduction factor is applied, and the sustainable yield is estimated to be 35,000 m3/a.

1996 – The PNGFA also prepared the Timber Project Guidelines, which reiterates the resource data set out in the Development Options Study.

August 1996 – The Hekiko (Gulf Portion) project was advertised on the basis of an available annual sustainable cut of 35,000 m3/a. Only one proposal was received, from Yeungs Group Enterprises (PNG) Ltd, which ignores the sustainable cut set out in the Project Guidelines, and is instead based on an annual cut rising to 100,000 m3/a in year three and 160,000 m3/a in year 5. The PNGFA’s evaluation of the proposal notes the discrepancy with the available sustainable cut and labels the proposal as “unrealistic”. It also notes that “the proponent has no record or experience in the forest sector in the country”. These comments would seem to be a solid basis for not accepting the proposal or the proponent. However the evaluation concludes that “Yeungs Group Enterprises (PNG) could be considered for the project since it is the only proponent” or alternatively that the project should be re tendered. In the event the Gulf PFMC selected Yeungs Group Enterprises Ltd as the preferred developer, and duly advised the PNGFA Board.

In January 1997 the PNGFA Board wrote to the Gulf PFMC advising it that “the Minister considers that an agreement should be negotiated with Yeungs Group Enterprises”, and further that “the Minister has advised the Board that he expects immediate action” and that “undue delay would have obvious effects on the allocation procedures and the interests of resource owners”. It is unclear what the effect on the allocation procedures might be.

In the same letter the PNGFA Board directed the PFMC to “request the proponent to recast its proposal on the basis of an annual sustainable log harvest of 24,000 m3”. The reason for the Board deviating from the sustainable yield set out in the Timber Project Guidelines on which the proponent had based his proposal is not clear, but it is assumed that the Board felt it had good reason. The reduction suggested by the Board is 30%, and may have derived from the comment in the September 1996 forest inventory report that there had been suggestions that the sustainable cut should be reduced by “a further 30% as experience from adjacent areas show that the volume that is extractable is lower than that of the inventory”. However the comment in the forest inventory report applied to a sustainable yield estimate of 49,400 m3/a, and a 30% reduction had already been applied to derive the 35,000 m3/a estimate included in the Project Guidelines. The Board was thus suggesting a second 30% reduction, and the realisation of this fact may explain why the Board did not further pursue the matter later (see below).

In January 1997 the PFMC resolved "not to go by the National Forest Board's decision to reduce the annual sustainable log harvest of 35,000 m3 to 24,000 m3 …… as such would be uneconomical in view of the fact that the developer intends to go into downstream processing after three years".

In February 1997 the PNGFA Board directed the Gulf PFMC to "enter into negotiations with Yeungs Group Enterprises (PNG) Ltd with a view to negotiating a project agreement on the basis of an annual log harvest of 35,000 m3". The earlier suggestion by the Board that the sustainable yield be reduced to 24,000 m3/a does not appear to have been further pursued.

April 1997 – The negotiating committee considered a draft Project Agreement. The discussion records note that:

- The issue of the level of cut is considered "contentious".
- The proponent argued strongly that 35,000 m3/a is "uneconomically viable" and "insisted" that the cut be increased.
- That an area of 5,840 ha had been added to the project area (being areas withdrawn from the Turama Block 1 FMA).
- That "The new annual allowable cut of 53,000 m3 is based on the increased area …….".

(This would seem technically questionable. If an additional 5,840 hectares were to support an increase in the sustainable annual cut of 18,000 m3/a, then the implied net harvestable volume per hectare for the additional area would need to be 108 m3/ha. The equivalent gross volume per hectare (based on the standard 30% reduction factor) would need to be 154 m3/a, which is unheard of for PNG natural forests. This also assumes that the entire 5,840 is covered with harvestable forest, and is not in any way excluded from harvesting by virtue of being devoid of forest, or under the logging exclusion criteria set out in the PNG Logging Code of Practice 1996.)

Subsequently the PFMC "endorsed the revised annual cut from 35,000 m3 to 53,000 m3" and "recommended to the National Forest Board to direct the proponent to submit the cash flow analysis based on the revised annual cut of 53,000 m3".

The minutes of the **30 April 1997** meeting of the PNGFA Board notes some discussion of the change in the allowable annual cut. The Board confirmed its view that the "question of sustainability would not be changed". The PNGFA member of the negotiating team noted that "the proponent company said it would be unviable to operate on a cut of 35,000 m3. As a result, the area released by TFI was taken into consideration and with reductions a new allowable cut was calculated at 53,000 m3".

A compromise solution appears to have been adopted in that the Project Agreement includes a requirement for a "re-survey", and a Board member suggested that the annual allowable cut set out in the Project Agreement should be linked to the survey results. This was accepted by the Board, which then also accepted the variation in the Project Agreement from an annual allowable cut of 35,000 m3 to 53,000m3.

May 1997 – Project Agreement is executed. It sets out the allowable annual cut as 53,000 m3/a (Clause 6). It also sets out the requirement (Clause 8) that "The Authority and the Company hereby agreed to a joint re-survey of the project Area as to available volumes of logs for commercial production on a sustained yield basis with a view to revising the annual allowable cut on a date to be determined at the convenience of both parties and solely at the Company's cost". A stronger position would have been for the PNGFA to insist on the re-survey and the re-assessment of the permitted annual cut before any harvesting was permitted to begin.

December 1997 – The selected Developer, Yeungs Group Enterprises Ltd, submitted an Environmental Plan to the Office of Environment and Conservation. This sets out volume per hectare information based partly on the volumetric inventory undertaken by the PNGFA in the Southern Highlands portion of the Hekiko area, and partly on an inventory undertaken on behalf of the company. The latter indicates a gross volume of 33.6 m3/ha based on a 0.05% sample.

The Environmental Plan indicates that the company intends to log 63,000 m3/a for the first ten years, which is in excess of both the sustainable cut specified in the Project Guidelines (35,000 m3/a) and that subsequently agreed to by the PNGFA for inclusion in the Project Agreement (53,000 m3/a). The 63,000 m3/a is based on gross area and the gross volume per hectare information obtained from the company's inventory. Clearly the company is continuing it's campaign to try and secure a higher annual allowable cut.

<u>Comments:</u>

It is clear from the above chain of events that the PNGFA resource estimates for the Hekiko (Gulf portion) were based entirely on inventory work undertaken in the Southern Highlands portion. Even then the inventory sample was very small, and the PNGFA considered the results so unreliable that they applied an arbitrary 50% reduction to the calculated results. Consequently the original estimate of sustainable yield of 35,000 m3/a must be considered unreliable. It would appear that the Board had doubts regarding the timber resource when it directed the PFMC to direct the developer to resubmit its proposal based on a more conservative 24,000 m3/a.

The only way to obtain a reliable estimate of the sustainable yield for a project area is to undertake a proper volumetric inventory achieving a 1% representative sample. To do this after a developer has been given the contractual right to harvest the resource would seem to be inadvisable as:

- The PNGFA lays itself open to claims that it has misrepresented the forest resource when it called for tenders;
- It undermines the industry and public perception of the PNGFA as a professional organisation "in charge" of the commercial forestry sector in PNG; and
- There is no guarantee that the selected developer would have submitted the best proposal if the true extent of the loggable resource was known.

It would also seem that the PNGFA Board has the right to assume that resource information presented to it by the National Forest Service is reliable, unless it is informed otherwise.

<u>Postscript:</u>

At its meeting 69 in November 2000, the issue of the Hekiko (Gulf Portion) was further considered by the Board. The “Facts” set out in the Board Paper claim that the annual allowable cut is 53,000 m3/a, and that the estimated resource is 1.9 million m3. This is merely the allowable cut multiplied by 35 years, and no mention of the earlier “contentious” resource issue is made. The paper goes on to note:

- That in December 1997 Yeungs submitted an Environmental Plan to OEC which OEC gave Conditional Approval.
- That the developer submitted a Forest Working Plan which was rejected in 1998.
- That the Environmental Plan was rejected in 1998 as conditions were not met.
- That a further Environmental Plan was submitted to OEC in 1998 which was also rejected.
- That the PNGFA served Yeungs a “Notice of Intention to Terminate the Project Agreement” in March 2000, as certain terms and conditions of the Project Agreement had not been complied with.
- Based on Yeungs response to the Notice, the PNGFA allowed a grace period of 6 months.
- That the grace period expired on 2 November 2000.

The paper recommended that the Project Agreement be terminated.

The minutes of the Board meeting (Meeting 68 held in late 2000) indicated that the Board agreed to:

- Defer making a decision to terminate the permit; and
- Instructed the Managing Director to obtain legal advice from his Legal Counsel and the State Solicitor as to whether there are sufficient grounds to terminate the Project Agreement.

APPENDIX 2 : CHECKLIST OF COMPLIANCE WITH LEGAL REQUIREMENTS

PROJECT – HEKIKO (GULF PORTION)

Step	Compliance	Non-Compliance	Not clear
1. Landowner Consultation			
Awareness campaign			?
Vesting of title	N/A		
ILG incorporation			?
PFMC certificate	See notes		
Attendance of landowners at PFMC meeting			?
2. Forestry Management Agreement			
Form and content	See notes		
Execution	See notes		
Ministerial approval	See notes		
3. Development Options Study			
Board to arrange	August 96		
or exemption	N/A		
Directions from PFMC			?
DOS given to Minister and PFMC	September 96		
4. Project Guidelines			
PFMC consults with L/owners and Prov Govt			?
PFMC to prepare draft	Confirmed		
Attendance of landowners at PFMC			?

meeting			
PFMC to submit draft to the Board	16/10/96		
Board issues final guidelines			?
5. Advertisement			
Project to be advertised	26/9/96		
Expressions of interest received	(1) 26/11/96		
6. Feasibility Studies			
Application by registered person	N/A		
7. Project proposals			
Proponents must be registered under section 105	Confirmed		
Placed in tender box	Confirmed		
Proper as to form and content	Confirmed		
Referred to PFMC	Confirmed		
Attendance of landowners at PFMC meeting			?
Evaluated with assistance of NFS	Confirmed		
Invitation for further information			
Evaluation of further information			
PFMC reports and recommends	11/12/96 Form 20		
Attendance of landowners at PFMC meeting	1 present		
Board consults Minister	7/4/97		
Minister gives views	8/4/97		
8. Negotiations			
Board directs PFMC as to proponent for further negotiations	April 97		
Board and PFMC set parameters	7/3/97		

PFMC negotiates agreement	23/4/97		
PFMC submits final draft to the Board	23/4/97 Form 22		
Attendance of landowners at PFMC meeting	Confirmed		
9. Project Agreement			
Board considers draft agreement	30/4/97		
Finance Minister's approval sought	13/5/97		
Board consults l/owners, Prov Govt and MP's of the area	Confirmed Form 10		
Board may execute agreement	21/5/97		
Board recommends to Minister to grant Timber Permit			?
10. Timber Permit			
Minister invites party to apply			?
Application is made for TP			?
Application must have approved Environment Plan	Plans rejected twice		
11. General Policy Objectives			
Encouragement of on-shore processing	Clause 6		
Participation of Papua New Guineans	Clause 18		
Recruitment and training of local staff	Clause 10		
Creation of Joint Ventures	No provision		

CHECKLIST NOTES:

1. It is impossible to make sense of the Forest Management Agreements that are supposedly applying to this project. There is an assumption that the Turama Block 1 FMA forms the basis of this project. In this regard some observations regarding this FMA should be made:

- The Turama project is itself shrouded in some controversy. It has been the subject of an Ombudsman Commission report in which the PNGFA fared very badly. At Meeting 19 in May 1995 the Board made the remarkable decisions to exempt the project from advertising, to execute the Project Agreement and the recommend that the Minister grant a Timber Permit, all in the one breath.

- The subsequent attempts to deal with the Gulf portion of the Hekiko project under the Turama FMA are inexplicable. There are now three parts to the Turama FMA. Part 3 remains in draft form. All of these Parts are in the standard FMA format. If the later Parts are intended to add to and/or delete ILG's from the Turama project then this should be stated clearly in the text of the Agreements. It is impossible to determine the intent of Parts 2 and 3. The standard of the contractual documentation is a disgrace.

- It must be said that the NFS has been seriously remiss in the manner in which it has sought to progress this project on a wholly inadequate contractual basis. However care must be taken when directing the blame for this. In May 1997 the Divisional Manager – Resource Planning attempted to get the PNGFA project lawyer involved in resolving this. He made the request in a professional and timely fashion. He pointed to the need to resolve this before the proposed Project Agreement was signed. There is no indication of any response from Mr Maurice Coughlan, who held the position within the NFS of Projects Lawyer. Nothing was done to remedy the clear inadequacies. The Project Agreement was signed nonetheless.

- Even the landowners had realised the need to base this project on a workable FMA. In June 1996 they had attempted to draft and execute one themselves. This was summarily rejected by the NFS. The Service was correct to do this but it was to transpire that the landowner's attempt to secure a FMA was done in a more competent fashion than anything that the NFS project lawyer was able to achieve.

2. There is some evidence that landowner representatives were in attendance at some relevant PFMC meetings but it is equally clear that their attendance was not arranged at some important meetings.

3. There is no evidence of consultation with landowners and the Provincial Government concerning the drafting of the Project Guidelines. The Development Options Study contains a section relating to the "Development Wishes of Landowners" but it has little detail of real substance.

4. The fact that the advertisement was placed before the Project Guidelines were even drafted could be seen as a breach of due process and an inappropriate attempt to "fast track" the project.

5. The almost automatic decision to grant the project to Yeungs Group Ltd must also be questioned. The following matters are noted:

- Yeungs Group Enterprises (PNG) Pty Limited, according to its registration with the PNGFA, is a classic K2 company. It is simply nonsense to allocate such a large commercial operation to a company with no financial basis.

- As far back as 1994 the company was mobilising landowners and enlisting their support. They have been intimately involved with a purported landowner company, Hekiko Timbers Limited. A company check indicates that Hekiko Timbers Ltd is 90% owned by Yeungs Group Ltd.

- In June 1995 the Papua New Guinea High Commissioner in Malaysia wrote a letter noting that a Malaysian Company had been invited by Yeungs to participate in the project. This was well in advance of Yeungs securing any operating right. In fact not a single step in the process had been undertaken at this time. It raised the clear suggestion that Yeungs was intending to deal with the project in a broker capacity.

- The company had no experience at all in the forestry sector within PNG and no known experience outside the country.

- Its proposed annual cut was nearly three times greater than the figure stated in the Project Guidelines. No details of the company's financial position were given. No project financial information was provided. No markets were identified. Even though the appraisal suggested that the proposal was "unrealistic" no serious consideration was given to any other path than the granting of the rights to Yeungs.

6. The project has not become operational because the company has not secured approval for its Environment Plan. In fact it has submitted two Plans and both have been rejected. The first was given "interim approval" for six months by a former Minister. This dubious procedure was described by a subsequent Minister as "unprecedented". And in rejecting the second Plan he noted that prosecution action might yet be taken due to the misleading information that the Plan contained.

7. In 1997 the company's 5 Year Working Plan was also rejected by the Managing Director.

8. It is hardly surprising that a number of ILG's have sought to be removed from the Hekiko project and to be brought back into the Turama project. Arguably they have never been part of anything other than the Turama FMA, but this requires very careful scrutiny and very considered remedial action.

9. The NFS has initiated action to terminate the Project Agreement. This is more than justified but such action must be taken on clear advice and without undue delay.

10. This project is a disaster. It is only fair to reiterate however that certain senior officers of the NFS were fully aware of the underlying problems surrounding the FMA and sought to involve the Projects Lawyer to overcome these. There is no evidence that these sensible requests ever resulted in the provision of sound

legal advice. In May 1999 Maurice Coughlan was finally sacked from the PNGFA having been charged with a number of counts of “negligence and incompetence”. The progress of this project was not the subject of any of these charges but it might well have been. Not long after Mr Coughlan was charged by the PNGFA, legal proceedings against him were initiated on behalf of the PNG Law Society. These proceedings alleged that he had represented himself to be a lawyer when he had not been admitted to practise in Papua New Guinea. Mr Coughlan avoided these proceedings by leaving the jurisdiction.

APPENDIX 3 : NOTES ON LANDOWNER ASPECTS

1 1 Oct 1996 - TFI get into the picture to try to arrange a 400,000 m3/a cut to satisfy the "demand of the landowners".

2 Urama Tribe landowners met with NFS over waterway compensation from TFI and RH. In the absence of any correct ILGs, payments made did not get down to the rightful people.

3 1.10.96 Dennis Hauka Lawyers state that they are representing the Gulf landowners.

4 30 Oct 96 NFS declined to advertise until SHP portion had been acquired.

5 EP prepared by two different consultants has been rejected twice by OEC. Reasons not given.

6 21 Mar 2000 NFS recommended that the Project Agreement be terminated.

7 May 1996 Gulf Provincial Government denied recognition of the Kikori ICAD vis-à-vis Hekiko project.

8 Landowners themselves drew up and signed an FMA. This was not recognised by NFS.

9 14.11.96 TFI was asked by NFS to release some portions of land from its Turama Block 1 FMA to Hekiko.

10 22.11.96 PNGFA General Manager advised Benjamin Wabua (landowner rep.) on the negotiation that was taking place with TFI.

11 23rd of May 1997, the General Manager of PNGFA wrote to the PNGFA General Counsel informing him that 37 ILGs that signed under the Turama FMA want to be separated and registered under the Hekiko FMA.

12 19th Jan.1998, Benjamin Wabua indicated to NFS landowner intentions to pull out from the Hekiko FMA and join the Turama FMA.

13 4th Jan. 2000, a letter from Waima Somila informing the MD of NFS that they are withdrawing 18 ILGs from Hekiko FMA to re-join the Turama FMA. The final outcome of this is not clear.

14 27th of March 2000, further indications by land groups supporting the Hekiko project that they want to withdraw and re-join the Turama project.