

The Inspection Panel

Report and Recommendation

on

Request for Inspection

Papua New Guinea: Governance Promotion Adjustment Loan (Loan No. 7021-PNG)

1. On December 6, 2001, the Inspection Panel (the "Panel") received a Request for Inspection (the "Request") dated November 29, 2001 related to the above-referenced loan. (Annex 1) On December 7, 2001, the Panel notified the representative of the Requesters, the Executive Directors and the President of the International Bank for Reconstruction and Development (IBRD or the "Bank") of receipt of the Request (meaning "Registration" under the Panel's *Operating Procedures*).¹

A. Financial Arrangements

2. The Governance Promotion Adjustment Loan (GPAL) made to the Independent State of Papua New Guinea (PNG) was approved by the Board of Executive Directors of IBRD on June 13, 2000.² It was a US\$90 million fixed-spread loan for 20 years, including a 5-year grace period at the Bank's standard variable interest rate and commitment fee for fixed-spread loans with an expected disbursement period of less than three years. The GPAL was to be disbursed in two tranches of \$35 million each, and a floating tranche of \$20 million. The first tranche was disbursed upon effectiveness, which took place on June 21, 2000. The second and the floating tranche were to be released upon satisfaction of the conditions set forth or referred to in Parts A and B, respectively, of Schedule 3 to the Loan Agreement. The floating tranche was disbursed in July 2001, while the last; second, tranche was disbursed in December 2001.

B. The Program

3. The GPAL was made "*in response to a request from the Papua New Guinea Government in mid-1999 to support its stabilization and structural reform efforts.*"³ According to the Loan Agreement, the Government of the Papua New Guinea designed a program of actions, objectives and policies to achieve structural adjustments of the country's economy (the "Program"), declared its commitment to the execution of the Program and requested assistance from the Bank to support its execution.⁴ The Bank agreed to support the Program by providing the GPAL.

¹ See The Inspection Panel, *Operating Procedures*, August 1994 at ¶ 17.

² IBRD Loan No. 7071 PNG.

³ PID, Report No. PID8970, p.1 at ¶ 1.

⁴ Loan Agreement No.7021 PNG between the Independent State of Papua New Guinea and the Bank, dated June 16, 2000 (the Loan Agreement), p.2 at ¶ (A).

4. The specific key objectives of the Government's Program were "*strengthening economic management and improving governance.*"⁵ The first objective was to be achieved by "*improving fiscal management to enhance macroeconomic stability; improving debt management; and improving operating environment for business, including through privatization.*"⁶ The second – by "*improving governance; improving civil service efficiency and effectiveness; improving delivery of health and education services; improving forestry management through strengthening the institutional framework; improving efficiency of financial services and reducing systemic risk through reform of the pension industry and privatization of the state bank group.*"⁷
5. According to Report and Recommendation of the President submitted to the Board of Executive Directors of IBRD about the Program, the Bank's loan "*would support the Government's ongoing efforts to redress past policy and governance shortcomings in a sustainable manner.*"⁸ The Program included several components to improve the following: "*fiscal and debt management; governance and civil service effectiveness; delivery of health and education services; forestry management; the quality and efficiency of financial services, including through privatization; and the operating environment for business.*"⁹ The main objective of the Program as stated was "*to strengthen governance in public institutions through enhanced transparency and accountability.*"¹⁰
6. The Letter of Development Policy (the "LDP"), submitted by the Government of PNG, described, *inter alia*, how the improvements to forestry governance were to be achieved. It stated that legislation was to be prepared and submitted to Parliament which would prevent the clearance of forested land ostensibly for agricultural or infrastructural purposes, but which was in fact based largely on the financial attractiveness of clear-felling large areas of natural forest at very low per unit bgs prices. It added that a careful process for environmental assessment of any clearing proposal would be applied through the Office of Environment and Conservation, which will be provided with the capacity to undertake such reviews. Furthermore, the LDP states that a transparent system of review, through the Forestry Board, would then be required prior to issue of any licenses to clear significant areas of forest for any purpose.¹¹
7. The LDP also stated that the composition and working of the Forestry Board itself would be reviewed and improved because the Government would revise the selection criteria and procedures that applied to the appointment of Board members. Specifically, the Government was to ensure that independent and capable membership was guaranteed. Also, all deliberations of the Forestry Board which were not of a sensitive commercial nature would be made public, and major decisions taken by the Board will

⁵ Report and Recommendation of the President of the IBRD to the Executive Directors on a Governance Promotion Adjustment Loan in an Amount of US\$90 Million to PNG, May 19, 2000, Report No. P-7374-PNG, p.iii at ¶ 3.

⁶ Ibid.

⁷ Ibid.

⁸ Id., p.8 at ¶ 35.

⁹ Ibid.

¹⁰ Ibid.

¹¹ Letter of Development Policy (LDP), May 15, 2000, § 55, p.15. Attached as Annex 1 to the Report and Recommendation of the President to the Executive Directors on a GPAL to PNG, May 19, 2000

be eligible for public hearings within a specified time frame, so that any objections or other claims could be lodged and heard.¹²

8. In respect to the moratorium on the issuance of the timber concessions declared in late 1999, the Government stated that a review of the forest resource license application and approval processes would be carried out, and that all projects included in this process would be placed on hold until the results of that review were known and had been evaluated by Government.¹³ Moreover, the Government was also to address major questions of efficiency and equity that have arisen in the sector. The pricing system for logs applied in the country, for example, was to be reviewed and adjusted, so that actual revenues collected from logging operations were close to the full economic rent and also to ensure that landholders received a fair and consistent share of the overall return for their resources. The capacity of the relevant Government agencies to carry out monitoring and enforcement of all regulations and codes in forest operations and in the exporting of forest output will be improved in a manner, which relied on inputs from independent experts or firms. This should enhance transparency and accountability in the system and, in this way, reduce the potential for governance issues and corruption to disrupt sustainable and environmentally responsible forestry operations in Papua New Guinea. The Government would also upgrade the processes, by which landowners are involved in the early decisions on resource based projects in the forestry sector, to ensure that they are adequately represented, and also properly informed as to the implications of the proposed project in their areas.¹⁴

C. The Request

9. The Request was submitted by the Center of Environmental Law and Community Rights Inc. (CELCOR), a Papua New Guinean non-governmental organization representing about 550 customary landowners of lands and forests in 21 villages in the Kiunga District of the Western Province of Papua New Guinea (the Requesters). CELCOR has submitted copies of authorization of representation signed by the Requesters, who have requested that their names be made available only to the Panel members, but otherwise remain confidential.
10. The Requesters claim that Management, in violation of the terms and conditions under which the Board of Executive Directors approved the GPAL, intends to release its last tranche, despite the fact that the Borrower, i.e. the Government, has not complied with disbursement conditions related to forestry management.¹⁵ Particularly, the Requesters point to the Borrower's failure to meet the following:
 - *“to reinstate the forestry log tax regime; and satisfactorily implement reforms on the forestry revenue and royalty to landowners regime.*
 - *to fund an independent inspection of log exports, pre-shipment.*
 - *[to maintain] a moratorium on all new timber concessions, pending a complete review of all existing concessions (but implemented as a review of new/proposed concessions).*

¹² Id, p.16, at §56.

¹³ Id, p.16 at §57.

¹⁴ Id, p.16 at §58.

¹⁵ At the time the Request was submitted, the second tranche of GPAL was yet to be disbursed. The approval of its disbursement by the Board took place on December 19, 2001.

- *[to enact] new laws on forest clearances for roads and agricultural schemes.*
- *[to enact] new laws restraining powers of delegation.*
- *[to enact] new laws insisting on a better balance on the Board of the Papua New Guinea Forest Authority.*
- *[to enact] new laws on transparency and non-commercial disclosure by the Forestry Board.”¹⁶*

11. The Requesters refer to the conditions for the release of the second tranche as they are defined in the Matrix of Policy Actions, which is an attachment to the Government’s Letter of Development Policy (specifically referring to the “Actions Taken/Outcomes Achieved” column). The Requesters maintain that the language of the above-referred document is binding on the Government of PNG and the Bank, and claim that this language is determinative with regard to the meaning and interpretation of the release conditions.¹⁷ The Requesters claim that the Government had not achieved full compliance with these conditions, which are required for disbursement of the second tranche.

12. Specifically, with respect to these conditions, the Requesters claim that the Bank’s disbursement of the second tranche without a full review of the contractual provisions of the Loan and without the Government:

- *“maintaining the moratorium [on all new timber concessions]*
- *fully implementing the findings of the partial review [of all timber concessions], including the requirements seeking the remediation of illegal activities,*

would constitute

- *a violation of the contractual provisions of the SAL by loaning to a borrower, who with bad faith, defaults to implement its own promises. There are, they claim, very clear examples set out in the body of this claim indicating the development objectives of the governance loan have not been met and are unlikely to be met, if the disbursement of the second tranche is completed.*
- *a violation of Operational Directives 13.05 on supervision and monitoring because of poor judgment and imprudent lending to a borrower who promotes illegal practices.*
- *A violation of the Bank’s forest policy OP 4.36 as the acts of the State show that it did not implement, follow, adhere to, or is in fact committed to, sustainable forest management, sustainable forestry, conservation-oriented forestry or good forestry practice.”¹⁸*

13. The Requesters also claim that the actions, described above, have caused and will continue to cause “grave financial loss to the claimants” and that the Request deals with “significant instances of social, cultural, ecological and economic harm.”¹⁹

14. The Requesters also claimed that they have or may be affected by the Bank’s failure to supervise the Borrower’s compliance with the terms and objectives of the Program

¹⁶ Request, at pp.5-6.

¹⁷ Request, Section 3.1, at p. 10

¹⁸ Id., p.3.

¹⁹ Ibid.

and the conditions of disbursement of the GPAL. Finally, they assert that some of the adverse effects they are suffering are caused particularly by the illegal logging and road construction project on their lands, the Kiunga-Aiambak Road, which is degrading their land and forest, damaging their culture, as well as inflicting substantial economic losses on them.²⁰

15. The Requesters' claims could constitute violations of, *inter alia*, the following Bank Policies and Procedures:

OP 4.36 on Forestry
OD 8.60 on Adjustment Lending
OD/OP/BP 13.05 on Project Supervision

D. The Response

16. On January 29, 2002, the Panel received Management's Response to the Request for Inspection. (Annex 2)
17. In its Response, Management states that the GPAL was "*designed as a structural adjustment loan (SAL) to support a reform program prepared by the Borrower, described in the Borrower's Letter of Development Policy (LDP), dated May 15, 2000, addressed to the President of the Bank.*"²¹ The Response further observes that the loan proceeds were to be disbursed in three tranches: the first (US\$35 million), followed by a floating tranche (US\$20 million), and a second tranche (US\$35 million). The latter two were subject to the conditions defined in the Loan Agreement between PNG and the Bank.
18. Since the conditions for the release of the second tranche are the subject of the controversy, Management refers to Schedule 3 to the Loan Agreement, which refers to twenty specific conditions for release of the second tranche. Moreover, Management indicates that there were "*two other general conditions for tranche release applicable to each of the tranche releases: (i) satisfactory progress in carrying out the Borrower's reform program; and (ii) a satisfactory macroeconomic policy framework.*"²² Management then restates the conditions relevant to forestry management as they are defined in the Loan Agreement.
19. One of the disputed issues between the Requesters and Management is, however, *where* the tranche release conditions are established: in the Loan Agreement and the LDP and Policy Matrix, or solely in the Loan Agreement. The Requesters contend that the release conditions for the second tranche are defined in the Policy Matrix prepared by the Borrower as an attachment to the LDP.
20. The Request for Inspection asserts that the "*conditions required for disbursement of the second tranche have not been met by the State.*"²³ The Requesters further contend that "*the disbursement of the second tranche of the SAL ... would constitute a violation of*

²⁰ As explained in paragraph 37 of this Report, the timber concession for the Kiunga-Aiambak road project was obtained in 1994, while the GPAL was approved in June 2000.

²¹ Management Response, Executive Summary, § 4, p.vi.

²² *Id.*, at p. vii.

²³ Request for Inspection, p.4.

the contractual provision of the structural adjustment loan, and a violation of the Bank's obligation to supervise and monitor its projects pursuant to the Bank's Supervision and Monitoring Policy, OD 13.05."²⁴

21. On this point, Management states in paragraph 56 of its Response that the Requesters misinterpret the facts. Management explains that *"there is no Matrix included in the Loan Agreement..."* and *"the language quoted by the Requesters is taken from the Matrix attached to the LDP, which serves only as a summary of actions taken or to be taken by the Borrower under the reform program that is fully described in the main text of the LDP. [...] Management regrets that this issue was not clarified in either the Report and Recommendation of the President on the GPAL or the Loan Agreement."* In paragraph 39 of its Response, Management cites the release conditions as they are set forth in Part A of Schedule 3 to the Loan Agreement.
22. However, the Panel notes that the Loan Agreement incorporates the LPD and the Program supported by the GPAL as follows: *"the Bank has received from the Borrower a letter, dated May 15, 2000, describing a program of actions, objectives and policies designed to achieve structural adjustment of the Borrower's economy (hereinafter called the Program), declaring the Borrower's commitment to the execution of the Program, and requesting assistance from the Bank in support of the Program during the execution thereof..."*²⁵
23. Furthermore, the LDP itself defines the Program as follows: *"the details of the Government's reform program and the specific actions that will be taken to achieve it are set out in the attached Matrix of Policy Actions, which together with this letter form the basis of the Government's structural adjustment program"*²⁶ adding that *"the remainder of this letter reports on recent progress and highlights the main areas of the program for which World Bank support is sought."*²⁷ (emphasis added). Thus, without

²⁴ Id., at p.10.

²⁵ The Loan Agreement, Whereas (A).

²⁶ Letter of Development Policy (LDP), May 15, 2000. Attached as Annex 1 to the Report and Recommendation of the President to the Executive Directors on a GPAL to PNG, May 19, 2000, § 6.

²⁷ There are a number of other references to the Program in the Loan Agreement, especially in Sections 2.02 (d), Section 3.01 and Section 4.01. Section 2.02 (d), in particular, states that *"no withdrawals of the proceeds of the Second Tranche shall be made from the Loan Account unless the Bank shall be satisfied...(i) with progress achieved by the Borrower in the carrying out of the Program."* In addition, Section 3.01, particularly part (c), states that *"without limitation upon provisions of paragraph (a) of this Section, the Borrower shall exchange views with the Bank on any proposed action to be taken after the disbursement of the Loan which would have the effect of materially reversing the objectives of the Program, or any action taken under the Program including any action specified in Schedule 3 to this Agreement"* (emphasis added). Section 4.01 refers to the additional event of suspension of the loan as a *"situation [that] has arisen which shall make it improbable that the Program, or a significant part thereof, will be carried out."* In addition, OP 7.00 on Lending Operations: Choice of Borrower and Contractual Agreements, when describing the variety of documents that define the Bank's contractual relationship with borrowers, refers to Letters of Development or Sectoral Policy as follows: *"For a structural adjustment loan or sector adjustment loan, the Letter of Development (or Sectoral) Policy sets out the salient elements of the proposed adjustment program and the borrower's commitment to carry out the program. The contents of this letter are defined as "the Program" and are incorporated by reference in the Loan Agreement. Receipt by the Bank of this letter, duly executed, constitutes a condition of Board presentation of the loan."* (emphasis added). Furthermore, it should be noted that OD 8.60 on Adjustment Lending states that: *"The Letter of Development or Sector Policy may be used to elaborate upon and explain some of the conditionality, particularly the conditionality on satisfactory macroeconomic performance."* While in paragraph 40, it states that *"a clear understanding with the government on the overall stabilization and structural programs is a prerequisite for putting the conditions for tranche releases in the proper context. The Letter of Development Policy (in the case of SALs) and the Letter of Sector Policy (in the case of SECALs), and the corresponding*

consideration of the specifics of the conditions in dispute, it is evident that the Program seems to be described in more detail and more specifically in the Policy Matrix than in the LDP itself or in the Loan Agreement.

24. In Management's opinion, the Bank's actions related to the GPAL were in compliance with the relevant policies and procedures. Concerning *"the reports of possible adverse effects on the Requesters,"* Management states that *"any such adverse effects were in no way connected with the GPAL, and there is no cause and effect between the adverse impacts and any actions or omissions of the Bank."*²⁸ With regards to the tranche release conditions at issue, Management states that *"the forestry-related tranche release conditions were all met prior to disbursement of the second tranche."*²⁹
25. In its Response, Management addresses each of the claims submitted by the Requesters and, specifically, the second tranche release conditions. Particularly, with regard to the failure to maintain a moratorium on all new timber concessions pending a complete review of all existing concessions, Management asserts that a moratorium was put in place by the National Cabinet in November 1999 and was later amended to change an alleged error in the language of the applicable Cabinet Decision. However, Management elaborated that *"the Cabinet Decision did not indicate any commitment to retain the moratorium after the review of pending applications was completed"*³⁰. Furthermore, Management stated that it supported the scope of the moratorium as defined by the Borrower in early 2000, i.e. a review of *all of the pending* timber concessions. The Bank is now financing a **Forestry and Conservation Project (FCP)**³¹, for which the Board recently approved an IBRD Loan and a GEF grant, that, inter alia, includes a review of *all of the existing* concessions. At the same time, Management admits that *"it was not possible to reach a complete consensus between the Bank and the Borrower and all stakeholders on the issue of the full scope of the moratorium and review, nor was the text of the various GPAL documents entirely consistent."*³²
26. The scope of the review of timber concessions, i.e. the review of all existing concessions as opposed to a review of all pending concessions only, is claimed by Management to be determined exclusively by the terms of the Loan Agreement. In response to the Requesters' citation of the Policy Matrix and Letter of Development Policy, Management states that the Requesters misinterpret the facts and states that the Matrix was not included in the Loan Agreement. Specifically, Management claims in paragraph 56 of its Response, that *"while the main text of the LDP clearly establishes*

policy matrices, spell out the macroeconomic targets to be monitored so as to avoid misunderstandings." Finally, a specific annex to OD 13.05 on Supervision entitled "Guidelines for the Supervision of Adjustment Loans" stated: *"An adjustment loan normally supports a program consisting of a number of policy measures intended to achieve certain macroeconomic and sector objectives. The measures are detailed in the loan agreement and the government's "Letter of Development Policy." The program and its rationale are further explained in the President's Report. Supervision has to focus primarily on program execution and, therefore, the timely adoption and effective implementation of the agreed policy measures and other actions, such as specific institutional arrangements and studies."* (emphasis added).

²⁸ Id., at §7.

²⁹ Ibid.

³⁰ Id., at §51.

³¹ An IBRD loan in the amount of US\$ 17.36 million equivalent and a Global Environment Facility (GEF) Trust Fund Grant in the amount of SDR 13.31 million equivalent were approved by the Board on approved on December 18, 2001 to finance the Forestry and Conservation Project (FCP).

³² Management Response, at §57.

the scope of the review to cover all recent major forest resource permit applications and approval processes, the summary in the Matrix does not accurately reflect the action set out in the LDP.” As stated above, Management regrets the fact that this situation was not clarified in the loan documentation. (See discussion in paras.19-23).

27. As to the review of timber concessions, Management refers to the conclusions of the Bank’s supervision mission that determined that *“the independent review was completed in accordance with the Loan Agreement, consistent with the LDP and the intent of the parties, and in Management’s view the Bank is in full compliance with its responsibilities under OD 13.05.”*³³
28. With regard to the second condition – to reinstate the forestry log tax regime and satisfactorily implement reforms on the forestry revenue and royalty to landowners regime – Management asserts that the Government of PNG carried out the requisite review, with a focus on taxation reforms and transfer pricing, and implemented adjustments to the log export tax in the 2002 budget.³⁴ However, Management admits that *“the analysis and recommendations of the review with regard to landowner royalties raised a number of unanticipated issues that require further detailed analysis.”*³⁵ According to Management, the Government’s commitment to deal systematically with the royalty issues raised by the review is now to be implemented under the Forestry and Conservation Project (FCP). In view of the foregoing, Management reached the conclusion that *“together with the revenue system amendments implemented in the 2002 budget, the steps towards implementing changes in the royalty system initiated through the review process and the Prime Minister’s letter pledging commitment were therefore considered by Management to be sufficient to comply with this second tranche condition.”*³⁶ **The Panel notes, however, that in recommending the release of the second tranche of the GPAL, Management, while acknowledging the need for a more measured longer term examination of issues related to royalties,³⁷ stated to the Board that the condition calling for the implementation by the Borrower of reforms to its forestry revenue and royalty regime, satisfactory to the Bank, “had been met.”³⁸ (emphasis added.)**
29. In addition, Management denies violation of OP 4.36 on Forestry, as claimed by the Requesters. In Management’s view, this particular policy is inapplicable to Structural Adjustment Loans. **The Panel, however, could not find any provision in the policy supporting such assertion.**
30. Regarding the next condition – to strike a better balance on a Board of the PNG Forest Authority– Management states that the relevant second tranche release conditions were satisfied. They called for adoption by the Borrower’s Parliament of amendments to the Forestry Act of 1991 covering, *inter alia*, delegation of powers of the Board to an

³³ Id, at §48. In addition, it should be noted that the PNG Forestry Review Team, established under the GPAL, did review the Kiunga-Aiambak timber concession. See Appendix 12 to the Request for Inspection, which is attached as Annex 1 to this Report.

³⁴ Id, at §46.

³⁵ Id, at §47.

³⁶ Id, at §47.

³⁷ President’s Memorandum entitled “Papua New Guinea-Governance Promotion Adjustment Loan-Loan No. 7021-PNG-Release of Second Tranche” dated December 6, 2001, at ¶ 41

³⁸ Id, at ¶ 64

individual and the composition of the Forestry Board. These amendments were “*passed in May 2000, and the conditions have therefore been met.*”³⁹

31. Management claims that the next condition – on enactment of new laws on transparency and non-commercial disclosure by the Forest Authority Board – was also met satisfactorily. The Government passed the necessary amendments to national laws and “*based on the commitment shown by the Borrower, it is expected that these laws will be enforced accordingly.*”⁴⁰
32. In response to the Requesters’ claim on the Bank’s failure to supervise adequately the GPAL, Management asserts that “*the Bank’s approach towards preparation and supervision was fully geared to the scope and content of the reform program under the GPAL.*”⁴¹ Management asserts that “*during supervision of the GPAL, satisfactory progress with the Borrower’s reform program and with each tranche release condition was thoroughly reviewed.*”⁴² In conclusion, Management states that “*the final supervision mission in December 2001 and Management’s recommendation to the Board concluded that the Borrower had fully complied with all conditions except two (not related to forestry) that were duly waived by the Bank’s Executive Directors on December 18, 2001.*”⁴³ Management concludes that supervision of GPAL was intensive and continuous with adequate technical and financial support.
33. As for the logging operations at the Kiunga-Aiambak Road and their consequences to the Requesters, Management declares its concern over illegal logging projects and restates its support for the Government’s efforts to stop these operations. However, Management contends that these logging operations “*do not in any way involve the Bank, that these actions are done by the private parties of whom the Bank has no control, and that these projects do not in any way constitute consequences of the failure of GPAL conditions.*”⁴⁴
34. In summary, with regard to the issues raised in the Request for Inspection, Management claims that the Bank’s actions related to the GPAL, including release of the loan tranches, were in compliance with its applicable policies and procedures and consistent with the legal agreements entered into between PNG and the Bank, and, that any adverse effects suffered by the Requesters were in no way related to the GPAL and there is no cause and effect between the alleged adverse impacts and any actions or omissions on the part of the Bank in this regard.

E. Eligibility

35. Paragraph 9 of the 1999 Clarification⁴⁵ provides that “*if the Panel so recommends, the Board will authorize an investigation without making a judgement on the merits of the claimants’ request, and without discussion except with respect to the following technical eligibility criteria:*

³⁹ Management Response, at §66.

⁴⁰ Id, at §64.

⁴¹ Id, at §41.

⁴² Id, at §42.

⁴³ Id, at §44.

⁴⁴ Id, at §29.

- (a) *The affected party consists of any two or more persons with common interests or concerns and who are in the borrower's territory.*
- (b) *The request does assert in substance that a serious violation by the Bank of their operational policies and procedures has or is likely to have a material adverse effect on the requester.*
- (c) *The request does assert that its subject matter has been brought to Management's attention and that, in the requesters' view, Management has failed to respond adequately to it, thus demonstrating that it has followed or is taking steps to follow the Bank's policies and procedures.*
- (d) *The matter is not related to procurement.*
- (e) *The related loan has not been closed or substantially disbursed.*
- (f) *The Panel has not previously made a recommendation on the subject matter, or if it has, that the request does assert that there is new evidence or circumstances not known at the time of the prior request.*⁴⁶

36. For purposes of determining the eligibility of the Request and the Requesters, the Panel reviewed the Request and Management's Response. Panel Members met World Bank officials in Washington, D.C. The Panel's Chairman Edward S. Ayensu⁴⁷ visited Papua New Guinea in March to establish eligibility of the Request and the Requesters. In Papua New Guinea he met with the NGO that is representing the Requesters, CELCOR, representatives of the Lake Murmy Resource Owners Association (LMROA), Eco-Forestry Forum (EFF), Environmental Law Center (ELC), Environmental Watch Group (EWG), Foundation for People, Community Development, and others. The Panel team also met with several Government officials, some Members of Parliament, some of the consultants who were in charge of the review of Forest Management Agreements under the GPAL, and representatives of local communities. The Panel team also met with the Bank's Country Director and the Senior Economist for PNG at the Bank's offices in Sydney, Australia, and for purposes of the preparation of this Report and Recommendation, the Panel consulted with the Executive Director representing Papua New Guinea and his staff.⁴⁸

37. In Port Moresby, the Panel also met with Kiunga-Aiambak Road area residents who confirmed that CELCOR was the representative of people who signed the Request for Inspection. The Kiunga-Aiambak area residents confirmed to the Panel Team their concerns over the situation in their community. They stated that on April 18, 1994, a purported landowner company called PAISO Limited applied to the Papua New Guinea Forest Authority for a timber concession and was successful in obtaining a Timber Authority to carry out road line clearance of forests in the Lake Murray area, which is a part of the Western Province in Papua New Guinea (the "Project"). This road was part of the government's national road plan to link up the Western Province to the Southern Highlands Province.

⁴⁶ 1999 Conclusions of the Board's Second Review of the Inspection Panel (hereinafter The 1999 Clarifications), § 9.

⁴⁷ Assisted by the Panel's Executive Secretary Mr. Eduardo Abbott.

⁴⁸ The Panel wishes to thank the Executive Director and his staff for their assistance. It wishes to thank the Government officials, NGO representatives and local people, who took time to meet with them. Finally, it would like to thank Bank staff in the Country Offices in Sydney and Port Moresby for their logistical support.

38. By law, the Timber Authority (TA) would continue for a period of twelve months and upon its expiration the TA holder must apply again to the PNG Forest Authority for a new TA to continue on with the road line clearance if it was not able to complete its task. Also the laws governing TAs forbid the TA holder from transferring its obligations and responsibilities to a third party.
39. PAISO Ltd. apparently breached these laws under two circumstances:
 - 1) On October 24, 1994, PAISO Ltd. entered into a Log Harvesting and Marketing Agreement with Concorde Pacific Ltd. (a Malaysian logging company) to undertake the Project.
 - 2) Upon expiration of the TA on April 18, 1995, both companies sought and were granted a renewal of the TA for a period of five (5) years, allegedly, from a former national Forest Minister under questionable circumstances. Both companies did not comply with proper procedures under the Forestry (Amendment) Act 1991.
40. The TA was issued purposely to construct 246 kilometers of road from Aiambak to Kiunga. Five thousand (5, 000) cubic meters of logs were allowed by law, as amended, to be harvested 40 meters from each side of the road alignment with a period of twelve months. Unfortunately, Concorde Pacific Ltd. seems to have totally breached these statutory requirements by going into large scale logging without proper authorization and supervision from the PNG Forest Authority (PNGFA).
41. Attempts by the PNGFA to suspend the TA have been unsuccessful due to a Court injunction restraining it from suspending the TA or interfering with the operations of Concorde Pacific Ltd. In November 1999, the PNGFA issued a "Notice to Suspend the Timber Authority" from Concorde Pacific Ltd. after allegations of its police brutality to landowners and serious breaches of the forestry laws. Concorde Pacific Ltd. then applied to the National Court and successfully obtained an interim injunction to restrain PNGFA from stopping its logging operations under the TA. This interim injunction against PNGFA was later extended until its decision to suspend the TA from Concorde Pacific would be fully decided in Court. Upon expiration of the TA, PNGFA issued a "Notice to Cease Operations" on Concorde Pacific Ltd., which resulted in a lawsuit brought by Concorde Pacific against PNGFA Managing Director for contempt of Court. Currently, PNGFA power has been curtailed by the Court's injunctions and this allows for Concorde Pacific Ltd. to continue with its operations whilst the substantive proceedings in Court are fully determined. It also prevents PNGFA from taking any action against either Concorde Pacific Ltd. or PAISO Ltd. until such time as the substantive proceedings in Court are fully settled. The substantive proceeding is the judicial review sought by Concorde Pacific Ltd. to review PNGFA intention to suspend the TA. The Court, in spite of the long elapsed time, has yet to set a date for these purposes.
42. As a consequence of the above-described situation, the customary landowners have suffered tremendously due to environmental destruction to their natural forests and rivers; non-payment of premium and royalty entitlements, and emerging social problems within village communities.
43. The national Government through the PNGFA seems to have been incapable of protecting the landowners and the rights to their land and from being deprived of their

forest resources. Contributing factors associated with geographical isolation and lack of access from essential services such as telephones, postal services and transport have made it even more difficult for the landowners to bring up their grievances to, and receiving assistance from, the appropriate Government authorities.

44. To get better acquainted with the overall situation of landowners affected by illegal logging in PNG, the Panel team visited the Collingwood Bay area. There, they interviewed landowners, NGO representatives and local people. During this visit, the residents of the Collingwood Bay area, claiming to have the same views and problems as the Requesters, supported and asked that their names be added to the Request for Inspection.⁴⁹
45. During this visit the Panel team learned that a controversy around the customary land in Collingwood area started with the Government's alleged transfer of two areas of customary land of about 38,000 ha. out of customary ownership into special state agricultural leases, through a lease-lease back procedure under the Lands Act. The lease-lease back transactions of this land were approved in January 1998 for the development of an oil palm project. Both agricultural leases were registered in the name of Keroro Development Corporation, Ltd. Keroro Development Corporation is apparently owned by 2 individuals, one of whom, allegedly, was also involved in Kiunga-Aiambak road project. The lease-lease back transaction undertaken by the Government was never formally authorized by the true landowners in the Collingwood Bay area.
46. Currently, the land titles continue to be registered in the name of the State and an oil palm project is still being planned. However, there is no guarantee that an oil palm project will ever be carried out, and thus, the proposed clearance of ancient forests for this purpose was perceived as a disguise by local people. The Environmental Plan prepared for the proposed oil palm project was also flawed and inadequate, and was approved without required consultations with area people and public. The landowners submitted their concerns to the Independent Forest Review Team on Collingwood, but, in their view, such concerns were not addressed adequately. The landowners are concerned that their customary land has now been transferred to the State and Keroro.
47. The issuance of the TAs to the Deegold Company to log the Collingwood Bay area land was supported by the Departments of Land and Agriculture. The TAs were issued in spite of the dispute over the validity of consent of the landowners to lease the land to the State. Later, however, the PNGFA declared these TAs void because the performance bonds provided by Deegold were set outside the required timeframe. Currently, the Collingwood landowners are concerned with the fact that private enterprises continue to operate within their TAs, irrespective of the fact that the PNGFA has declared them invalid.
48. The only option available to area landowners to stop the logging operations is through a Court action, which has proven to be very time consuming. It started in June 1999 and is expected to go to trial on May 9-10, 2002. Furthermore, local lawyers lack resources to adequately assist landowners in filing their complaints with the Court, and their lack of

⁴⁹ The Panel wishes to express special gratitude to local communities for their assistance and cooperation during Panel's visit.

means is especially worrisome when compared with the resources available to the logging industry to hire their legal counsel. In practice, the Collingwood Bay landowners are being forced to do their own fighting and are involved in a very costly exercise to get back their customary lands. Assistance received by these landowners comes from local NGOs, as well as a donation from overseas to fund the legal action.

49. Legal action was commenced by the landowners in June 1999 against the State, Registrar of Titles and the PNGFA, inter alia, in an attempt to have the leases declared void and have the State titles rescinded in order to return the lands back to their original owners. In August 1999, the landowners began land mediation processes in the local Court in Popondetta Oro Province. This failed and the landowners were forced to take out Court orders to get the Senior Provincial Magistrate to conduct mediation. The landowners had to threaten contempt proceedings to get the mediation eventually to start. Finally, mediation was conducted and the Provincial Land Court in Popondetta approved the agreement reached. The agreement reached by the landowners, as part of the mediation process was to clarify customary ownership and rights under the Land Disputes Settlement Act. It dealt with the issue of whether the right owners gave consent to the lease-lease back arrangement. Therefore, currently there is no logging operation taking place in the Collingwood Bay area, but the landowners ended up with a costly and complex litigation in order to get their customary land back. The demand for "customary land back" is the center of the National Court Action. The landowners expect the Court to quash the state lease over the customary land.
50. In conclusion, the landowners of the Collingwood Bay area wanted to raise their concerns about violations of their right to control their own land and resources. The landowners want to participate in the decision-making process affecting development of their land. Sworn statements taken and filed in Court for the purposes of the legal action show a total disregard of the wishes of the landowners. The landowners and NGOs have demanded consultation between the landowners and the various state authorities in charge of development projects. Further, they demand their customary land back. Until the dispute before the National Court is resolved, they want no further deals involving their land.
51. The Panel's visit to PNG was of great value for acquiring a first-hand appreciation of the many problems faced by local landowners in dealing with forestry, environmental and economic issues resulting from illegal and/or unrestricted logging in otherwise pristine areas. The numerous meetings with NGO representatives also served to provide a better understanding about their views regarding the execution of the Program, the Bank's conditionality, and the sustainability of the reforms supported by the GPAL. Some specific examples of these views are worth noting in this Report.
52. On the matter of the Government's review of timber concessions, for example, the Requesters and other NGOs – after acknowledging the fact that there were quite a number of consultations on the subject – questioned not only the limited number of reviews but also their specific terms of reference and the fact that only three field visits were made by the consultants in charge of the reviews, mostly to validate the methodology. In their view, this was not acceptable in a country with 20 provinces where many important decisions related to timber concessions are taken locally. The manner in which the results of the different reviews were consolidated was also a source

of concern, since, in several instances, it seemed to distort the findings of individual reviews.

53. As for the sustainability of the reforms (especially those which were conditions for the release of the second tranche), the local NGOs noted that the amendments to the forestry revenue regime consisted in a mere adjustment of a tax rate, in the context of the budget approval process, and that no amendments were made to the royalty regime in spite of its evident shortcomings.⁵⁰ They commented further that, even during the limited moratorium, several new timber concessions were granted. Moreover, in spite of formal changes to the composition of the Forestry Board its membership basically remained the same (the Panel was able to verify the legitimacy of these claims.) Finally, they noted that these reforms may be short-lived, since several Government officials oppose them and the composition of Government is likely to change as a result of the forthcoming elections.
54. During its visit, the Panel gained adequate insight into the many problems faced by interested Government officials and Bank staff when addressing these issues and the efforts made by them to provide technical and financial assistance to support sustainable improvements in governance. The visit also allowed the Panel team to confirm Bank staff's concern about the situation of the Requesters. Bank Management has indicated that it will consider a number of measures to assist the Requesters in dealing with present problems and their conservation and sustainable development efforts.

F. Conclusion

55. In the Panel's view, the evident harm suffered by the Requesters is not related to an act or omission of the Bank,⁵¹ as required by paragraph 12 of the Resolution. Indeed, the actions causing the harm are inflicted by private entities that have no relationship to the Bank's assistance program in Papua New Guinea. These harmful logging projects that pre-date the GPAL, cannot be regarded as the consequence of an alleged failure by the Bank to supervise the execution of the Program supported by the GPAL and/or the Borrower's compliance with the applicable tranche release conditions.

G. Recommendation

56. In the light of the foregoing and the provisions of paragraphs 12 and 19 of the Resolution, and relevant provisions of the 1996 and 1999 Clarifications,⁵² the Panel does not recommend an investigation into the matters alleged in the Request.

Annexes

Annex 1 – Request for Inspection

Annex 2 – Management Response

⁵⁰ See para. 28 of this Report.

⁵¹ Paragraph 3 of the 1999 Clarifications states: *"In its initial response to the request for inspection, Management will provide evidence that... iii. the serious failures that may exist are exclusively attributable to the borrower or to other factors external to the Bank... The Inspection Panel may independently agree or disagree, totally or partially, with Management's position and will proceed accordingly."*

⁵² 1996 Clarification of Certain Aspects of the Resolution, dated October 17, 1996 (the 1996 Clarifications).