

Validation of Papua New Guinea
Draft Validation Report
CowaterSogema Independent Validator
19th October 2018

1. EXECUTIVE SUMMARY

The government of the Independent State of Papua New Guinea (PNG) committed to implement the EITI on 14 March 2013 by through National Executive Council (NEC) Decision 90/2013. An interim Multi-Stakeholder Group (MSG) was formed in 2012 and a permanent MSG was appointed in November 2013. The country was accepted as an EITI Candidate on 19 March 2014 at the EITI Board's meeting in Oslo.

On 25 October 2016, the Board agreed that PNG's Validation under the 2016 EITI Standard would commence on 1 April 2018. This report presented the findings and initial assessment of the International Secretariat's data gathering and stakeholder consultations. The International Secretariat has followed the Validation Procedures and applied the Validation Guide in assessing PNG's progress with the EITI Standard.

The Secretariat's preliminary assessment is that 14 of the requirements of the EITI Standard have not been fully addressed in PNG. Nine of these are assessed as unmet with inadequate progress. The recommendations and suggested corrective actions identified through this process relate in particular to license allocations (#2.2), license register (#2.3), state participation (#2.6), production data (#3.2), export data (#3.3), comprehensiveness (#4.1), SOE transactions (#4.5), direct subnational payments (#4.6), data quality (#4.9), distribution of revenues (#5.1), subnational transfers (#5.2), mandatory social expenditures (#6.1), SOE quasi-fiscal expenditures (#6.2), outcomes and impact of implementations (#7.4).

This draft validation report follows on from a quality assurance review of the International Secretariat's initial assessment. The Validator agrees with the Secretariat that Papua New Guinea has not yet reached EITI standard, with 14 requirements failing to be met satisfactorily.

There are no scoring changes recommended.

2. BACKGROUND

Papua New Guinea (PNG) is a significant producer of gold, copper, nickel, silver, cobalt and oil and gas¹, ranking as the world's 13th largest gold producer² and 10th largest LNG exporter³ in 2016. With extractives accounting for about 55% of exports and 24% of GDP in 2016, PNG's economy is one of the most reliant on extractives in the Asia Pacific.⁴ The country has traditionally been reliant on mining, with minimal crude oil production starting in 1992, although the start of significant liquefied natural gas (LNG) production and exports from 2014 has radically changed the structure of extractive industry revenues.

PNG had eight producing large-scale industrial mines in 2016⁵, alongside an extensive artisanal and small-scale mining (ASM) sector employing an estimated 80,000 small-scale miners directly as of November 2016

¹ US Geological Survey (July 2017), 'The mineral industry of Papua New Guinea 2014', accessed [here](#) in April 2018, p.2.

² World Gold Council (2017), Gold mining map, accessed [here](#) in April 2018.

³ International Gas Union (2017), 2017 World LNG Report, accessed [here](#) in April 2018, p.9.

⁴ NRGi (2017) 'Resource Governance Index 2017: Papua New Guinea', accessed [here](#) in April 2018.

⁵ PNG EITI (December 2017), 'PNG 2016 EITI Report', accessed [here](#) in April 2018, pp.65-73.

according to the regulator, the Mineral Resources Authority (MRA).⁶ Most producing mines are joint ventures between the government and foreign mining companies, alongside some wholly-foreign owned mines (e.g. Lihir) and the Ok Tedi copper mine, state-owned since 2013.⁷ The country's industrial copper and gold production is concentrated in three large mines (Porgera, Lihir and, whilst declining, Ok Tedi), alongside smaller and developing mines in Simberi, Hidden Valley and Tolukuma.⁸ The Toronto-listed Nautilus Minerals and the government have been piloting underwater deep seabed mining in the Bismarck Sea west of central New Ireland in 2017-2018.⁹

Having acquired Chevron Niugini Ltd's operations in 2003, Australia-listed Oil Search operates the five oil-producing fields in PNG¹⁰, having been involved in the country since 1929.¹¹ While PNG's oil production has contracted by around a third between 2007 and 2014¹², its natural gas production and exports have expanded dramatically since the ramping up of PNG LNG's production in early 2014, ahead of schedule.¹³ The project is operated by ExxonMobil (holding a 33.2% stake in the project), alongside joint venture partners Oil Search (29%), state-owned Kumul Petroleum Holdings (KPH, 16.8%), Australia's Santos (13.5%), Japan's JX Nippon Oil and Gas Exploration Corporation (4.7%), and local governments and landowners through the Mineral Resources Development Company (2.8%).¹⁴ With an initial 6.9m tons per annum (tpa) production capacity over two LNG trains, the USD 18.8bn project relies on a network of 700km of pipelines connecting it to gas fields spread across the Central, Gulf, Hela, Southern Highlands and Western Provinces. While PNG LNG had committed around 95% of its projected 6.9m tpa capacity to Asian customers¹⁵ in contracts signed in 2009-2010, production reached 20% above planned production (8.3m tpa) by the first quarter of 2017.¹⁶ The PNG LNG partners are planning an expansion, drawing on the existing Hides fields and new gas fields in P'nyang and Elk-Antelope.¹⁷ The Elk-Antelope field in Gulf Province, operated by Total (40.1%) alongside partners InterOil (acquired by ExxonMobil in 2017¹⁸) (36.5%) and Oil Search (22.8%), is the largest, with estimated reserves of 9.9 standard cubic ft (scf) of gas.¹⁹ In February 2018, ExxonMobil and Total announced an agreement to invest an additional USD 13bn to expand PNG LNG's capacity to 16m tpa through three new LNG trains (two from Elk-Antelope and one from P'nyang).²⁰

The extractive industries have been associated with social tensions in PNG.²¹ There has been a history of protests by customary landowners against activities of mining companies, with a particularly notable example in the Bougainville civil war in the 1990s. The focus of host communities' concerns related to mining has been on the environmental and social impacts of extractives activities.

⁶ Ibid, p.73.

⁷ US Geological Survey (July 2017), 'The mineral industry of Papua New Guinea 2014', accessed [here](#) in April 2018, p.2.

⁸ US Geological Survey (February 2015), 'The mineral industry of Papua New Guinea 2012', accessed [here](#) in April 2018, p.2.

⁹ Nautilus Minerals (February 2018), 'Nautilus Completes Successful Trials in PNG', accessed [here](#) in April 2018.

¹⁰ PNG EITI (December 2017), 'PNG 2016 EITI Report', op. cit., p.86.

¹¹ Wood MacKenzie (January 2018), 'Papua New Guinea upstream summary', accessed [here](#) in April 2018.

¹² Platts (July 2014), 'Papua New Guinea's Kutubu crude gets lighter on production boost from PNG LNG', accessed [here](#) in April 2018.

¹³ PNG EITI (December 2017), 'PNG 2016 EITI Report', op. cit., p.85.

¹⁴ Platts (February 2018), 'PNG LNG facility shutdown after earthquake: Oil Search', accessed [here](#) in April 2018.

¹⁵ These long-term customers include China's Sinopec with a commitment for 2m tpa, Tokyo Electric Power Company with 1.8m, Japan's Osaka Gas at 1.5m and Taiwan-based Chinese Petroleum Corporation for 1.2m. See Reuters (April 2017), 'ExxonMobil markets mid-term Papua New Guinea LNG supplies', accessed [here](#) in April 2018.

¹⁶ Platts (April 2017), 'PNG LNG production surges 20% above nameplate capacity in Jan-Mar: Oil Search', accessed [here](#) in April 2018.

¹⁷ Platts (April 2018), 'Key gas field for PNG LNG expansion gets huge resource upgrade', accessed [here](#) in April 2018.

¹⁸ Hydrocarbons Technology (February 2017), 'ExxonMobil completes InterOil acquisition for \$2.5bn', accessed [here](#) in April 2018.

¹⁹ PNG EITI (December 2017), 'PNG 2016 EITI Report', op. cit., p.92.

²⁰ Reuters (February 2018), 'Papua New Guinea LNG partners set plans for big expansion', accessed [here](#) in April 2018.

²¹ Lowy Institute (August 2017), 'Internal security in Papua New Guinea: trends and prospects', accessed [here](#) in April 2018, p.1.

In the 2017 Resource Governance Index produced by NRGi, PNG received an overall score of 47/100 (“weak”) ranking 46th of 89.²² In particular, PNG was ranked as “poor” (40/100) on the enabling environment and weak rankings for value realisation and revenue management (both 50/100). The country’s best score is in taxation (“satisfactory” – 60/100), mainly due to the transparency in its production and exports, while its worst is in licensing (39/100) and control of corruption (27/100).

In line with the Validation Guide, the International Secretariat carried out the first phase of validation—initial data collection, stakeholder consultations, and preparation of their initial evaluation of progress against the EITI requirements (the “Initial Assessment”). CowaterSogema was appointed as the independent Validator to evaluate whether the Secretariat’s work was carried out in accordance with the Validation Guide. CowaterSogema’s principal responsibilities as Validator are to review and amend the Initial Assessment, as needed, and to summarize its independent review in this Validation Report for submission to the Board through the Validation Committee.

1. Work Performed by the Independent Validator

The Secretariat’s Initial Assessment was transmitted to CowaterSogema on August 31st 2018. Our Validation Team undertook this phase of the Validation process through: (1) In-depth review and marking up of the EITI Assessment by each team member; (2) Detailed review and comments by the Multi-Stakeholder Specialist of Requirements 1 and the Civil Society Protocol; (3) Detailed review and comments by the Financial Specialist of Requirements 4, 5 and 6; (4) Consolidation of reviews and the production of this draft Validation Report, sent to the International Secretariat on the 14th September 2018.

2. Comments on the Limitations of the Validation

The Validator carefully reviewed the Secretariat’s Initial Assessment and at this stage has no comments on the limitation of the validation process.

3. Comments on the International Secretariat’s Initial Assessment

The initial data collection, stakeholder consultations, and drafting of the Initial Assessment were generally undertaken by the International Secretariat in accordance with the 2016 Validation Guide. The data collection took place across three phases. Firstly, a desk review of the available documentation relating to the country’s compliance with the EITI Standard, including but not limited to:

- The EITI work plan and other planning documents such as budgets and communication plans;
- The multi-stakeholder group’s Terms of Reference, and minutes from multi-stakeholder group meetings;
- EITI Reports, and supplementary information such as summary reports and scoping studies;
- Communication materials;

²² NRGi (2017) ‘Resource Governance Index 2017: Papua New Guinea’, accessed [here](#) in April 2018.

- Annual progress reports; and
- Any other information of relevance to Validation.

A country visit took place on 3-10 May 2018. All meetings took place in Port Moresby. The International Secretariat met with the multi-stakeholder group and its members, the Independent Administrator and other key stakeholders, including stakeholder groups that are represented on, but not directly participating in, the multi-stakeholder group. In addition to meeting with the MSG as a group, the International Secretariat met with its constituent parts (government, companies and civil society) either individually or in constituency groups, with appropriate protocols to ensure that stakeholders are able to freely express their views and that requests for confidentiality are respected.

Finally, the International Secretariat prepared a report making an initial assessment of progress against requirements in accordance with the Validation Guide. The initial assessment did not include an overall assessment of compliance. The report was submitted to the Validator, with the National Coordinator (NC) also receiving a copy.

2. GENERAL COMMENTS

- **Progress in EITI Implementation**

PNG is relatively new to EITI, being accepted as an EITI Candidate on 19 March 2014 at the EITI Board's meeting in Oslo. On 25 October 2016, the Board agreed that PNG's first validation under the 2016 EITI Standard would commence on 1 April 2018.

Since the start of implementation, PNG has annually published four EITI Reports covering four fiscal years, namely, 2013-16. The last two reports were published simultaneously on 30 December 2017, ensuring PNG is well ahead of its reporting deadlines. PNG's EITI Reports have always been candid in describing and examining gaps in government systems, providing factual basis for institutional reforms.

Permanent members of the MSG were selected on 1 November 2013, following a nationwide selection process and a series of workshops with different constituencies. The current MSG is composed of 30 representatives, with 15 members representing government, eight members representing civil society, and seven members representing industry. Each constituency has seven voting members. Industry is engaged through the PNG Chamber of Mines and Petroleum²³. The CSOs are represented by an umbrella organisation, the PNG Resource Governance Coalition²⁴.

Over the years the number of MSG representatives has changed, although the timing of changes in the composition of the MSG are difficult to discern through available documentation, aside from the inclusion of SOEs as part of government representatives on the MSG decided in 2017, as an outcome of the recommendations from the first EITI Report. The MSG members are due for renewal in 2018. There had

²³ Companies represented in the MSG include: Total E&P Ltd, Barrick Niugini Ltd, ExxonMobil PNG Ltd, Harmony Gold Ltd, Newcrest Mining Ltd, Oil Search (PNG) Ltd, PNG Chamber of Mines & Petroleum.

²⁴ Organisations represented in the MSG include: Transparency International PNG, Institute of National Affairs, Consultative Implementation and Monitoring Council, Eco-Forestry Forum, Business Against Corruption Alliance, PNG Mining Watch Association Inc., PNG Council of Churches, PNG Resource Governance Coalition.

been changes to memberships over the years, but mostly with regard to individuals, not to agencies, companies or organisations represented in the MSG.

- **Impact of EITI Implementation**

The EITI Standard is uniquely relevant to PNG, a country that has oscillated between commodity-driven booms and busts since independence in 1975. Requirements related to license management, state participation, traceability of revenues to the national budget, subnational revenue flows and social expenditures hold the key to providing much-needed transparency in issues of contention between host communities, companies and (local and national) government. In some ways, the minimum requirements of the EITI Standard are particularly demanding given the complex flows of extractives revenues to non-state actors like landowner groups.

The transparency achieved through the EITI reporting to date has had a remarkable impact in and of itself. Disaggregated data on per-company extractives revenues were provided for the first time ever – and immediately used in detailed civil society analysis questioning the benefits to government and host communities of some of the country’s largest investment projects. Addressing areas of concern for government, industry and civil society, PNG EITI has led to the first public disclosures related to oil and gas license management, tax-deductible infrastructure spending, social expenditures and the flow of revenues between extractives state-owned enterprises and the government.

The civil society constituency and MSG have made extensive efforts to bridge gaps in civil society’s (technical and financial) capacity. These challenges are compounded in a country the size of California with only 700km of paved roads. Despite financial constraints, civil society has held roadshows in extractives communities and sought to maintain regular communications with a constituency of interested stakeholders. While unable to regularly undertake its own studies, PNG’s civil society has been a regular contributor to research by CSOs in the Pacific, drawing on EITI data.

Industry and government have been regular users of EITI data in public presentations and have leveraged EITI reporting and recommendations as diagnostic tools to support reforms, for instance in oil and gas license management. There is growing scope for government agencies to draw on the lengthening time series of open-format extractives revenue and non-financial data to strengthen its fiscal modelling capacities and improve its oversight of the extractive industries.

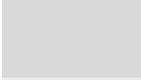
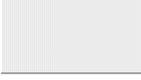
As PNG nears investment decisions on two LNG projects and several large new mines, the commercial impetus is matching the social justice imperative of strengthening key disclosures along the value chain while translating this newfound transparency into accountability in PNG’s natural resource governance.

The Independent Validator's Assessment of Compliance

Figure 1 – Validator's assessment

EITI Requirements		LEVEL OF PROGRESS				
		No progress	Inadequate	Meaningful	Satisfactory	Beyond
Categories	Requirements					
MSG oversight	Government engagement (#1.1)				█	
	Industry engagement (#1.2)				█	
	Civil society engagement (#1.3)				█	
	MSG governance (#1.4)				█	
	Work plan (#1.5)				█	
Licenses and contracts	Legal framework (#2.1)				█	
	License allocations (#2.2)		█			
	License register (#2.3)			█		
	Policy on contract disclosure (#2.4)				█	
	Beneficial ownership (#2.5)	█				
	State participation (#2.6)			█		
Monitoring production	Exploration data (#3.1)				█	
	Production data (#3.2)		█			
	Export data (#3.3)			█		
Revenue collection	Comprehensiveness (#4.1)		█			
	In-kind revenues (#4.2)	█				
	Barter agreements (#4.3)	█				
	Transportation revenues (#4.4)	█				
	SOE transactions (#4.5)			█		
	Direct subnational payments (#4.6)		█			
	Disaggregation (#4.7)				█	
	Data timeliness (#4.8)				█	
	Data quality (#4.9)		█			
Revenue allocation	Distribution of revenues (#5.1)		█			
	Subnational transfers (#5.2)		█			
	Revenue management and expenditures (#5.3)	█				
Socio-economic contribution	Mandatory social expenditures (#6.1)			█		
	SOE quasi-fiscal expenditures (#6.2)		█			
	Economic contribution (#6.3)				█	
Outcomes and impact	Public debate (#7.1)				█	
	Data accessibility (#7.2)	█				
	Follow up on recommendations (#7.3)				█	
	Outcomes and impact of implementation (#7.4)			█		

Legend to the assessment card

	The country has made no progress in addressing the requirement. The broader objective of the requirement is in no way fulfilled.
	The country has made inadequate progress in meeting the requirement. Significant elements of the requirement are outstanding and the broader objective of the requirement is far from being fulfilled.
	The country has made progress in meeting the requirement. Significant elements of the requirement are being implemented and the broader objective of the requirement is being fulfilled.
	The country is compliant with the EITI requirement.
	The country has gone beyond the requirement.
	This requirement is only encouraged or recommended and should not be taken into account in assessing compliance.
	The MSG has demonstrated that this requirement is not applicable in the country.

3. DETAILED FINDINGS

This section highlights areas where the Validator disagrees with the findings of the Initial Assessment or requires further clarification.

Although no disagreements with the scores, we have augmented the recommendations below.

Although not strictly a requirement under 2.4, serious consideration should be given to publishing contracts, possibly via a Freedom of Information Act or other legal instruments. It appears that for mining at least, there is strong potential for such contracts to be published, increasing the value and impact of EITI in PNG.

4. RECOMMENDATIONS

1. In accordance with requirement 1.1, PNG is recommended to ensure a process by which representatives of a specified seniority are involved at pre-agreed intervals if their schedules prevent regular MSG participation.
2. In accordance with Requirement 1.2, PNG is recommended to develop a strategy to engage with the virtually unchanged number of non-reporting companies to resolve their failure to report.
3. In accordance with Requirement 2.2, PNG is required to publicly disclose information related to the award or transfer of mining tenements and oil and gas licenses pertaining to companies covered in the EITI Report. This information should include the number of mining tenements and oil and gas licenses awarded and transferred in the year under review, a description of the award and transfer procedures, including specific technical and financial criteria assessed, and any non-trivial deviations from statutory procedures in practice.
4. In accordance with Requirement 2.3, PNG should maintain a publicly-accessible register(s) or cadastre system(s), including comprehensive information on licenses for all oil, gas and mining companies. In the interim PNG should ensure that information set out under EITI Requirement 2.3.b is publicly accessible for all mining, oil and gas companies.
5. In accordance with Requirement 2.6, PNG should clearly establish its definition of SOEs to delineate the SOEs within the scope of EITI reporting. It should also ensure that a comprehensive list of state participation in the extractive industries, including terms associated with state equity and any changes in the year under review, be publicly accessible. PNG must also clarify the rules and practices governing financial relations between all SOEs, including their subsidiaries, and the state, including the existence of any loans or guarantees extended by the state, or SOEs, to extractives companies or projects.
6. In accordance with Requirement 3.2, PNG should ensure that the complete production volume for oil and gas, and production values for each of the extractives commodities produced during the year under review be publicly accessible, disaggregated by commodity. To strengthen implementation, PNG may also wish to consider disclosing the methodology adopted for calculating production volumes and values, not least given the robust public debate surrounding

these figures. Public disclosure would likely also help the government in tax administration and monitoring responsibilities.

7. In accordance with Requirement 3.3, PNG should ensure that export volumes and values are publicly disclosed for each mineral commodity (including oil, condensate and gas) exported in the year under review. Given the high public interest in export data, PNG may wish to consider disclosing additional information on the mechanisms for tracking mining, oil and gas exports and the methodology for calculating export values. Public disclosure would likely also help the government in tax administration and monitoring responsibilities.
8. In accordance with Requirement 4.1, PNG should ensure that the materiality threshold for selecting companies ensures that all payments that could affect the comprehensiveness of EITI reporting be included in the scope of reconciliation. The MSG should ensure that PNG's next EITI Report includes the IA's assessment of the materiality of omissions from non-reporting entities, an assessment of the comprehensiveness of the EITI Report and that full unilateral government disclosure of total revenues, including from non-material companies, is provided for each of the material revenue streams. In accordance with requirement 8.3.c.i, the MSG should develop and disclose an action plan for addressing the deficiencies in comprehensiveness of reporting documented in the initial assessment.
9. In accordance with Requirement 4.5, PNG should undertake a comprehensive assessment of transactions between extractives SOEs (and their subsidiaries) and mining, oil and gas companies, as well as between the extractives SOEs (including their subsidiaries) and government in its scoping for future EITI Reports. All SOEs collecting material revenues or making material payments to government should be included in future EITI reporting.
10. In accordance with Requirement 4.6, PNG should establish whether direct subnational payments (to government entities) by extractives companies are material. Where material, PNG is required to ensure that direct subnational payments are reconciled between company payments and subnational government entities' receipts. Given widespread confusion yet vivid interest among stakeholders from all constituencies over extractives revenue flows accruing to subnational governments, PNG should to consider mapping out subnational revenue flows associated with each individual extractive project, drawing on results from the scoping study on subnational revenue flows being prepared in 2018.
11. In accordance with Requirement 4.9.a, the EITI requires an assessment of whether the payments and revenues are subject to credible, independent audit, applying international auditing standards. In accordance with requirement 4.9.b.iii and the standard Terms of Reference for the Independent Administrator agreed by the EITI Board, the MSG and Independent Administrator should:
 - Ensure that the Independent Administrator provides a clear and categorical assessment of comprehensiveness and reliability of the (financial) data presented, including an informative summary of the work performed by the Independent Administrator and the limitations of the assessment provided.
 - Ensure that the Independent Administrator provides an assessment of whether all

companies and government entities within the agreed scope of the EITI reporting process provided the requested information. Any gaps or weaknesses in reporting to the Independent Administrator must be disclosed in the EITI Report, including naming any entities that failed to comply with the agreed procedures, and an assessment of whether this is likely to have had material impact on the comprehensiveness and reliability of the report.

In accordance with requirement 8.3.c.i, the MSG should develop and disclose an action plan for addressing the deficiencies in the reliability of reporting documented in the initial assessment.

12. In accordance with Requirement 5.1, PNG should clarify which extractive revenues are recorded in the national budget. Where revenues are not recorded in the national budget, the allocation of revenues should be explained, with links provided to relevant financial reports. PNG is encouraged to publicly clarify the equivalence of revenue classifications in EITI reporting with those used in its national budget (e.g. group tax and corporate income tax) to strengthen citizen oversight of the budgetary process.
13. In accordance with Requirement 5.2, PNG is required to ensure that material subnational transfers of extractives revenues are publicly disclosed, when such transfers are mandated by a national constitution, statute or other revenue sharing mechanism such as benefit-sharing agreements. The MSG should also disclose any discrepancies between the transfer amount calculated in accordance with the relevant revenue sharing formula and the actual amount transferred between the central government and each relevant subnational entity on an annual basis. PNG is encouraged to reconcile these transfers.
14. In accordance with Requirement 6.1, PNG should ensure that reporting of mandatory social expenditures be disaggregated by type of payment and beneficiary, clarifying the name and function of any non-government (third-party) beneficiaries of mandatory social expenditures. To strengthen implementation, PNG may also wish to consider the feasibility of reconciling mandatory social expenditures.
15. In accordance with Requirement 6.2, PNG should undertake a comprehensive review of all expenditures undertaken by extractives SOEs (and their subsidiaries) that could be considered quasi-fiscal. PNG should develop a reporting process with a view to achieving a level of transparency commensurate with other payments and revenue streams, and should include SOE subsidiaries and joint ventures.
16. In accordance with Requirement 7.3, the MSG should consider introducing SMART objectives (specific, measurable, achievable, relevant and time-bound), in order to avoid recommendations which are seen by stakeholders as vague, difficult to implement or without deadlines.
17. In accordance with Requirement 7.4, the MSG is required to review the outcomes and impact of EITI implementation on natural resource governance in PNG by ensuring that all the prescribed details of the annual progress report are mentioned in the next report. The MSG should ensure that all stakeholders, including those outside of the MSG, are given an opportunity to participate in the production of, and have their view reflected in, the annual progress report.
