

II. TRADE AND INVESTMENT POLICY REGIME: FRAMEWORK AND OBJECTIVES

1. The Independent State of Papua New Guinea gained internal self-government in December 1973 and political independence from Australia in September 1975. It is a constitutional monarchy with the British Sovereign, represented by a governor-general approved by Parliament, as ceremonial Head of State. The national Government is elected for a maximum period of five years by universal adult suffrage. It is headed by the Prime Minister who, elected by Parliament, presides over and appoints ministers to the National Executive Council (the Cabinet).

(1) THE INSTITUTIONAL FRAMEWORK

2. Under the 1975 Constitution, legislative authority is vested in the single-chamber National Parliament. This provides for the separation of powers between the legislature, the executive, and the judiciary.¹ Parliament is based on the Westminster system, and consists of 109 Members representing 89 constituencies. A product of the political system and the fluidity of party allegiances has been a large number of short-lived coalition governments. No government or prime minister has yet seen out a full term in office, with no-confidence votes against governments being commonly successful. Governments therefore often change without recourse to public elections. In an attempt to foster greater political stability, the Constitution was amended in 1992 to increase from 6 to 18 months the statutory grace period accorded to new governments against parliamentary no-confidence votes.²

3. PNG comprises 19 provinces and the National Capital District of Port Moresby. Each province has its own elected member of the National Parliament. Provinces were created in 1977 under the Organic Law on Provincial Government. Each had their own constitution and elected assemblies and executives, with certain tax and revenue-raising powers to supplement national government grants. Provincial assemblies were accountable to Parliament and to the national Government. However, frequent disputes occurred between national and provincial governments over the distribution of powers and responsibilities. In 1995, this legislation was replaced by the Organic Law on Provincial Governments and Local-Level Governments. This abolished elected provincial assemblies and replaced premiers with centrally appointed governors. Provincial revenue-raising powers were also reduced, removing their authority to levy sales tax (legislatively capped at 5% but generally levied at a rate of 3%), for example, in return for increased conditional grants from the national Government, including transfers under District Support and Infrastructure Grants.³ The third tier of government covers a number of local government councils centred on townships, funded mainly by their respective provincial government.

¹ Constitutional changes are rare, and require an absolute two-thirds, or in some cases, a three-quarters parliamentary majority.

² This period was effectively increased to 24 months by the previous Government, which adjourning Parliament for seven months in December 1998 to avert an expected no-confidence vote. This delayed the implementation of key economic reforms announced in the 1999 Budget, thereby further undermining international confidence in the economy's outlook and the Government's commitment to economic reform. The decision to adjourn Parliament was subsequently declared unconstitutional by the Supreme Court in June 1999. On resumption of Parliament in July 1999, a new Government was voted into office following the resignation of the former Prime Minister.

³ Provincial governments on average collect about one quarter of their total revenue from internal sources, including from provincial sales taxes, natural resource royalties, fines, fees, and investments. Provinces are compensated for the elimination of provincial sales taxes by receiving from the national Government an agreed share of the new VAT. The national Government has reportedly failed to make grant payments in full to provincial governments, or to make adequate budgetary provisions for such transfers as required under the new Organic Law.

4. The new Organic Law is being implemented progressively, but the pace of reform has been slow. Several functions, such as greater responsibilities for education funding, have been or are in the process of being transferred from the national to provincial governments. District and provincial treasurers are responsible to the Secretary of the Ministry of Finance (now called Treasury and Planning), and must submit a financial statement annually. However, approval of provincial budgets – which cannot be in deficit – is the responsibility of the Minister for Village Services and Local-Level Government. Parliament can grant and withhold (through legislation) the powers of provincial and local governments.

5. Provincial governments have concurrent power with the national Government in many important areas, including agriculture, commercial and industrial development, forestry, fishing, transportation, labour, and mining. Thus, although national laws take precedent over provincial laws, provincial governments do play an important role in formulating and administering trade-related policies. They can make and enforce their own laws in these areas provided they do not conflict with national legislation.

6. The three-tiered legal system of PNG is based on English common law. The highest court, the Supreme Court, headed by the Chief Justice, is the final court of appeal and is responsible for hearing all constitutional matters. Next is the National Court of Justice, which has unlimited jurisdiction both in civil and criminal matters. There are also district and village-level courts, as well as specialized agencies, such as the National Lands Commission, to deal with customary land disputes and to handle civil cases relating to mining. The legal system has also adopted several traditional or customary local values required by the Constitution, particularly covering community land rights, which mainly affect foreign investors wishing to acquire land or rights to develop natural resources, especially minerals and forests.

(2) STRUCTURE OF TRADE POLICY FORMULATION AND IMPLEMENTATION

7. The principal ministries responsible for international trade matters and other economic policies are the Prime Minister's Department; Foreign Affairs and Trade; Commerce and Industry; Treasury and Planning; Agriculture and Livestock; Mineral Resources, Petroleum and Energy; Land and Physical Planning; Provincial Affairs; and Employment and Youth. A number of offices falling within various departments are also relevant, such as Public Enterprises, Rural Development, and Environment and Conservation. The National Planning Office was re-created in 1995 to improve development planning and aid coordination. The lead department in trade policy is the Department of Foreign Affairs and Trade. It handles international trade policy formulation and involvement in trade treaties and other trade-related agreements, including dealings with international agencies, such as the WTO and UNCTAD, as well as with foreign governments on regional and bilateral trade initiatives, such as APEC. It also deals with foreign policy.

8. There are a number of important sector-specific statutory authorities that also have a major bearing on trade-related policies. These include the PNG Forest Authority, the PNG Fisheries Authority and the PNG Tourism Promotion Authority. In addition, responsibilities for trade in services involve the Departments of Transport, Works and Civil Aviation, Communications, and Health and Education.

9. PNG's trade policies have been conducted on a largely ad hoc basis. No clear trade policy goals were set, and poor coordination of trade policies existed between responsible departments, especially between Foreign Affairs and Trade and Industry prior to trade and foreign affairs functions being amalgamated within the Department of Foreign Affairs and Trade. Trade policy formulation

was therefore fragmented and often lacked coherence. Major efforts are currently being directed at improving trade policy formulation and coordination.

10. The Bank of PNG, which is the Central Bank, plays a significant role in managing the country's monetary and exchange rate policies. In principle, the Bank is run by its Board and is independent from the Government. However, the responsible minister, the Minister of Finance (now Treasury and Planning), has broad statutory powers, under the Central Bank Act 1973, over monetary and exchange rate policies, and can direct the Bank to follow government policies.⁴ Disputes between the Minister and the Board are to be resolved by the Head of State, the Governor-General, on taking advice from the Government. Monetary policy is determined annually by the Bank's Board – comprising the Governor, Deputy Governor, Finance (Treasury and Planning) Secretary and six to eight additional members appointed by the Government – and is endorsed by the Minister before formal adoption as policy by the Bank. Thus, ultimate responsibility for setting monetary and exchange rate policies rests with the Government. The Government appoints the Bank's Governor, for a maximum period of five years. However, the legislation is ambiguous on the procedures for appointment, term of office, and criteria for the removal of the Governor. There have been several governors in recent years.⁵

11. Recent developments would appear to have undermined the Bank's capacity to pursue an independent monetary policy. The Bank, for example, failed in its legislative duty to suspend borrowings to the Government, despite having breached the maximum 25% statutory limit on outstanding central bank debt at end 1998. The Government had directed that commercial banks temporarily swap their cash reserves for Treasury Bills in order to meet a narrow interpretation of the statutory credit limits. However, PNG authorities indicated that the Government had exceeded this ceiling by 7 percentage points.⁶ The Bank also appears to have sanctioned a number of government quasi-budgetary arrangements surrounding the corporatization of the PNG Banking Corporation group of companies. It was announced in the 1999 Budget that the Bank would in future follow a more independent role in monetary policy: according to authorities, the Government would separate its debt management from the Bank's monetary policy implementation.

12. While the Bank's day-to-day intervention in the foreign exchange market to support the currency is at the Governor's discretion, overall exchange rate policy is determined in consultation with the Government. The Government announced in the 1999 Budget that it had followed an interventionist approach to exchange rate setting since August 1998.

13. As well as its supervisory functions over the financial system, the Bank plays an important general advisory role to the Government on monetary and banking matters, and on economic policy in general. It is also the major source of economic statistics on the PNG economy. The National Statistical Office has very limited resources;⁷ this impairs the preparation of reliable statistics, which in turn hampers the formulation and evaluation of policy. The Bank produces important regular public reports and commentaries on the state of the economy, including annual reports, quarterly bulletins, and updates. The Economic Policy Unit of the Department of Treasury and Planning also

⁴ Such directions are to be in writing and must be notified to Parliament within 15 sitting days from when the direction was given. The legislation first requires the Board to endeavour to agree with the minister on differences over policy matters.

⁵ The Minister may terminate the Governor's appointment, *inter alia*, if the incumbent "becomes permanently incapable of performing his duties" (Section 16 of Central Bank Act).

⁶ According to authorities, the Minister is required to present this breach to Parliament for endorsement.

⁷ Official GDP and other national account data have not been produced since 1993. Moreover, there are a number of deficiencies in statistics produced on balance of payments, prices, and government finances.

produces, somewhat irregularly, a *Monthly Economic Monitor* of economic statistics and a *Treasury Weekly Newsletter* highlighting important economic developments.

14. The customs division of the Internal Revenue Commission collects excise and trade taxes (import tariffs and export taxes). The Commission was formed in 1992 when the collection of all, including direct, taxes was unified upon the amalgamation of the Taxation Office and the Bureau of Customs and Excise. In the past, tariff changes were often proposed to the Government by the Industry Assistance Board, a statutory inter-departmental board chaired by the Commerce and Industry Secretary. However, this Board, which could hold public inquiries into matters of industry assistance, has been effectively defunct for many years. More recently, calls from industry for tariff changes have been considered by the Internal Revenue Commission, either directly from the industry concerned, or through the Council of Manufacturers and/or the Department of Commerce and Industry. The Commission therefore has both revenue collection and policy setting roles. The tariff reduction programme, for example, was primarily determined by the Internal Revenue Commission conducting a line-by-line review of the tariff schedule in close consultation with industry. Future tariff rate increases must be passed by Parliament, whereas tariff reductions require only the approval of the Government.

15. The Government, on the approval of the Minister for Treasury and Planning, may authorize exemptions, remissions, and concessions on trade and excise taxes. Such applications are handled by the Internal Revenue Commission in consultation with relevant departments. Proposals are examined on a case-by-case basis, and depend on the overall benefit to the economy of the project, such as export orientation and local procurement, as well as revenue forgone. Several legislative provisions are also included for specific exemptions of import duties based on end-use arrangements that benefit particular organizations or uses, such as the Lae Mackerel Cannery and mining and petroleum projects. Most import exemptions were removed, in April 1999, subject to "grandfathering" of existing arrangements. Price controls are administered by the Consumer Affairs Council using price levels and mark ups set mainly by the Treasury and Planning Secretary.

16. PNG has no independent statutory body to review or advise the government on economic policies, including the provision of government assistance to industry. Most policy advice to the Government comes from the Central Bank, or from international agencies, such as the IMF and the World Bank. The Institute of National Affairs was established in 1976 and functions as a privately funded "think tank" aimed at providing independent advice to the Government. It commissions public research into areas of current economic interest and liaises with government through various channels, including regular meetings of the Consultative Implementation and Monitoring Council, formed by the Government in 1998 to promote public dialogue; and the National Development Forum, the latest held in August 1999 on reconstruction and the 2000 Budget. The Industry Assistance Board replaced the Tariff Advisory Committee, principally to advise the government on industry assistance, however, it has seriously lacked the institutional capacity and government commitment to be effective.

17. The private sector has established a close working relationship with the Government, mainly through the PNG Manufacturers' Council, which consults regularly with government departments and statutory bodies. The private sector is therefore actively represented in the decision-making process. Many government delegations to various conferences and negotiations involve private sector representation. Other private associations include the Business Council of PNG, the Chamber of Commerce, and the Chamber of Mines and Petroleum. An Economic Summit was held in February 1998 to enable the private and public sectors to engage in public dialogue on matters of key economic interest. This resulted in the formation of eleven sectoral committees to look at areas such as health, education, commerce and industry, forestry, fishing, agriculture, infrastructure, and order.

18. An Indirect Tax Summit held in September 1996 laid the foundations for the package of VAT and tariff reforms implemented on 1 July 1999.

(3) IMPLEMENTING THE STRUCTURAL ADJUSTMENT PROGRAMME

19. The previous Government reaffirmed in its 1999 Budget, released in November 1998, its commitment to implementing structural reforms. These are seen primarily as a continuation of reforms under the Structural Adjustment Programme agreed with the IMF and the World Bank in 1995. A number of key reforms were introduced in 1995 and 1996 (Box II.1). However, since then the programme has stalled badly, and a large unfinished agenda remains to be implemented. Many of these outstanding reforms were directly incorporated in the previous Government's Economic Recovery Package.

Box II.1: 1995 Structural Adjustment Programme

As part of the 1995 budget, the Government announced a Structural Adjustment Programme aimed at regaining macroeconomic stability and improving the economy's international competitiveness. The reform programme was agreed in consultation with the World Bank, the IMF, and other major aid donors. Its main elements were to:

- establish a market-determined exchange rate;
- raise the minimum liquid assets ratio and introducing a weekly kina auction;
- limit the fiscal deficit to 1%;
- undertake reforms to enhance competitiveness and restore business confidence;
- create the basis for sustainable development of renewable natural resources, particularly forests;
- replace import bans (e.g. sugar, cement, beef, and lamb) with tariffs;
- reform and downsize the public sector;
- improve public services, especially education, health, and agriculture;
- upgrade public infrastructure needed for private sector development; and
- divert development resources to the rural sector.

During the year of the Structural Adjustment Program in 1995, the Government made progress in a number of key areas. It:

- contained the fiscal deficit to 1% of GDP;
- established a floating exchange rate regime;
- introduced market-determined interest rates;
- removed Central Bank guidelines for spreads of commercial interest rates on deposits and lending;
- raised the minimum liquid assets ratio;
- deferred sitting of the Minimum Wages Board;
- began to reduce the size of the public service;
- subjected government agencies to import duties;
- reintroduced value-based taxation of fringe benefits;
- established monthly ceilings on public expenditure;
- set 25% targets for public expenditure on education, health, agriculture, and infrastructure;
- reduced import duties on industrial inputs;
- initiated studies on tariffs and value-added taxation;
- established the National Economic Development Forum;
- introduced surveillance and monitoring of log exports and ocean fisheries;
- provided additional funding for the National Forests Authority;

Box II.1 (cont'd)

established a logging code of conduct;
introduced a progressive taxation and royalty system for log exports;
legislated for transfers of additional funding to provincial and local governments; and
announced a five-year programme for reducing import duties, including on beef, lamb, and cement.

Implementation of the Structural Adjustment Program continued in 1996 but proved more difficult. Moreover, a number of these announced decisions were subsequently reversed or delayed indefinitely.

Source: Asian Development Bank (1997a), *Country Economic Review of Papua New Guinea*, Manila.

(i) Economic Recovery Package

20. The previous Government announced, in June 1999, Economic Recovery Package to be implemented in line with the Structural Adjustment Programme, aimed at reinforcing macroeconomic stability, boosting public confidence in the economy, and deepening structural reforms. The package contained fiscal, monetary, exchange rate, and structural reform policies to ensure that the 1999 Budget and macroeconomic framework remained on track (Box II.2). The Government believed that further tightening of fiscal and monetary operations were needed to cope with the continued pressure on the exchange rate and international reserves. Implementation of these reforms was to begin immediately.

21. The Economic Recovery Package included principally economic reforms yet to be completed under the Structural Adjustment Programme – it contained few new initiatives. Fiscal reforms included expenditure control and revenue enhancement measures aimed at limiting the overall 1999 budget deficit to less than 1% of GDP. Revenue measures included mainly improved enforcement and compliance procedures for collecting direct and indirect taxes, but also non-specified future increases in log export taxes and certain other taxes. Monetary and exchange rate reforms involved, in particular, a tightening in monetary conditions and continued active intervention in the foreign exchange market by the Central Bank to maintain an appropriate level of international reserves. The main structural reforms covered taxation, with the introduction of VAT, and tariff reductions that began on 1 July 1999; the public sector; labour markets and minimum wages; the quality of economic data and reporting; privatization; and the financial sector.

(ii) The 1999 Budget

22. Key features of the previous Government's reform programme, announced earlier in its 1999 Budget, included:

- maintaining economic and financial stability, including the introduction of the VAT from 1 July 1999, and improved performance of statutory corporations (minimum 10% return) and public asset sales;
- promoting rural development;
- reforming the public sector, including major public service downsizing, termination of 15 statutory authorities, agencies, and committees, at an estimated cost of K 65 million in 1999, to be funded largely by the proceeds of asset sales;
- private sector development, including implementation of the tariff reform programme (endorsed by Parliament in September 1998) from 1 July 1999, as well as introducing

a national investment policy aimed at investment liberalization and removal of all import duty exemptions granted under the Pioneer Industries Act, rationalization of investment incentives, and the implementation of a comprehensive privatization programme aimed at selling initially government plantations, the PNG Banking Corporation, Telikom, and public equity in mining ventures;

- financial sector reform, including the deepening of the foreign exchange and treasury bills markets, the establishment of a Stock Exchange (which commenced operations in May 1999) and more effective central bank supervision of banks and especially non-bank financial institutions; and
- sectoral reforms, including streamlining of the incentives framework for promoting mineral and petroleum development; as well as provincial and local government reforms to speed up implementation of the 1995 new Organic Law, including cuts in financial grants to provinces in line with the Government's tight budgetary position.

Box II.2: The Economic Recovery Package

Announced by the **previous** Government on 7 June 1999, the comprehensive package contains measures to reinforce economic and financial stability and to deepen structural reforms. The background to the package, according to the Government, was the deteriorating public confidence in the economy, caused by spiralling prices due to a steady decline in the exchange rate. This had encouraged capital flight, and was threatening macroeconomic stability. The package contained fiscal, monetary, exchange rate, and structural reforms.

Fiscal reforms are directed at a tight stance to limit the overall budget deficit in 1999 to under 1% of GDP, to be entirely funded by the least expensive source of external financing. Measures announced included expenditure controls to limit public expenditure to essential payments and avoid spending overruns and new commitments, saving an estimated K 20 million in 1999. Revenue enhancing measures, expected to raise additional funds of K 85 million in 1999 when fully implemented, include a range of improved revenue collection initiatives on direct and indirect taxes. Some future tax increases are also proposed, such as raising log export duties in July aimed at generating an extra K 20 million in 1999. The Government intended to intensify dialogue with the World Bank and the IMF aimed at securing finance for the 1999 Budget. Alternative sources of external finance would also be developed. These would include a line of credit for US\$100-120 million with offshore commercial banks, and PNG's inaugural Eurobond float of up to US\$250 million.

Monetary policy and exchange rate reforms are aimed at establishing price and currency stability. Monetary conditions are to remain very tight pending availability of foreign financing and rebuilding of international reserves to comfortable levels. The Central Bank is to maintain a market-determined exchange rate and will actively intervene to maintain an appropriate level of reserves. Foreign retention guidelines will be strengthened. Restrictions are also to be removed on current account transactions, and prudential measures are to be enhanced.

Structural reforms cover tax changes, including tariff and excise tax reform and the introduction of VAT; completion in 1999 of public sector reforms to improve service delivery; labour market reforms to allow payment of piece rates and to conclude the current minimum wage review; improving the quality of economic data and reporting; completing the 1999 privatization programme; and a range of reforms to the financial sector.

Commencement of these reforms is to begin immediately by the Budget Implementation Committee in close cooperation with key departments, such as Treasury and Planning, Internal Revenue Commission, and the Central Bank.

Source: Government of Papua New Guinea.

23. A ministerial Budget Review Committee (BRC), chaired by the Secretary of Treasury and Planning, was formed after the 1999 Budget to oversee its implementation and that of the reform programme generally. The BRC reports to the Cabinet sub-committee on Economics and Finance, which is chaired by the Minister of Finance (Treasury and Planning). It is assisted by thirteen sectoral working groups comprising both departmental heads and ministers. Another committee, the Budget Implementing Committee (BIC), reviews submissions from the working groups before they are considered by the BRC. Other policy proposals are considered by the National Development Advisory and Implementation Committee before consideration by the National Planning Committee, and then by the National Executive Committee (NEC).

24. However, there appears to be considerable duplication and inefficiency associated with the current arrangements, together with deficiencies in the established procedures for the presentation and processing of policy submissions to the NEC. A number of NEC decisions have been reversed after a short time or challenged in the courts. It seems that the National Development Advisory and Implementation Committee and the National Planning Committee have become redundant, and that instead the BIC and BRC have become the main avenues for considering most submissions even if unrelated to implementation of the 1999 Budget or the reform programme.

25. In January 1999 an Advisory Secretariat was established to support the Office of the Prime Minister on sectoral issues, including overseeing National Executive Council decisions and implementation of the 1999 Budget. The Secretariat has responsibilities in areas of public service and provincial governments; legal, law and order; economic, finance, commercial statutory authorities, privatization, and natural resources, chaired by the Prime Minister's Chief Economic Advisor; infrastructure, budget implementation and foreign aid management; health and education; family, church and non-government organizations. Located within the Prime Minister's Office, the creation of the Advisory Secretariat is seen as an integral part of the reform process.

(iii) The August 1999 Supplementary Budget

26. The incoming Government of July 1999 moved quickly to restore international confidence in the economy and to address the looming financial and currency crisis, including re-opening discussions with the World Bank and the IMF aimed at obtaining the necessary external financing. The Government introduced a supplementary budget on 12 August 1999 aimed at maintaining the 1999 budget deficit to 1.7% of GDP (Box II.3).

(4) POLICY OBJECTIVES

27. The Government has embarked on an overall policy of gradual trade liberalization as part of its continuing Structural Adjustment Programme. It recognizes the increasing role that marketing-opening measures must play in improving the economy's competitiveness and diversification of exports and markets. The need for private-sector-led development, by redirecting resources away from the public sector, is also recognized. The Government is attempting to formulate a coherent trade policy that will foster outward orientation and improved trade performance.

28. The authorities regard private investment, both domestic and foreign, as an important catalyst for growth. Therefore, the Government is keen to remove administrative obstacles to investment, to improve the transparency of investment policies, and to create an atmosphere designed to restore business confidence.

29. A major objective of the Government's reform programme is to implement sustainable management policies with regard to its key natural resources, such as forests, marine, mineral, and agricultural commodities. Economic self-reliance is to be achieved through implementation of

policies aimed at promoting sustainable development. Implementing effective control over the exploitation of such resources and encouraging greater domestic processing are seen as important government priorities.

Box II.3: August 1999 Supplementary Budget

The 1999 Supplementary Budget delivered by the incoming Government in August was aimed at restoring macroeconomic and budget stability. Corrections were considered necessary due to the 1999 Budget being formulated on overly optimistic assumptions and unrealistic policy initiatives. The Supplementary Budget introduced a distinct shift in the Government's fiscal stance. It aims for a surplus of 0.6% of GDP for the last half of 1999, compared with a 2.3% deficit for the first six months, to achieve an overall deficit for the year of 1.7%, or K 265.7 million. This would have risen to 3.1% had the budget been left unchanged.

The budget deficit is to be funded entirely from external sources, such as the IMF and the World Bank, thereby creating no new domestic financing requirements for 1999. The Budget also proposes a major privatization programme to be completed by 2002, which would be used to secure an external loan, to be used to reduce domestic public debt by retiring Treasury Bills held by the Central Bank. The Supplementary Budget was designed to prepare the foundation for the 2000 Budget to be endorsed by the IMF and the World Bank. In the meantime, public expenditure and taxation reviews would be conducted.

The Supplementary Budget introduced new tax measures to raise an estimated additional K 72.4 million in 1999, and expenditure reductions worth K 140 million. Revenue measures comprised increases in excise taxes on fuel, tobacco products, and alcoholic beverages, as well as a higher luxury excise tax rate of 110% (compared with 60%) on passenger motor vehicles with an engine capacity of 2,800 cc and above. The temporary relief granted to loggers in 1998 was removed and the log export taxes restored to their previous levels. In addition, the 4% mining levy was retained, while the interest withholding tax, introduced in the 1999 Budget on resource industries, was terminated.

The Supplementary Budget is based on the incoming Government's economic objectives of:

- restoring integrity to state institutions and respect for the laws;
- stabilizing the exchange rate at a realistic level by a consistent mix of fiscal and monetary policies that will also contain inflation;
- focusing on fewer priorities, including less impingement on commercial activities by the Government, while privatizing public institutions for fair returns; and
- improving business opportunities for all by removing investment barriers, as well as privatizing and improving price competitiveness of utilities.

Source: 1999 Supplementary Budget, Minister for Treasury, August 1999.

30. Government policy is no longer geared heavily towards import substitution strategies. This approach dominated economic policies from independence until the late 1980s and early 1990s. According to authorities, since then there has been a progressive move by successive governments towards export-oriented policies, and this is currently the main trade policy objective. The major objectives of trade policy are to develop an open, outward-looking and export-oriented economy that generates rapid rates of growth and higher living standards. While the importance of the mining sector will continue, higher growth in the non-mining sector is also being targeted.

31. The Government's primary development policy objectives are job creation and improved delivery of public services, especially in rural communities. These are contained in the "Medium Term Development Strategy 1997-2002; a Bridge into the 21st Century (MTDS)", adopted by Parliament in 1996. The main objectives of the five-year rolling plan is to adhere to structural adjustment policies; to redefine and limit the functions and role of the Government as a facilitator of

development; to redefine the role of the private sector as the main source of growth; to ensure effective provincial government; and to focus resources on human resource development. The MTDS provides the Government's main policy statement in its agenda for economic and social development to meet the National Goals and Directive Principles laid out in the Constitution. It is also aimed at better integrating the planning and budgetary processes. The Government's expenditure and investment plans on specific development projects are contained in its five-year Public Investment Programme.

32. As part of the MTDS, a medium-term resources framework was also developed, aimed at improving the performance of government activities in priority sectors. The Government also adopted in 1997, as the basis for its development of sustainable human resource development, the "Country Strategy Note 1997-2002: Sustainable Human Development; Integrating Economic, Social and Environmental Development in PNG", devised in conjunction with major aid donors. The 1999 Budget strategy of redirecting resources away from recurrent to developmental expenditures reflects these principles and those contained in the development plan. Priority areas of development expenditure include rural development and agriculture; health; education; infrastructure maintenance and development; law and order; and capacity building within institutions at all levels of government.

33. To help sharpen the focus of the development strategy, the National Planning Office was reformed in 1995, and is intended to play a leading role in the structural reform process. As well as monitoring and coordinating the development budget and facilitating public sector reform, the Office is to assist provincial administrations in development planning and to develop comprehensive policies for the non-renewable resource sectors.

34. The Government views greater integration of the PNG economy with the world economy as a high priority. It believes that the conclusion of the Uruguay Round and its membership of the WTO provide important challenges and opportunities, and is attempting to bring its domestic policies into conformity with its WTO commitments. It is also committed to APEC objectives and is gradually changing its sectoral policies to comply with these requirements. The Government believes that meeting these trade liberalization objectives should improve the country's production and bring resource allocation more into line with its comparative advantage.

35. PNG's economic and trade relations with Asian and Pacific neighbours are also taking on increasing importance, as reflected in the Government's "Look North" and "Work the Pacific" initiatives. The "Look North" policy is aimed at increasing trade and investment ties with Asia, while the "Work the Pacific" is aimed at strengthening relations with South Pacific neighbours. The Government in principle supports the establishment of regional free-trade areas as an opportunity to further develop trading relations with neighbouring countries.

(5) LAWS AND REGULATIONS

36. The laws of PNG consist of the Constitution and those adopted by Parliament either under the Constitution or in the normal course of government business. The constitutionally based Organic Law provides for provincial and local governments and contains the division of powers and responsibilities between the three layers of government. The national Government also makes emergency regulations and subordinate legislation. Customary (called the underlying law) is also relevant in some areas, such as land rights. Provinces are able to make their own laws and regulations governing areas of their responsibility.

37. Laws are enacted by Parliament and become operative after receiving certification by the parliamentary Speaker and publication in the *National Gazette*. In addition, relevant ministers issue enabling regulations, guidelines, and administrative directives.

38. Treaty-making powers are vested in the national Government by the Constitution (Section 117). However, international treaties or conventions are not domestically applicable unless implemented in domestic legislation. Where there is applicable domestic legislation covering an aspect of WTO requirements, any person can, in principle, enforce these provisions through the National Court (Section 155 of the Constitution). Although PNG's accession to the WTO did not, according to authorities, adhere strictly to constitutional procedural requirements for practical reasons, it was ratified by Parliament and hence PNG's laws and regulations must conform to its WTO obligations. Although domestic law would in principle prevail in the case of inconsistencies with international treaty obligations, such as those of the WTO, the PNG Government would take steps to ensure that domestic laws and regulations reflected its international obligations.

39. The main trade-related laws in PNG are the Customs Act; the Customs (Dumping and Subsidies) Act; Exports (Control and Valuation) Act; Commercial Advertisement (Protection of Local Industries) Act; Foreign Exchange Control Act; Land Act 1996; and the National Institute of Standards and Industry Technology Act. In addition, there are a number of specific Acts that cover the development of particular sectors, such as mining, forestry, and fishing. These include mainly the Mining Act 1992, Oil and Gas Act 1998, Forestry Act 1991, and Fisheries Management Act 1994.

(6) TRADE AGREEMENTS AND ARRANGEMENTS

(i) Multilateral agreements

40. With minor exceptions, PNG accords MFN treatment to all trading partners. As a de facto member of the GATT, from 1960, by virtue of its status with Australia, PNG could become a GATT contracting party following independence on assuming full autonomy in the conduct of its external commercial relations. The PNG Government exercised this right on 16 December 1994. PNG became an original Member of the World Trade Organization on 9 June 1996 when it accepted the WTO Agreement (Article XI of the Marrakech Agreement).⁸ PNG is not a signatory to any of the WTO Plurilateral Trade Agreements. The status of PNG's notifications to the WTO is given in Table II.1.

41. PNG's sector-specific commitments under the General Agreement on Trade in Services (GATS) on market access and national treatment cover a broad range of services. These are business services (professional legal, accounting, architectural, and engineering services, consultancy services covering computer hardware installation, management consultancy services); communication services (courier services, excluding letters and postcards); construction (general construction work for buildings and civil engineering); certain financial services, such as banking services; hotels and restaurants; maritime transport services; and certain basic telecommunication services, including voice telephony.⁹

⁸ Like other developing countries, PNG was given an additional year, until 15 April 1995, to submit its schedules on goods and services. However, this period was extended by WTO Members at the Government's request to 13 August 1996.

⁹ GATS/SC/118, 16 November 1995 and GATS/SC/118/Suppl.1, 11 April 1997.

Table II.1
Notification requirements to the WTO as at 30 June 1999

WTO Agreement	Description of requirement	Periodicity	Status as at August 1999 and document number of latest notification
Agriculture (Art. 18.2)	Domestic support	Annual	Outstanding
Agriculture (Art. 10 and 18.2)	Export subsidies (outlays and quantities)	Annual	Outstanding
Subsidies (Art. 32)	Laws and regulations	Once by March 1995, then changes	Outstanding
Subsidies (Art. 25)	Specific subsidies granted	Annual	Outstanding
Subsidies (Art. 25.11)	Countervailing duty actions taken	Every six months when measure is taken	No notification received
Anti-dumping (Art. 18)	Laws and regulations	Once by March 1995, then changes	Outstanding
Anti-dumping (Art. 16.4)	Anti-dumping actions taken	Every six months preliminary or final anti-dumping actions	No notification received
Safeguards (Art. 12)	Laws and regulations	Once by March 1995, then changes	Outstanding
Safeguards (Art. 12)	Investigations and actions taken	Ad hoc	No notification received
Technical Barriers to Trade (Art. 15.2)	Administrative arrangements taken to implement Agreement	Once by March 1995, then changes	Outstanding
Preshipment Inspection (Art. 5)	Laws and regulations that put the Agreement into force	Once, then changes only	Outstanding
Import Licensing Procedures (Art 7.3)	Questionnaire; rules and information concerning procedures for the submission of applications	Annual for questionnaire; rules and information once, then changes	Outstanding; G/LIC/N/2/PNG/1, 24/07/1998
Import Licensing Procedures (Art.1.4(a) and 8.2 (b))	Laws and regulations relevant to import licensing	Once, then changes only	Outstanding
Customs Valuation (Arts. 20.1 and 22.1)	Delay in commencement of provisions and changes in laws	Once on delay, then changes only	Outstanding
Rules of Origin (Art. 5.1 and Annex II, para. 4)	Preferential and non-preferential rules of origin	Non-preferential in April 1995; preferential as soon as entry into force	Outstanding
Trade-related Investment Measures	Notifications under Article 6.2 of the TRIMS agreement of publications in which TRIMS may be found	By February 1997 or upon membership	Outstanding
GATT 1994 (Part IV)	Enabling Clause	Ad hoc	No notifications received
GATT Council of Trade in Goods on State Trading (Art. XVII:4(a))	State trading entities and activities	Annual	Outstanding
GATT Council for Trade in Goods, G/L/59	Complete notifications on non-tariff measures	Every two years, beginning January 1996	Outstanding
GATS (Art. 3.1)	Alterations to rules governing scheduled sectors	Annual	No notification received
TRIPS (Art. 63.2)	Laws and regulations	Once, then changes	Outstanding; IP/N/1/PNG/1, 21/07/1998
TRIPS (Art. 63.2)	Arrangements for patent protection on pharmaceutical and/or agricultural chemicals	Ad hoc, but only if patent protection on these goods not already granted	No notification received

Source: WTO documents.

42. PNG made horizontal GATS commitments on two modes of supply. Commercial presence by foreign service providers is subject to normal approval and registration requirements for all foreign investors by the Department of Treasury and Planning.¹⁰ Externally incorporated firms must register their name with the Investment Promotion Authority. Foreign nationals and foreign-owned firms cannot purchase freehold land but must lease it from Government or land-holding groups. Financial service providers are subject to approval from the Central Bank. The temporary movement of managers and specialists who possess necessary skills unavailable locally is limited initially to three years with extensions subject to labour and employment requirements.

43. The authorities hope that the incorporation of agriculture into the WTO will improve world prices for tropical oil products by constraining the use of subsidies by the European Union and the United States. Such subsidies are seen as a major factor behind the continually low prices received for copra and coconut oil exports.

44. The Government is keen to ensure that its domestic legislation conforms to its WTO commitments. A priority area is intellectual property, and new legislation on copyrights, patents and industrial designs, and trade marks have been drafted since PNG joined WIPO in December 1996. Other areas requiring changes and receiving priority include customs valuation, safeguards, and anti-dumping arrangements. These are largely the responsibility of the Internal Revenue Commission.

(ii) Regional agreements

(a) The Lomé Convention

45. Papua New Guinea became a signatory in 1978 to the Lomé Convention between the European Union (EU) and 70 countries in Africa, the Caribbean and the Pacific (ACP). There are seven other Pacific ACP States.¹¹ The current (fourth) Lomé Convention extends non-reciprocal trade preferences to all ACP States, and is due to expire end-February 2000. According to the authorities, the Lomé Convention has been important for the development of tree crops and the export of canned tuna products.

46. Imports from ACP States enter the EU free of duty and quantitative restrictions, subject to a safeguard clause and rules of origin.¹² Commodities covered by the EU Common Agricultural Policy may be excluded from preferential treatment. The only PNG export benefiting from preferential duty-free access to the EU market under Lomé IV is canned tuna. Without this, it is doubtful whether the foreign-owned cannery at Madang, which commenced operations in 1997, would be able to compete in the EU, its main export market. Other canned tuna imports enter the EU at a tariff rate of 24%. These tariff preference margins will, however, be reduced over time as the EU lowers its MFN rates on fish products in accordance with its WTO commitments.

47. The Government is concerned that the extension by the EU of Lomé tariff preferences to all least-developed countries, including non-ACP countries, as of 1 January 1998, in line with WTO

¹⁰ These criteria are the provision of new services; improvement of the economy's productive structure; viability of the project with respect to foreign exchange savings or earnings; and employment implications.

¹¹ The others are Fiji, Kiribati, Samoa, Solomon Islands, Tonga, Tuvalu, and Vanuatu.

¹² The Lomé IV rules of origin require that qualifying products be either wholly obtained or "significantly worked or processed" in one or more ACP States. The latter definition is based on the product being sufficiently modified in the ACP State for it to be classified under a different four-digit HS tariff item.

requirements, will intensify competition for key exports, especially tuna but also coconut products, cocoa, palm oil, and timber.

48. According to the authorities, PNG has not fully utilized the Lomé trade preferences available because of stringent and cumbersome procedures that have to be followed in order to receive such preferences. The main areas of concern for PNG are the rules of origin requirements; poor shipping services to the EU; EU quarantine requirements; and EU standards and conformance requirements. In the case of canned tuna exports, duty-free access to the EU market is currently allowed under temporary arrangements, pending the outcome of negotiations on these products meeting the rules of origin requirements.

49. PNG has also received substantial financial assistance from the EU under the Lomé arrangements, amounting in total to K 2.8 billion as at December 1995. The EU provides support to ACP States through the European Development Fund (EDF), the main assistance arm of the EU; the European Investment Bank for commercial loans; the Stabilization of Export Earnings Scheme (STABEX), which currently covers 49 agricultural products and is aimed at reducing the effects of price or quantity fluctuations on export earnings; SYSMIN a financing facility for minerals; and development projects funded under the National Indicative Programme (NIP). Almost two thirds of EU support to PNG has been provided under the NIP, mainly on rural roads and training programmes. Most of the remaining assistance has been provided from STABEX funds (K 589 million), the sixth largest beneficiary from such assistance, and EIB loans (K 247 million). STABEX assistance was used in PNG to fund the price support schemes for cocoa, coffee, cocoa, and oil palm growers.

50. The Lomé Convention is currently being renegotiated. PNG together with other Pacific ACP States agreed in 1997 to support the expansion of the ACP to include other Pacific island countries. As the WTO waiver for the EU to provide trade preferences under the Lomé Convention expires at the conclusion of Lomé IV, continuation of these arrangements will require another means of achieving WTO compatibility.

51. One proposal being considered to replace the Lomé Convention is the creation of a Regional Economic Partnership Agreement (REPA) between the EU and the developing Pacific ACP States of PNG, Fiji, and Tonga. The EU is committed to negotiating a reciprocal free-trade area with these States after the expiry of Lomé IV in February 2000.¹³ Other alternatives being examined include an enhanced GSP scheme provided by the EU, and the possibility of continuing preferential access to the EU under commodity-specific waivers at the WTO after 2005.¹⁴

(b) Forum for Asia Pacific Economic Cooperation (APEC)

52. This forum was launched in 1989 to enhance regional economic cooperation and the liberalization of trade and investment measures in the Asia Pacific region. There are now 21 members of APEC, following the admission of Russia, Peru, and Viet Nam in 1999. PNG joined APEC in 1994.

53. APEC economies are committed to the Bogor objectives of voluntarily achieving free trade and investment in developed economies by 2010, and by 2020 for developing members. Liberalization is to be comprehensive by including agriculture and services, and non-discriminatory,

¹³ The EU has agreed to a two-stage process, with a preparatory period of five years followed by a transition to free trade over a period of 12 years (by the year 2017). Under the proposal, developing island economies will be required to provide reciprocal access to the EU. PNG, as a developing economy, will therefore be required to provide the EU with reciprocal duty-free access.

¹⁴ South Pacific Forum (1999).

based on the concept of "open regionalism" that is to be fully consistent with the WTO. The three pillars of APEC are trade and investment liberalization; facilitation; and economic and technical cooperation.

54. To meet these commitments, APEC economies agreed in Manila in 1996 to submit comprehensive plans, known as individual and collective action plans, on how they would proceed in meeting APEC objectives. PNG submitted its Individual Action Plan in 1997.

55. In 1997, APEC economies adopted the so-called Early Voluntary Sectoral Liberalization (EVSL) initiative, aimed at advancing trade liberalization in certain sectors. Members agreed on 15 sectors, of which nine were to be fast-tracked for liberalization. PNG participated in these negotiations and supported other members in the nomination of several sectors for early liberalization, including food, chemicals, and transport equipment. APEC economies decided in 1998 to transfer such initiatives to reduce tariffs in these sectors to the WTO, while continuing to advance liberalization of non-tariff measures in these sectors.

56. PNG views APEC's trade liberalization and other initiatives as crucially underpinning its own domestic reforms, and, according to the authorities, is continuing to take steps consistent with implementing its Individual Action Plan.

(c) South Pacific Regional Trade and Economic Agreement (SPARTECA)

57. This trade and economic cooperation agreement, concluded in 1981, provides Forum island countries (FICs) with non-reciprocal preferential treatment on goods exported to Australia and New Zealand.¹⁵ Its objectives are to achieve progressively duty-free and unrestricted access for a wide range of products to Australian and New Zealand markets for FICs; to accelerate FIC development through expansion and diversification of their exports to Australia and New Zealand; to facilitate expansion and diversification through elimination of trade barriers; to promote FIC exports through promotion of investment; to promote FIC exports in Australia and New Zealand by cooperatively marketing and promoting such products in these markets; and to promote and facilitate economic and technical cooperation. It includes special provisions for the smallest FICs, but these are not applicable to PNG.

58. Since 1 July 1986, FIC exporters have been eligible under SPARTECA for free and unrestricted access to the Australian market, except for textiles, clothing and footwear, and sugar.¹⁶ Australia removed the limitation on TCF products from 1 March 1993, and on sugar from 1 July 1997 when it eliminated sugar tariffs. Rules of origin must be met, however. These require the last process of manufacture to be carried out in the country claiming the preference, and for products to have at least 50% local content in that country.¹⁷ Australia or New Zealand may vary or suspend preferential access under special safeguard provisions, and actions against dumped or subsidized exports are handled according to each country's national legislation.

¹⁵ The FICs are the Cook Islands, Federated States of Micronesia, Fiji, Kiribati, Republic of the Marshall Islands, Nauru, Niue, Palau, PNG, Samoa, Solomon Islands, Tonga, Tuvalu, and Vanuatu.

¹⁶ From 1981 to 1986, the FICs received duty-free and unrestricted entry on a fixed list of products and duty-free and restricted entry on a further short list of products.

¹⁷ Also counted as local content are inputs from any or all FICs, as well as from Australia and New Zealand (up to 25% of the required 50% minimum). In July 1994, New Zealand reduced the local-content requirement to 45% for garments imported from Fiji, while Australia agreed to include more marketing and packaging elements in the calculation of local content for these products.

59. Economic cooperation and development provisions were expanded in 1994 to cover assistance in the areas of institutional capacity for export development; inter-island trade; consumer protection and standards; harmonization of trade law; and quarantine management capabilities. Australia, for example, funds the South Pacific Trade Commissioner located in Sydney to help promote and market FIC products in Australia.

60. The preference margins available to FIC exporters have been eroded following tariff reductions in Australia and New Zealand. Consequently, the importance of SPARTECA to PNG has declined and will continue to do so.

61. SPARTECA was notified initially to the GATT under the Enabling Clause in 1971. The extension of the agreement in 1980 to Nauru and Vanuatu by New Zealand was notified in 1982.

(d) South Pacific Forum

62. PNG, along with other FICs, Australia, and New Zealand, is a member of the South Pacific Forum. It was established in 1971 to develop a collective response to a number of regional issues, and its Secretariat is located in Suva, Fiji. Forum leaders meet annually; forum economic ministers also meet annually (since 1997) at the Forum Economic Ministers Meeting (FEMM). Trade ministers met for the first time in Fiji in June 1999.

63. The 1997 FEMM adopted an Action Plan whereby Ministers made commitments to develop individually comprehensive national economic reform strategies. The Action Plan provided for adoption of principles of best practice for public accountability; open, liberal, and transparent investment policies, consistent with the APEC non-binding investment principles; and to work towards a common goal of free and open trade and investment on a unilateral basis. Ministers agreed to rationalize and progressively reduce tariffs, in accordance with several guiding principles, while recognizing the specific requirements of some smaller FICs, and to introduce administrative reforms to facilitate trade.¹⁸ They also agreed to consider the acceleration of tariff reductions for agreed sectors, and for goods and services typically traded within the region.

64. Economic ministers, recognizing that preference margins under agreements such as Lomé and SPARTECA are diminishing, also agreed to implement, to the extent practicable, domestic measures consistent with WTO and APEC principles and obligations, and to report on policy changes taken to achieve this objective.

65. The FEMM Action Plan was endorsed by leaders at the Forum meeting in September 1997. They reaffirmed their commitment to free and open trade among Forum island countries through tariff reform and by ensuring investment transparency, and supported the creation of a Free Trade Area between Pacific island nations. The Forum holds observer status in the Asia Pacific Economic Cooperation (APEC) and the WTO, and will play an important role in assisting nations to achieve these objectives.

66. Ministers agreed at the FEMM held in Fiji, during July 1998, to further develop a framework for achieving a free-trade agreement among Forum members that would be WTO consistent and pay due regard to the benefits both from preferential and non-preferential approaches. Telecommunications, energy, and transport sectors were also endorsed for further consultations on

¹⁸ These guiding principles for tariff improvements are: not to use protective tariffs; to use a standard general rate; to provide a duty drawback system to exporters; to use *ad valorem* rates, unless serious valuation and problems exist; to levy tariffs on c.i.f. and not f.o.b. or current domestic value (CDV); and on those goods that have high tariffs for social, health or environmental reasons to levy a similar excise duty on domestic goods.

advancing the non-preferential tariff reductions. Ministers also agreed to implement domestic measures consistent with WTO and APEC principles and obligations. In preparation for the next round of WTO trade negotiations, members supported the formation of alliances to focus on agricultural liberalization; fishing subsidies; trade and environment; trade in services; government procurement; trade and competition policy; and investment policy. These matters were further discussed at the FEMM in Samoa in July 1999.

67. Trade matters, such as the formation of a free-trade area, were further examined at a meeting of Forum trade ministers held in Fiji during early June 1999. They endorsed in principle a free-trade area among Forum island countries, to be considered by Forum Leaders in Palau in October 1999, and agreed to negotiate a draft framework agreement. The agreement, based on negative lists of exempted products, is expected to be implemented for goods in 2001 with tariffs to be eliminated over a number of years. Additional work is to be conducted on the effects of including services trade and on extending the agreement to French and U.S. Pacific island territories and on longer term integration with the Closer Economic Relations Trade Agreement (ANZCERTA) between Australia and New Zealand.

68. Although such regional initiatives should be considered, a free-trade arrangement, especially without Australia and New Zealand, would in all probability mainly divert trade, thereby providing only illusory trade liberalization and economic benefits to members. Empirical studies show only small economic gains are likely from such an agreement.¹⁹ This could undermine PNG's long-term economic interests if, in practice, such moves delayed MFN trade liberalization and failed to provide the necessary momentum to liberalize the PNG economy (Box II.4). By contrast, unilateral MFN liberalization by PNG and other FICs would unquestionably create trade, thereby maximizing economic benefits. Gains from trade liberalization come mainly from cheaper access to imports and improved efficiency of resource-use at home, rather than from lowering overseas barriers to exports. Evidence suggests that economies and investment grew faster after broad liberalization both in the short and long term, but slower after participation in a regional trade agreement.²⁰

69. The Papua New Guinea Government generally supports the notion of a WTO-compatible regional free-trade area among the Pacific island countries, but opposes Australia and New Zealand membership. According to PNG authorities, initial membership should be open to the MSG countries with other FICs encouraged to join at a later stage. It is closely following developments within the South Pacific Forum.

70. Intra-FIC trade is relatively minor. In the case of PNG, less than 1% of its exports and imports are with other FICs.

¹⁹ Scollay (1998).

²⁰ Vamvakidis (1999).

Box II.4: Proposed preferential free-trade area (FTA) among Forum island countries

Trade ministers recently endorsed in principle the formation of a WTO-consistent free-trade area (FTA) among PNG and other FICs. This would initially cover goods, and exclude Australia and New Zealand, although the long-term integration with CER is to be examined. A draft framework is to be negotiated based on a negative list of exemptions so that it can operate for tariffs in 2001.

The costs and benefits of establishing a preferential FTA among FICs were examined in a study commissioned by the South Pacific Forum Secretariat. Another study also looked at the impact of a larger free-trade area between FICs involving Australia and New Zealand.

The economic benefits of a preferential FTA fundamentally depend upon whether it creates trade among members or simply diverts trade. While additional unassisted exports between partners will be beneficial, the case of increased imports is ambiguous. Trade diversion occurs when a preferential FTA leads to switching imports from third countries to partners, usually less efficient producers. Trade creation occurs when increased imports from member countries replace less efficient domestic production rather than displacing imports from third countries. While both will enhance regional trade among members, only when it is trade creating will there be genuine trade liberalization and welfare gains to members. Such gains will be illusory where trade diversion predominates, and may even reduce members' welfare.

Trade theory suggests that a preferential FTA among small countries with similar economic characteristics will have small or even negative net welfare effects. The empirical study by Scollay estimated small economic gains to most Forum island countries from an FTA among FICs, Cook Islands, Kiribati, Samoa and Tuvalu being made worse off. PNG was found to receive a tiny increase in GDP of 0.03%. It concluded that modest economic gains would accrue to all FICs only if the FTA was accompanied by an overall 25% MFN tariff cut. It thus confirmed the crucial importance to PNG and other FICs of non-preferential liberalization in assuring economic benefits from trade reforms.

The inclusion of Australia and New Zealand in the FTA among FICs would increase considerably the economic benefits to all FICs: greater liberalization, and hence trade creation, would be associated with increased imports from more efficient Australian and New Zealand sources. PNG's GDP would increase by almost 1.5%, equivalent to an expected annual gain of K 78 million. Although economic gains to PNG are increased substantially with the inclusion of Australia and New Zealand, they remain less than those available to PNG from substantial MFN liberalization.

It is often claimed that a FTA among FICs could provide a first step to wider trade liberalization, and encourage greater cohesion among members. However, the evidence is ambiguous. Foroutan urges caution in believing that regional trading pacts among developing countries lead to more liberal trading regimes. His analysis suggests that a FTA is neither a necessary nor sufficient condition for an open and liberal trading regime. Moreover, since a predominantly trade diverting FTA means that some members gain only at the expense of other partners, such arrangements may in fact undermine regional relations. Thus, any FTA would need to be strongly oriented towards further broader (multilateral) liberalization, supported by a set of well defined measures.

It must also be remembered that the above studies may overstate the economic benefits from a FTA among FICs. This is because experience with negotiating FTAs demonstrates clearly that if pursued for their own sake they are likely to end up being very discriminatory, by either excluding key products, or even reducing third-party access through adopting convoluted rules-of-origin requirements or due to the differential effects of other non-tariff barriers. These results are likely to increase the chances of FTAs being trade diverting, and welfare reducing on balance.

Care is needed to ensure that any FTA among PNG and other FICs is concluded in a way that promotes overall trade openness and does not frustrate MFN liberalization. If not, then it could be questionable whether the formation of such an FTA is worth the substantial administrative costs members would have to incur to service the agreement, or indeed would be making best use of the Forum Secretariat's financial and other resources.

Source: WTO Secretariat; ADB (1999b); Foroutan (1998), Scollay (1998); and Stoeckel and Davis (1998).

(e) Melanesian Spearhead Group (MSG) Trade Agreement

71. The MSG (comprising the three founding members, Solomon Islands, PNG, and Vanuatu, as well as New Caledonia and Fiji since September 1996), was formally launched in 1988 to promote political cooperation among members. In 1993, the MSG Trade Agreement was formed between the founding members. Fiji ratified its membership of the Trade Agreement in July 1998.²¹ It initially covered duty-free entry of only three commodities, one from each member: tea from PNG, beef from Vanuatu, and canned tuna from the Solomon Islands. Revenue imposts on eligible imports are not to exceed those applied to similar goods if produced domestically. Safeguard provisions allow any member to suspend obligations should imports increase so as to cause serious damage to existing industries producing like or directly competitive goods, or against dumped or subsidized goods. Moreover, parties may abrogate their obligations should they decide to develop new industries.²²

72. There are a number of other clauses in the MSG that allow parties to rescind obligations. Quantitative restrictions and tariffs may be imposed on eligible imports under balance-of-payments difficulties. Quantitative export restrictions are prohibited, unless necessary to prevent circumvention via the re-export of goods.

73. Members are committed in principle to extending the coverage of the agreement to ensure that duties and other trade restrictions are eliminated between the parties. In 1995 the coverage of eligible products was extended to 140 tariff items, and agreement, yet to be ratified, was reached in 1997 to expand the list to 150 items. Eligible products now include edible fruit and nuts, coffee, coconut-milk powder, jams, cement, and certain wooden furniture. Fiji has proposed the addition of 80 tariff items to the eligible list, but although accepted by officials, this has not yet been accepted by the MSG governments. Fiji has not been given the same preferences as other members, but has had to negotiate them on a bilateral basis.

74. The structure of MSG trade has changed during the 1990s. PNG has expanded its MSG exports of tinned meat and coffee. Since opening its cement factory in 1994, PNG has increased exports substantially to the Solomon Islands and Vanuatu. PNG continues to import substantial canned tuna from the Solomon Islands. However, MSG imports by PNG of canned mackerel from Fiji ceased in 1995 when PNG introduced import restrictions, later replaced by high tariffs, to support a new mackerel canning plant in Lae. PNG now exports canned mackerel to the Solomon Islands.

75. Eligible products under the MSG Trade Agreement account for a substantial part of intra-MSG trade. Some 78% of PNG trade with the Solomon Islands is covered, and for trade with Vanuatu the coverage rises to some 94%.²³ However, intra-MSG trade, estimated in total at almost US\$16 million in 1997, up from almost US\$12 million in 1994, has remained a very low share of their total trade, accounting for less than 0.5% of members' total trade.²⁴ Moreover, intra-MSG trade is less important to PNG than for other members. Since 1994, the importance of PNG as a destination for MSG exports has declined, while it remains an increasingly important source of MSG exports. In 1997, MSG exports by PNG amounted to US\$5.2 million, up from US\$2.7 million in 1994. However, MSG imports by PNG declined over this period from US\$4.5 million to US\$3.9 million.

²¹ Membership of the MSG does not automatically extend to the MSG Trade Agreement, which was initially formed only between founding members. Although any member of the MSG or South Pacific Forum is eligible to join the Trade Agreement, membership must be negotiated.

²² This obviously creates a high degree of uncertainty among members, and may discourage trading opportunities.

²³ Economic Insights (1999a).

²⁴ The expansion of trade amongst the original MSG countries is almost all attributable to growth in a few commodities, namely fresh, frozen and canned beef; coffee; canned fish; cement; and pasta and noodles.

76. The MSG Trade Agreement has therefore had a negligible impact on expanding trade within the South Pacific region. Moreover, its impact, if any, is likely to have diverted regional trade rather than creating it, and thereby provided only illusory trade liberalization and economic benefits to its members. Indeed, it has been estimated that the MSG Trade Agreement is most likely to have reduced the region's economic welfare, with at best only minimal gains to the PNG economy (Box II.5). The MSG Trade Agreement was described, soon after its formation, as essentially a political agreement, with few economic benefits.²⁵

Box II.5: The MSG Trade Agreement

It has been estimated that the MSG Trade Agreement has been primarily trade diverting. Trade diversion has occurred in all main products traded under the MSG, namely fresh, chilled, and frozen beef; pasta and noodles; and cement. The only product experiencing trade creation was found to be coffee, while for canned meat and fish there was a mix of trade diversion and trade creation. This is because governments have negotiated the agreement to avoid providing tariff reductions on goods produced locally that may be threatened by concessional imports.

On this basis, it was concluded that the Agreement has had a small impact on MSG economies, most likely reducing their combined GDP by 0.03%. The upper range was an increase in GDP of 0.02%.

It is likely that Vanuatu and possibly Papua New Guinea would have gained most from the agreement at the expense of the Solomon Islands. The Solomon Islands is estimated to have borne a high share of the costs imposed by trade diversion. Papua New Guinea and Vanuatu on the other hand are estimated to have gained from an expansion in exports. These benefits are estimated to have outweighed the cost to these economies of trade diversion on other commodities.

Source: Economic Insights (1999a), *Review of the MSG Trade Agreement*, Report for South Pacific Forum Secretariat, Suva, May.

77. The MSG Trade Agreement has not been notified to the WTO under either GATT Article XXIV or the Enabling Clause.

(f) First Agreement on Trade Negotiations Among Developing Member Countries of the Economic and Social Commission for Asia and the Pacific (the Bangkok Agreement)

78. PNG acceded to the Bangkok Agreement in 1994, but has not implemented the agreement due to ratification delays in Parliament. It has operated since 1976 between Bangladesh, India, Laos, the Republic of Korea and Sri Lanka.²⁶ This provides limited reciprocal tariff concessions between members on certain goods.

(g) Other agreements

79. PNG has observer status in the Association of South-East Asian Nations (ASEAN) and is considering whether to seek full membership.

80. It is a signatory to several plurilateral fishing agreements with neighbouring Pacific States on dividing access to highly migratory fish species within its water and the international waters of the Western Pacific. The Palau Agreement of 1997 requires PNG and other signatories to reduce by 10% annually the number of licensed foreign fishing vessels operating in their waters. It is also a party to

²⁵ Grynberg and Kabutaulaka (1995).

²⁶ Afghanistan has also acceded in principle to the agreement.

the Federated States of Micronesia Agreement whereby signatories provide each other's domestically registered vessels free access to their waters; and to the 1988 regional fishing agreement between the United States and the 16 members of the Forum Fisheries Agency (the U.S. Multilateral Fisheries Treaty).

(iii) Bilateral agreements

(a) Australia PNG Trade and Commercial Relations Agreement (PATCRA)

81. PNG has a bilateral agreement with Australia that establishes a non-reciprocal free-trade area providing duty-free access for all exports to Australia. It was formed on independence and notified to the GATT under Article XXIV in November 1997.²⁷ A revised version, signed in 1991, included provisions on investment promotion, assistance to PNG's small business sector and primary industries, and promotion of PNG exports by Australian overseas trade representatives.

82. Excepted goods for Australia include certain sugar imports, beverages, tobacco, and mineral fuels (Schedules A and B). For PNG all products are excepted (Schedules C and D).

(b) PNG/Fiji Trade Agreement

83. This reciprocal trade agreement was formed in August 1996. Certain goods can enter PNG's market at concessional tariff rates, subject to quarantine approval on most eligible agricultural products. Prior to 1 July 1999, the concessional tariff rate was set at 10% to match the 10% VAT imposed by Fiji on PNG eligible exports. Currently, eligible imports enter PNG at zero tariff, but are levied the 10% VAT.

84. The agreement currently covers 45 agricultural and manufacturing products, including chilled or frozen mackerel as well as certain dairy products, including cheese; fruit such as pineapples; tea and other beverages; spices, such as chilli; cement; wood and wood articles; and clothing. Negotiations are continuing aimed at expanding the product coverage of the agreement. The agreement also allows for cooperation in other measures, such as services, quarantine, rules of origin, and other trade facilitation measures.

85. This Agreement has not been notified to the WTO under either Article XXIV or the Enabling Clause.

(iv) Generalized System of Preferences (GSP)

86. PNG is a beneficiary of GSP schemes run by 27 industrialized economies. According to authorities, these have been particularly important in the case of the United States (fisheries and agricultural products); Germany and the United Kingdom (coffee and cocoa); and Japan (timber).

(v) Other agreements and arrangements

87. PNG is a member of several multilateral organizations that have a bearing on its economic policies and development. These include the International Monetary Fund, the World Bank, the Asian Development Bank, and UNCTAD.

88. PNG belongs to several international commodity agreements that, according to authorities, are important to its export interests. These include the International Coffee Agreement, International

²⁷ GATT document L/4571, November 1977.

Cocoa Agreement, Association of Natural Rubber Producing Countries, Asia Pacific Coconut Producing Countries, International Tropical Timber Agreement, and International Spice Organisation.

89. Trade and investment links with the United States have been strengthened by the signing of a Memorandum of Co-operation under the U.S. Market Access and Regional Competitiveness (MRAC) Program. PNG also has quota access rights to the U.S. sugar market. In 1998-99, the U.S. allocation to PNG for the export of raw and refined sugar was 7,528 tonnes.

(7) TRADE DISPUTES

90. PNG has not been a party to any formal dispute within the WTO, either directly or as an interested third party.

91. There are no formal dispute settlement procedures in regional arrangements involving PNG. Disputes are handled bilaterally. The Fiji/PNG Trade Agreement and the MSG Trade Agreement contain provisions for consultations on disputes.

(8) FOREIGN INVESTMENT POLICIES AND PROCEDURES

92. The PNG Government welcomes foreign direct investment (FDI) and believes that it can make an important contribution to the country's economic development. However, outside the mining sector, where investment is lumpy and variable, PNG has attracted relatively little FDI. The Government's reform programme recognizes the importance of private-sector-led growth, and targets foreign investment policies and their enhanced transparency as priorities for reform.

93. FDI in PNG has always fluctuated in line with investments in the mining and petroleum sector. Mining investment accounted for more than three quarters of FDI over the period 1994-98. After peaking at US\$475 million in 1995, due to record mining investment of US\$428 million, FDI declined sharply to US\$23 million in 1997, with negative mining investment, rising modestly to a projected level of US\$130 million in 1998, due mainly to an expected increase in mining investment to US\$104 million (Table II.2). The slump in FDI largely reflects a loss of confidence by overseas investors in government stabilization and other economic policies, as well as the poor and uncertain state of the economy generally and the depressed international conditions for the mineral and petroleum sectors. The current poor macroeconomic outlook (Chapter I) combined with previous opaque and unpredictable investment policies have also discouraged capital inflows.

Table II.2
Foreign investment, 1993-98
(US\$ million)

	1993	1994	1995	1996	1997	1998 ^a
Foreign direct investment (net)	81	74	475	226	23	130
Mineral	..	10	428	184	-7	104
Non-mineral	..	64	47	42	30	26

.. Not available.

a Estimate.

Source: International Monetary Fund (1999), *Papua New Guinea – Staff Report for the 1999 Article IV Consultation*, Washington, D.C.

94. Data on investment approvals by the Investment Promotion Authority are shown in Table II.3. While this is likely to differ from actual data, it provides useful indications of changes in the overall

investment climate. Approvals data show a large reduction in 1998, from K 1.8 billion to K 0.5 billion, primarily due to a sharp decline in investment approvals for logging projects, from K 0.4 billion to K 40 million, as well as substantial falls in manufacturing and construction investment. Mining investment approvals also declined sharply in 1996, from K 1.3 billion to K 0.4 billion, and remained at about that level in 1998 despite a small improvement in 1997. Most FDI in recent years has come from Australia, Malaysia and North America, although China accounted for almost half of approvals in 1998, while that from Malaysia declined substantially.

Table II.3
Foreign investment approvals, 1995-98
(K million and per cent)

Sector/Country	1995	1996	1997	1998
Sector				
Agriculture	464	152	7	1
Forestry	398	148	407	40
Mining	1,345	399	501	359
Manufacturing	17	67	232	7
Construction	43	131	282	16
Transport & communication	85	853	72	33
Other	104	169	302	82
Total	2,456	1,919	1,803	538
Country (%)^a				
Australia	21	21	21	17
Malaysia	18	18	18	9
North America	18	18	18	17
China	3	3	3	46
Japan	0.3	0.3	0.3	5
Other Asian crisis economies	3	3	3	2
Other	37	37	37	4

a Figures for 1995-97 are three-year averages.

Source: Asian Development Bank (1999a), *An update on the Impact of the Asian Financial Crisis on PMDC Economies*, Office of Pacific Operations, April; and the PNG Investment Promotion Authority.

95. Many aspects of current legislation appear highly restrictive: foreign investment is prohibited in substantial segments of the economy even though little activity exists in many of these sectors. In addition, the procedures for FDI approval have lacked clarity and transparency, and have been subject to political influence. Uncertainty about the future shape of investment conditions, including the structure of incentives, is likely to compound the unattractiveness for foreign investment.

96. The Constitution prohibits foreign investors or non-citizens from owning freehold land. They must lease land from the Government for specified purposes. This is a major restriction on foreign investment, especially in agriculture and mining developments: some 97% of land in PNG is customary-owned land; despite legislative attempts, little customary land has been registered or "adjudicated". A recent survey of foreign investors showed they had only a "reasonable appreciation" of PNG's investment policies.²⁸ This same survey found the main impediments to new foreign investors in FICs to be, in descending ranking, bureaucratic delays and inefficiencies; application of government policies; and land tenure issues.

²⁸ South Pacific Forum Secretariat (1998).

97. A survey conducted by the PNG Investment Promotion Authority in late 1994 found the top five impediments to investment to be the high cost of doing business; law and order problems; poor infrastructure; inconsistencies in government policies; and the difficulty of negotiating stable contractual agreements with landowners.²⁹

98. While the Government favours joint ventures, and promotes local partners, there are no legislated foreign ownership limits; these are determined commercially by the partners. No performance requirements are imposed, although the Government usually prefers the use of local materials. According to authorities, PNG's investment regime fully complies with the WTO Agreement on Trade-Related Investment Measures (TRIMS).

99. The Government's current investment policies target the manufacturing sector, including the downstream processing of natural resources as well as the production of industrial goods, such as clothing, textiles, leather goods, food, timber products, footwear, chemicals, plastic products, paper products and motor vehicle parts. Village eco-tourism and large-scale resort developments are also priority areas for investment. The Government does not, however, discriminate between proposals, provided they contribute to economic growth; create new jobs; utilize domestic, especially renewable, resources; assist in skills acquisition; expand exports; develop remote areas; facilitate increased ownership of investment by locals; and promote import replacement.

100. Special procedures apply to mining and petroleum investment as well as to forestry and fishing, where respective ministers exercise discretionary approval in accordance with set procedures. Several stages are required in the Development Forum process for mining, for example: the application for exploration licence; the exploration phase; negotiation of terms for project approval and the Government's participation; application to the Government for project approval, including granting of a special mining lease; and project approval and construction (Chapter IV). The Ministers for Lands and Physical Planning and for Environment and Conservation also have some discretionary powers over foreign investment.

(i) Legislative framework for FDI

101. Foreign investment policies are governed by the Investment Promotion Act 1992 (Table II.4). This created the Investment Promotion Authority, within the Ministry of Commerce and Industry, to facilitate foreign investment outside the mining and petroleum sectors. All foreign enterprises wishing to carry on business in PNG must be certified by the Authority, which screens FDI proposals. Business enterprises are either citizen (wholly owned by a citizen); national (more than half-owned by a citizen); or foreign (half or more owned or controlled by non-citizens). Before commencing business, foreign companies must, like domestic firms, register under the Companies Act. The Authority is also responsible for monitoring foreign investment.³⁰ It must also approve changes in a firm's operations, including its location, and variations in ownership above certain threshold levels.

102. Although processing of applications by the Authority takes on average less than the legislative requirement of 35 days for issuing a certificate, evidence suggests that such arrangements

²⁹ Duncan and Lawson (1997).

³⁰ The commercial banks are authorized to approve foreign investments below annual limits of US\$270,000. They can also usually approve foreign currency borrowings by resident businesses or individuals (outside mining or petroleum) up to the level where aggregate foreign currency borrowings exceed the equivalent of US\$2.7 million at a debt to equity ratio of no more than 5:1. The Central Bank normally requires foreign investors to maintain a satisfactory gearing ratio of total loans to shareholder funds for the locally incorporated company receiving the investment. It handles all exchange controls in mining, petroleum, and forestry.

can be slow and cumbersome, especially for more sensitive developments; such delays add considerably to investment and business costs. The National Land Board screens applications for land allocations and makes recommendations for approval to the Minister of Lands.

Table II.4
Summary features of foreign investment policies and proposed changes

Investment principle	Reported progress in implementation as at April 1998	Plans for meeting 1998 target date
Transparency	No response sought	No response sought
Non-discrimination between source countries	Reviewing the reserved activities list, with the last exclusions being the manufacturing industries	A further review to go to Cabinet end-April 1998 to classify reserved activities into job creation and protection
National treatment	Addressed partly under the review of the reserved activities list, but also addressed in the draft national investment policy relating specifically to review of the certification process	Technical assistance sought from World Bank to assist review of act
Investment incentives	In review of investment incentives, relaxation of health, safety and environmental regulations do not feature. These requirements will continue to exist.	Regulatory status is on-going
Performance requirements	To be implemented under the Government's overall national investment policy framework, in which one of the main policy statements is aimed at eliminating all regulatory and procedural obstacles to trade and investment	Draft national investment policy being drafted and expected to go to Cabinet by June 1998
Expropriation and compensation	A signatory to the International Convention for Dispute Settlement. Domestic legislative framework also allows for fair and impartial settlement of commercial disputes	No plans to change in 1998
Repatriation and convertibility	Repatriation and convertibility is allowed for and facilitated under the requirement of the Banking Act administered by the Central Bank	An on-going activity. The Government announced a public review of the financial sector in 1998. This aspect of banking may be considered.
Settlement of disputes	No response sought	No response sought
Entry and sojourn of personnel	Current immigration procedures being applied. Discussions commenced in APEC on Business Visa	On-going activity
Avoidance of double taxation	Double tax agreements have been signed with United Kingdom, Australia, Canada, Malaysia, China, Germany and Korea, Dem. Rep. Negotiations with Fiji are complete	Agreements being considered with United States, Japan, New Zealand and the Philippines. Work on a PNG Double Taxation Model under way.
Interest behaviour	All investor inquiries and approvals are processed with the underpinning assumption that other applicable laws of the country are complied with	On-going
Removal of barriers to capital exports	Under the Government's Structural Adjustment Programme and the overall public sector reforms, the regulatory and institutional barriers to the free flow of capital are being addressed	On-going

Source: Foreign Investment Advisory Service (1998), *FIC National Investment Policies: Consistency with APEC Non-Binding Investment Principles and the Status of Reform*, Session 2 Background Paper, Forum Economic Ministers Meeting, Fiji, 7-8 July.

103. Appeals against rejection of applications or terms and conditions imposed by the Authority can be made to the Minister of Commerce and Industry. These must be settled within 35 days. The Minister's decision is final.

104. The Foreign Investment Advisory Service (FIAS), on behalf of the South Pacific Forum Secretariat, reviews the transparency features of investment policies of FICs.³¹ The latest assessment was based on PNG's 1997 investment legislation.³² PNG received an average score of 2.4, with individual scores across the categories examined ranging from one to four (out of a maximum of 5). PNG received a rating of two or below in eight categories (Table II.5). Criteria used by the FIAS to assess the transparency of a country's investment legislation are public availability, consistency in application, and the extent to which the policy statement is complete, understandable, and unambiguous.³³

Table II.5
Transparency ratings of investment policies and practices

Investment policy category	Comment	Score (1-5)
Approval criteria	Approval criteria and criteria levels not specified	1
Approval procedures	No detailing of process or time frame	2
Approval cancellation	Not mentioned	1
Sectoral restrictions	Not fully specified	1
Local equity requirements	No requirements	5
Repatriation restrictions	Some clarification needed as process appears to be discretionary	3
Incentives award criteria	Incentives and broad objectives are given, but details of awards and criteria are not evident	1
Incentives award process	Broadly outlined only. No time frame given	1
Investment protection	Availability indicated but no details provided	1
Import duty exemption criteria	Not clear whether all or only some exporters are eligible	2
Import duty exemption process	The process is outlined but more detail is needed, for example, what constitutes 'evidence'	3
Export requirements	Not included in statement	
Work permit approval criteria	Data requirements given but no decision criteria or criteria levels	3
Training requirements	Training requirements are presented but the acceptability criteria for a programme are not	3
Exchange controls	Requirements are not fully specified	3
Local borrowing restrictions	Some clarification needed	4
Investment guarantees	Extensively documented	5
Average		2.4

Source: Foreign Investment Advisory Service (1997), *Pacific Island Country Foreign Investment Policies: A Further Assessment of Transparency*, Sydney.

105. FIAS conducted a further assessment of FIC investment policies for the 1998 FEMM by examining the consistency of FIC their investment policies with the APEC non-binding investment principles. This assessment is particularly relevant to PNG, given its membership of both fora. Of the twelve principles, PNG was found to comply with three, possibly four; and to approach compliance in one, possibly two, other principles. No assessment was possible for the remaining principles due to insufficient information (Table II.6).

³¹ FIAS is a joint service of the World Bank and the International Finance Corporation.

³² Foreign Investment Advisory Service (1997).

³³ These aspects are assessed on the basis of transparency ratings for 17 investment categories, such as approval criteria, sectoral restrictions, and provision of incentives. A score of two out of five indicates that very little of the policy category is clear or that most elements are missing. A score of one, two or three would suggest major improvements in transparency are possible.

Table II.6
Compliance of investment policies with APEC non-binding principles

APEC non-binding investment principle	Assessment
Transparency	Response not sought
Non-discrimination between source countries	Assessment could not be given based on the information in the response provided
National treatment	Compliance, but with some uncertainty surrounding assessment
Investment incentives	Compliance
Performance requirements	Approaching compliance, but with some uncertainty surrounding assessment
Expropriation and compensation	Assessment could not be given based on the information in the response provided
Repatriation and convertibility	Compliance
Settlement of disputes	Response not sought
Entry and sojourn of personnel	Assessment could not be given based on the information in the response provided
Avoidance of double taxation	Approaching compliance
Interest behaviour	Assessment could not be given based on the information in the response provided
Removal of barriers to capital exports	Approaching compliance, but with some uncertainty surrounding assessment

Source: Foreign Investment Advisory Service (1998), *FIC National Investment Policies: Consistency with APEC Non-Binding Investment Principles and the Status of Reform*, Session 2 Background Paper, Forum Economic Ministers Meeting, Fiji, 7-8 July.

106. These studies suggest that the transparency of PNG's investment policies could be improved, especially in the area of approval procedures and criteria, the criteria and use of investment incentives, and in investment protection. PNG joined the World Bank's Multilateral Investment Guarantee Agency in 1990, ensuring that the investor would be compensated should nationalization occur. Similarly, the Investment Promotion Act contains protection against expropriation, cancellation of contracts, and discrimination. It also allows for remittance of earnings overseas and capital repatriation to meet payments of principal, interest, dividends, royalties, and service charges; similar liabilities on foreign loans; and costs of other foreign obligations approved by the Government (Section 37). The legislation also applies the Investment Disputes Convention Act to any disputes involving foreign investors.

107. Investment promotion and protection agreements have also been ratified with Australia, Malaysia, and China. These bilateral treaties are administered by the Department of Foreign Affairs and Trade, and accord reciprocal assurances or guarantees against nationalization or expropriation of investment in respective territories. PNG also has double taxation agreements with several countries, and is considering such agreements with Chinese Taipei, Indonesia, New Zealand, the Philippines, Thailand and the United States.³⁴

108. Residency or employment visas will only be issued by the Department of Foreign Affairs after the Authority issues a certificate. Foreign investors are expected to employ nationals in areas where the required expertise exists, and must apply for a work permit from the Department of Industrial Relations for each non-citizen employee. Specific occupations, covering 578 vocation codes out of a total of 1,048, are reserved for nationals.³⁵ Foreign investors must include a training and localization programme in accordance with the Employment of Non-Citizens Act. Work permits are usually for three years and cover a particular position. The employee working in the position can be replaced without approval. Work permits are only issued after the employee has arrived in PNG.

³⁴ PNG has double tax agreements with, Australia, Canada, China, Fiji, Germany, the Republic of Korea, Malaysia, Singapore and the United Kingdom.

³⁵ Foreign workers may be used in these prohibited occupations where it can be shown that nationals with suitable skills are not available.

(ii) The national investment policy

109. Many of the shortcomings in the current investment regime are recognized in the Government's National Investment Policy released in June 1998. The legislative provisions are being reviewed and amendments proposed to the Act. Legislation is to be amended to refocus the Authority's role to promote, rather than control, FDI. The new national investment policy is designed to provide transparency, equal treatment, and consistency to investors, and specifically proposes:

- strengthening the Authority's investment support functions by establishing a one-stop shop to process investors more efficiently;
- modifying the Investment Promotion Act to shift from a case-by-case approval process for foreign investments to a simpler system of registration of businesses, with ex post monitoring of investments;
- repealing the Pioneer Industries Act, subsequently achieved, to eliminate case-by-case ministerial discretion in approving investment incentives; and
- reviewing investment procedures under specific sectoral legislation and making the procedures and requirements consistent with a more liberal approach to foreign investment.

110. The aim is to develop the Authority as a "one-stop shop" to facilitate investment. At the same time, however, the investment policy specifies that the legislation will be reviewed to remove investment barriers while also allowing for discrimination in provisions for increased support to the domestic sector. The Government is reviewing the negative list of activities reserved for domestic investors with a view to reducing its coverage (Chapter III). Manufacturing and construction activities were removed from the list in August 1995. The Government has approved a phase-out schedule for other reserved activities, and is again reviewing the list's coverage. Entry restrictions are also to be removed on post and telecommunications, commercial shipping, abattoirs, and agricultural marketing and processing activities.

111. Investment incentives are to be rationalized under the tax and customs laws (Chapter III). It was announced in the 1999 Budget that a uniform and consistent set of investment incentives would be administered by the Authority. According to the investment policy, the new arrangements are designed to remove case-by-case ministerial discretion in the use of investment incentives in order to avoid intense lobbying and misuse.