THE BOUGAINVILLE AGREEMENT: IS A DEAL A DEAL?

ABDUL PALIWALA*

The Papua New Guinea government has taken the first steps towards re-negotiation of the Bougainville Copper Agreement. The Chief Minister stated the following political and economic reasons for re-negotiation in his statement to the House of Assembly on 4 March 1974:

> Whenever a country has a project that is so big and so profitable, the country's leaders must look closely to be sure that the project provides enough benefits for the people. We must be sure that the taxes and other payments that the project produces are high enough to give us the funds we need for our development. And we must be sure that the government has enough control over the project so that it will contribute to the kind of development that we want.[1]

An even more radical call has been made by a group of leading Papua New Guinean politicians, public servants, ministerial advisers and community leaders, including John Kaputin, the Minister for Justice, and Father John Momis, deputy chairman of the Constitutional Planning Committee. The group suggested:

> The time for re-negotiation of the agreement along conservative lines... is well past. Clearly the whole basis of the agreement is unjust and exploitative and the agreement itself must therefore be scrapped.[2]

---

* Senior Lecturer in Law, University of Papua New Guinea. I am grateful to Bruce Ottley, Peter Bayne and Stephen Zorn for their help in the preparation of this article.

1 *House of Assembly Debates*, 4 March 1974.

2 Press release, 4 February 1974.

The early response of Bougainville Copper officials was to oppose any re-negotiation of the agreement on the grounds that "a deal is a deal".[3] However, the firmness shown by the government led to a modification of this position. The company now accepts that the government should have a greater share of the revenue from the mine but argues that this should be achieved only by the means of the purchase of a greater share of the equity by the government.[4]

I have been prompted by these events to attempt to clear some of the mystification surrounding the nature of the agreement, and to examine the legal avenues open to the government of Papua New Guinea.

1 *The Act and the Agreement*

The Bougainville Copper Agreement[5] was made on 6th June 1967 between the former Administration of Papua New Guinea and the Bougainville Copper Pty. Ltd. (B.C.P.), which is a company incorporated in Papua New Guinea and under the control of the Conzinc Riotinto of Australia group of companies.

The Administration had previously granted Prospecting Authorities 1-7 to C.R.A. Exploration Pty. Ltd., a company which is a wholly owned subsidiary of Conzinc Riotinto of Australia Ltd. (C.R.A.), which in turn is owned as to 80.7% of share capital by the Rio Tinto Zinc Corporation Ltd. (R.T.Z.) of the United Kingdom.[6]

The purpose of the agreement was to give B.C.P., its successors or assigns authority to mine and export the vast low-grade copper deposit on Bougainville Island. B.C.P. was expected to invest between $34 million and $106 million. Under the terms of the agreement, the Administration was entitled to take up to 20% of the share capital in B.C.P.,[7] and the Administration in fact took up the full 20%. A very large proportion

---

3 *Papua New Guinea Post-Courier* (6 Feb 1974).

4 *Papua New Guinea Post-Courier* (13 May 1974).

5 The agreement is contained in the schedule to the *Mining (Bougainville Copper Agreement) Act* 1967, No.70 of 1967.

6 See the Charts below, which were abstracted from *Facts About C.R.A.*, published by C.R.A.(1973).

7 See *preamble* to the agreement.

CHART I

ORIGINAL STRUCTURE OF COMPANIES INVOLVED IN BOUGAINVILLE MINING

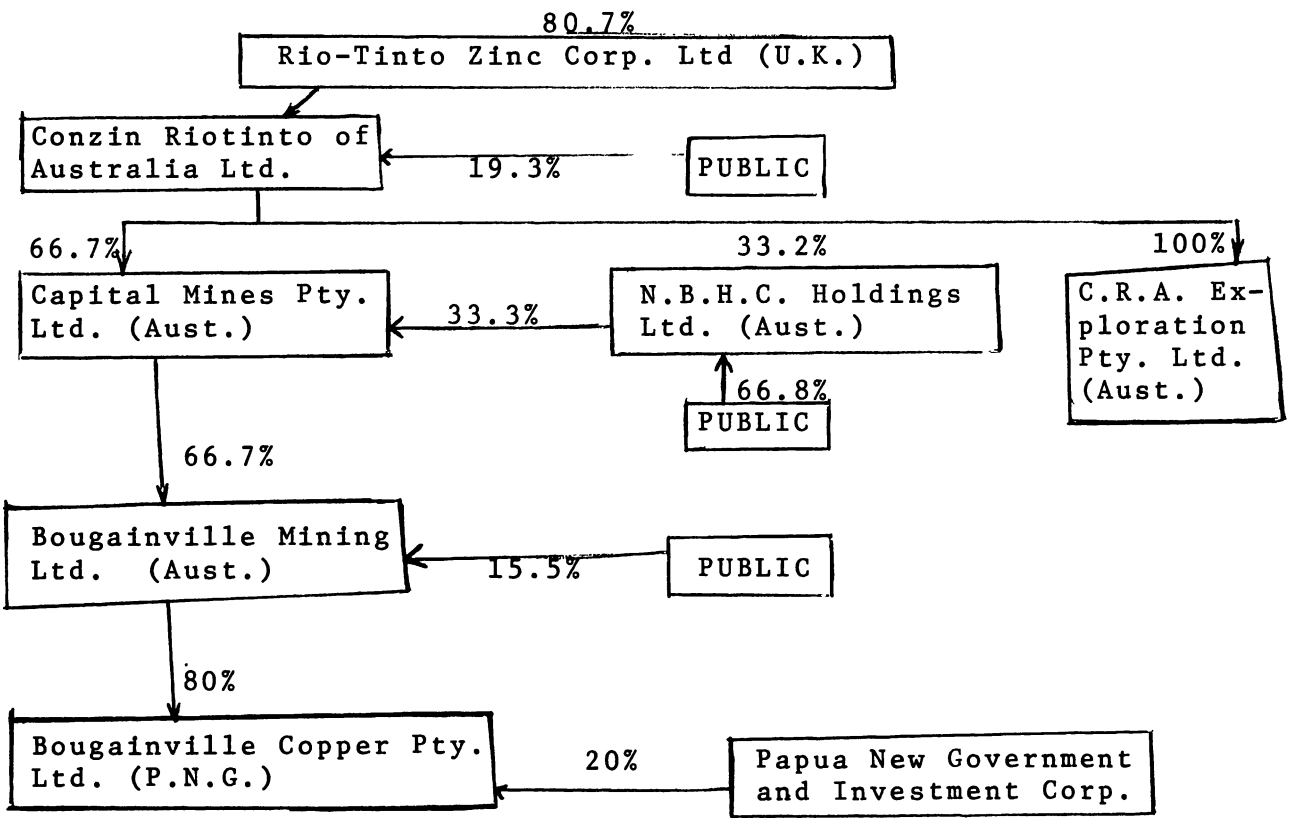
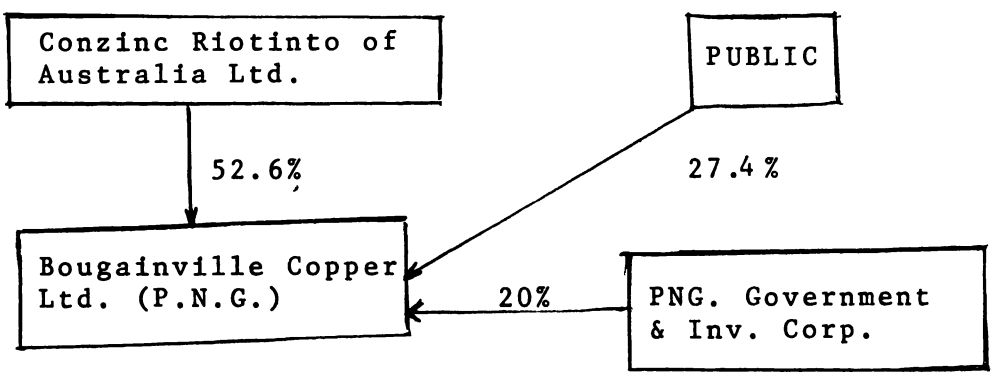


CHART II

Re-organised structure as announced 8 June 1973



of the financing of the operation was done by means of money raised on the international loan market.[8] At the same time the P.N.G. Administration had the burden of providing substantial infrastructure and services, which it has in fact provided, at an estimated cost of $42 million,[9] in addition to the $26 million required for the purchase of the 20% equity.

The agreement gives the company wide powers, including some semi-governmental powers in running the mining operation.[10] In addition, the company has a substantial tax holiday period.[11]

Clause 2 of the agreement provided that as soon as reasonably practicable, the Administration should enact through the House of Assembly an act to approve the agreement in the form agreed upon by the parties. This act was duly enacted as the *Mining (Bougainville Copper Agreement) Act* 1967.[12]

---

8 The breakdown of outstanding loans as of August 1973 was as follows:

Bank of America consortium	US$ 177 million
Japanese cash loan	30 million
U.S. export-import Bank	61 million
Japanese export-import Bank	23 million
Other	52 million
TOTAL	US$ 343 million

9 *Papua New Guinea Budget Papers* 1973-74.

10 See clause 8(c) (d) and clause 14(b) (c), for example.

11 See clause 7. B.C.P. has a full tax holiday for its first three years of commercial production. Subsequently it is to be taxed at 50% of taxable revenue, but this rate is reached only by a four-year progression from the general rate of company tax (presently 25%) to the 50% rate. In addition, B.C.P. is allowed to take accelerated depreciation under Division 10 of the *Income Tax Act* in the years immediately following the end of the tax holiday period. This has the effect of postponing any liability for an additional three or more years, depending on the amount of profits. Also, 20% of all income earned from mining is exempt from any tax for the life of the project.

12 No. 70 of 1967.

II. *The Nature of the Agreement*

The agreement may best be described as a concession agreement. The main feature of such agreements is the involvement of the government on the one part and the foreign controlled firm on the other. In the case of the Bougainville agreement, we also have an example of a joint international business venture, in that the government has a significant minority shareholding. The legal nature of concession agreements may become important in connection with the classification of rights and duties involved. Thus, in the ARAMCO arbitration, an important legal question was whether a concession agreement should be classified as contractual or as an act of state.[13] The answer was important in determining the choice of law rule concerned. There is considerable conflict as to the proper classification of concession agreements. However, the correct approach is to treat them as agreements of a special nature, and different from ordinary contracts. Thus, international practice establishes that these agreements are not invariable but are subject to frequent changes. As Steiner and Vagts say:

> The unmistakable pattern of change through re-negotiation of concession agreements over the past decades has been to shift a larger percentage of revenues to the government.... When such problems emerge, lawyers are faced with a situation to which that of lawyers in a dispute over a contract between private parties affords only remote analogies. More than in private bargains, purely legal considerations tend to recede into the background.[14]

A special legal nature has been given to the Bougainville agreement by virtue of sections 4 and 6(1) of the act:

> S. 4 'The Agreement is approved and shall take effect according to its tenor.
>
> S. 6(1) Except as provided in subsection (2) of this section, the Agreement has the force of law as if contained in this Act and applies not

---

13 *Arbitration between Saudi Arabia and the Arabian American Oil Company (ARAMCO)*, Arbitral Award of 23 August 1958, (1963) 27 *IntLR* 117.

14 Steiner and Vagts, *Transnational Legal Problems* (1968) 373.

> withstanding anything to the contrary in any other law in force in Papua New Guinea or a part of Papua New Guinea.

Professor Enid Campbell argues that mere approval of an agreement by the legislature is not sufficient to give it the force of law.[15] However, in the case of the Bougainville agreement, section 6 removes any doubt by expressly providing to that effect. Professor Campbell further argues that once an agreement has the force of law, it ceases to be governed by the law of contract, and the rights and duties created under the agreement become statutory rights and statutory duties. This may have important consequences. For example, the law of contract as to privity and variation ceases to apply and these matters become entirely governed by the regime created in the Act and agreement. Thus the agreement becomes merged into the act and subject to such changes as the legislature has the constitutional power to make. It is for this reason that by clause 2(c) of the agreement an attempt is made to protect the rights under the agreement of B.C.P. and its shareholders where a subsequent act expressly or impliedly amends or repeals the principal act or the agreement. What effect the clause has in practice will be discussed later.[16]

Another important feature of the act is its attempt to entrench the act and the agreement by section 6(3):

> No law at any time in force in Papua New Guinea or a part of Papua New Guinea made after the date of commencement of this Act shall affect this Act or the Agreement -
>
> (a) unless the contrary intention appears, either expressly or by implication, in that law;
>
> (b) except as provided by the Agreement; or
>
> (c) unless before that law comes into force the Company consents thereto.

It is probably correct to interpret the three paragraphs as disjunctive; that is, the act or the agreement may be amended or repealed by another law where the provisions of any of the

---

15 Campbell, "Legislative Approval of Government Contracts" (1972) 46 *ALJ* 217 at 217-8.

16 See text at footnote 29.

three paragraphs are complied with. If the legislature had intended otherwise, it would have inserted the word "and" between the subparagraphs.

Even if another interpretation were possible, the provisions of section 6(3) are not constitutionally sufficient to provide adequate entrenchment. Campbell has suggested that it may be possible in the case of a non-sovereign legislature such as that of an Australian state or the present Papua New Guinea House of Assembly to provide an entrenchment clause by a provision similar to paragraph 6(3)(c). However, there would need to be another provision in the act prescribing the manner and form for enacting statutes that amend or repeal the entrenchment provision. Otherwise the entrenching provision itself could be amended and repealed in the normal manner by a provision in any other act.[17]

This argument may be correct for an Australian state, but is not at present applicable to Papua New Guinea as the House of Assembly cannot deviate from the specific method of legislation provided for in the *Papua New Guinea Act* 1949-1973. Whether entrenchment is possible after independence will depend on the provisions of the Constitution.

Therefore, it appears that paragraphs 6(3)(b) and 6(3)(c) become relevant only when a later law of Papua New Guinea *would not*, according to the rule in paragraph 6(3)(a), affect the act of 1967. According to Campbell, paragraph 6(3)(b) assumes that a later law might affect the act because the agreement contains terms rebutting the maxim *generalia specialibus non derogant*. She also contends that paragraph 6(3)(c) in effect delegates to the company the power to give a later law a wider sphere of application than it would otherwise have, and that it definitely does not impose any restraint on the legislative authority of the House of Assembly. Paragraphs 6(3)(b) and 6(3)(c) may best be interpreted as providing rules of normal practice rather than attempts at entrenchment.[18]

---

17 The two Australian authorities on this issue are *A.G. for N.S.W. v. Trethowan* (1931) 44 *CLR* 394; and *Clayton v. Heffron* (1960) 105 *CLR* 214.

18 Campbell, *op. cit.*

Therefore, the Papua New Guinea House of Assembly's legislative powers at the moment are not in fact fettered by any privisions in the act. That is, the legislature has the legislative power to amend or repeal the act and to vary or rescind the agreement irrespective of any provisions in the act or agreement. This does not necessarily mean, however, that B.C.P. would have no remedy under the municipal law of a third country or under international law.

III. *Is the Papua New Guinea Government Bound by the Agreement under International Law?*

The original parties to the agreement were the Australian Administration of Papua New Guinea and B.C.P. The question therefore arises as to whether the government of a *self-governing* Papua New Guinea and subsequently the *sovereign government* of an *independent* Papua New Guinea succeds to the agreement under international law. Undoubtedly a strong moral argument can be made out by the government of this country to the effect that it should not have to bear the yoke of onerous obligations agreed upon by a colonial government. Moreover, in the realm of international law, legal, moral and political issues are often closely interwoven. Steiner and Vagts go even further, suggesting that in the case of concession agreements "legal considerations recede into the background."[19]

The legal arguments on the question of succession to concession agreements are closely related to the arguments over succession to treaties. Political and economic considerations may also have influenced the discussion of issues in this area. In the days when the British empire was expanding by conquest, courts in England adhered to the view that

> The conquering sovereign can make any conditions he thinks fit concerning the financial obligations of the conquered country, and it is entirely at his option to what extent he will adopt them.[20]

This negativist view was opposed by the "universal successions" theorists who suggest that the succeeding state acquires all the rights and obligations of the state to which

---

19 Steiner and Vagts, *op. cit.*, at 373.

20 *West Rand Gold Mining Co. v. The King* (1905) 2 KB 391. The Transvaal Concessions Commission had in fact recommended an *ex gratia* acceptance of most concessions of the type involved in the above case. The British practice on granting independence has been to assign contractual rights and obligations to successor governments. See O'Connell, *International Law*, Vol 1, (1970) 382.

it succeeds.[21] In this century, the idea of universal succession has suffered heavy blows. This is largely because the character of the succeeding state is often very different from that of the state to which it succeeds. The earliest example was that of the Soviet state, created as a result of the Bolshevik Revolution in Russia, which is based on a fundamentally different concept of rights and obligations from those of the Czarist state. Whereas the Czarist state had a concept of "private property," the abolition of private property is one of the fundamental aspects of Soviet socialism. Similarly, it may be argued that an important aspect of colonialism was the acquisition of property and land rights for the benefit of the colonial power and settlers. It is this aspect which led to the economic dependence of the colony on the metropolitan state. Therefore, one aim of an independent state must be to bring an end to economic as well as political dependence.

This argument is in line with a modified version of the negativist theory which seems to command fairly general acceptance today. Thus Okoye says:

> The commonly accepted views as to the consequences of succession seems to have been that obligations under contracts are terminated upon changes of sovereignty.[22]

However, this termination is subject to:

> ..."the obligation" to respect the acquired rights of the private party by indemnifying him for taking over the equitable interest (not the contract *per se*) created as a result of the money he has invested and the labour he has expended.[23]

State practice generally tends to support this view.

The colonial powers have normally attempted to insist on some constitutional protection for the property rights of their

---

21 See generally Odokang, *Succession of New States to International Treaties* (1972) 449, citing four different approaches on the subject mentioned by Delson, "Comments on State Succession," (1966) *Am. Soc. Law Proc.* 111.

22 Okoye, *International Law and the New African States* (1972) 108; see also O'Connell, *op. cit.* 382.

23 *Ibid.*

> the meeting at which a notice under subsection (2) of this section is laid before it or at the next following meeting disallow that notice.

This section provides the normal process by which any consensual re-negotiation of the agreement may be effected. It is important to note that the House of Assembly has the ultimate controlling power over any such re-negotiation. Nevertheless, section 5 does not provide the only method for variation of the agreement. The alternative technique is variation by legislation, as provided for in section 6(3).[27] Although B.C.P.'s consent will normally need to be obtained under paragraph 6(3)(c), this may be over-ridden by a contrary intent, whether express or implied, in the law.

Yet clause 2(c) of the agreement is intended to control the obviously wide powers of unilateral variation provided by section 6(3)(a). This sub-clause provides that in the event of unilateral variation, the company, the members of the company, and the beneficial owners of shares in the company shall have the same rights and remedies as if there were a breach of the agreement. This is an attempt to protect the status of the agreement as an agreement irrespective of its incorporation into the act as part of the law of this country.

It is not easy to determine whether this attempt would be effective. Let us assume, for example, that the legislature should pass an act expressly abolishing the tax holiday period provided in clause 7(a). This would operate as a valid unilateral variation of the agreement under section 6(3)(a). However, could the company succeed in an action claiming breach of the agreement by virtue of clause 2(c), either in the courts of this country or in a foreign forum?[28]

The Papua New Guinea Supreme Court would have to apply Papua New Guinea law as the governing law. It would be bound to apply the new taxation provision, and apart from clause 2(c) there would be no question of any right to damages. However, it is arguable that clause 2(c) does effectively preserve the rights of the company to damages. Strangely, though, this would be by virtue of the status of the clause as part of the enacted law of

---

27 The word used in the subsection is "law," implying changes brought about by case law as well as by legislation.

28 Apart from a specific breach of clause 7(a), a breach of clause 17(a)(ii) which prohibits discriminatory legislation against B.C.P. might also be involved.

the country. Thus, the right may be abrogated by appropriately worded legislation, specifically preventing the operation of the sub-clause.[29]

Where the action is brought in a foreign forum, the result would depend on the conflict of laws rules of the country concerned. In the normal case, the court will apply the law of Papua New Guinea as the law governing the agreement.[29A] Yet, again, where there is express derogation from clause 2 the foreign court would have to apply the provision concerned, unless it could find a reason of public policy for refusing to apply it.[30]

The real effect of clause 2(c) is probably to preserve the company's rights under public international law, as different from private law. Thus, apart from consensual re-negotiation of the agreement, the Papua New Guinea government, so long as it is bound by the agreement, has fairly broad powers of unilateral variation of the agreement as recognised by section 6(3) of the act. These powers are, however, subject to preservation of the rights of the company to compensation under international law. The nature of these rights will become clearer in the next two sections on expropriation and compensation.

V. *Expropriation*

Clause 17 of the agreement specifically prohibits interference with the company and expropriation. Thus, clause 17(a) prohibits interference with the rights of B.C.P., members of the company and beneficial owners of shares in the company, particularly in relation to:

---

29 The relevant arguments are the same as those relating to fetters on the sovereignty of the House of Assembly; see footnote 15.

29A Clause 27 of the agreement provides, "The Agreement shall be governed by the law of the Territory."

30 Assuming the defences of sovereign immunity or act of state are not applicable. A court from common law countries cannot use the ground that it would be applying a foreign tax statute, as the question of enforcement only arises as an incidental issue. See Dicey and Morris, *Conflict of Laws* (1967) 161-2. Courts of civil law countries give a much wider ambit to public policy than courts in the common law countries do.

(a) B.C.P.'s freedom to choose its employees (clause 17(a)(i));

(b) B.C.P.'s freedom to declare credit or pay dividends (clause 17(a)(i));

(c) discriminatory industrial, fiscal, social or other legislation (clause 17(a)(ii)).

By clause 17(b) the government is prohibited from:

(a) cancelling any leases, permits, etc. (clause 17 (b)(i)); and
(b) resuming or expropriating any assets, products or shares (clause 17(b)(ii)).

The prohibitions in clause 17 are, however, made subject to the proviso that the powers of the government to acquire land compulsorily under the *Land Act* are preserved where the action is:

(a) necessary for the defence or public safety of the Commonwealth of Australia or of Papua New Guinea; or

(b) if such acquisition is for a public purpose and does not prejudice B.C.P. or interfere with its operations under the agreement.

Expropriation is defined in clause 17 more broadly than in international law. The agreement prohibits "substantial interference with the rights of the owner fully to utilize and enjoy or deal with or dispose of" his products, shares or business."[31] Such a definition could include government measures like excess profits taxes, import and export restrictions, leasing conditions and even reporting requirements. Moreover, clause 17 adds to the definition of expropriation current in international law; it provides that government interference will be deemed expropriatory unless it meets three conditions: first, it must not be expropriation as generally defined in international law; but, further, it must be "equitable" and "in the circumstances of the case and having regard to similar action taken in relation to other persons in the Territory reasonable and necessary for the peace order and good government of the Territory."[32] Thus, a government

---

31 *Mining (Bougainville Copper Agreement) Act* 1967, Schedule, Clause 17, Proviso.

32 *Ibid.*

action, which the general principles of international law would not consider expropriatory, could still be defined as expropriation under the agreement if it were, for example, not necessary to the peace, order or good government of Papua New Guinea.

The clause is very comprehensive in its prohibitions. The proviso appears to allow only minor exceptions and action only in times of national emergency or civil commotion in the area. However, the main froom for manoeuvre on the part of the Papua New Guinea government lies in the rights of expropriating of the House of Assembly under Papua New Guinea law and of the government under international law.

As we have seen already, the legislative powers of the House of Assembly to repeal or amend the act and to rescind or vary the agreement remain unfettered.[33] Thus, the government could enact through the House of Assembly legislation varying clauses 2(c) and 17, [34] and at the same time expropriating B.C.P. in the public interest. The rights of B.C.P. under Papua New Guinea law would then depend on whether provision for compensation had been made in the new legislation. If such provision had been made, it would be the only right for compensation available to the company under Papua New Guinea law. Where no such provision had been made, the company would have a right to seek compensation through arbitration or by action in the courts of this country, unless the legislation expressly or by implication prohibited payment of compensation. Thus, it is possible for the government, by taking appropriate steps, to ward off any claims for compensation under Papua New Guinea domestic law.

The government's position may be different where the action is brought in a foreign forum by B.C.P. or where a claim is made under international law on behalf of the shareholders by a state representing them. In both situations the status of the expropriatory legislation would be in issue.

An action in a foreign court directly against the government can normally be avoided by a plea of sovereign immunity by the Papua New Guinea government after independence and by the Australian government on behalf of Papua New Guinea before independence. However, actions are often brought not against the

---

33 See above at text accompanying footnotes 24-27.

34 These clauses will need to be amended for the reasons discussed in relation to variation of the agreement.

government itself but against third parties who, for example, are in possession of some of the expropriated assets. A good example is the series of disputes arising as a result of the Iranian nationalisation of the Anglo-Iranian Oil Company.[35] In all these cases, the Anglo-Iranian Oil Co. claimed that the nationalisation laws should not be given effect in a foreign court because they were confiscatory and thus contrary to accepted principles of international law. However, in most of the cases, the courts refused to find the nationalisation confiscatory because a scheme of compensation had been provided. In only one case -- the Rose Mary case -- the British court at Aden decided that nationalisation of the company's assets was invalid because the scheme of compensation provided in the nationalisation law was not "prompt, adequate and effective."[36] The general tendency however, is for foreign courts to refuse to interfere with expropriatory acts of a foreign state so long as some compensation scheme is provided. Even where the compensation is obviously inadquate, courts may sometimes refuse to interfere by allowing an "act of state" defence.[37]

A claim for compensation under international law may be made on behalf of the shareholders by their state of nationality against the government of Australia before independence,[38] and against the Papua New Guinea government after independence. The outcome of such a suit under international law is in much doubt today. For many years, it was generally agreed that there could be no expropriation without "prompt adequate and effective" compensation. However, with the onset of socialist revolutions

---

35 *Anglo-Iranian Oil v. Idemitsu Kosan Kabushiki Kaisha* (1953) *Int LRep* 305; *Anglo-Iranian Oil Co. Ltd. v. Jaffrate (The Rose Mary)* (1953) 1 *WLR* 246, (1953) *IntLRep* 316; *Anglo-Iranian Oil Co. Ltd. v. S.U.P.O.R. Co. (The Mirrella)* (1955) *IntLRep* 19; *The Anglo-Iranian Oil Case (The United Kingdom v. Iran)* (1951) *ICJ Rep* 89, (1952) *ICJ Rep* 93.

36 *Anglo-Iranian Oil Co. v. Jaffrate (The Rose Mary)* (1953) 1 *WLR* 246, (1953) *IntLRep* 316.

37 *Banco Nacional de Cuba v. Sabbatino* (1964) 376 *US* 398, (1964) *AJIL* 779.

38 As the controlling shareholder in B.C.P. is an Australian company, there can be no claim under international law on behalf of C.R.A. before independence.

nationals as a condition for granting independence.[24] These attempts have often failed to succeed, and it appears to be accepted that most new states may refuse succession to rights and duties under concession agreements.[25]

At present sovereignty over Papua New Guinea remains in the hands of the Australian government, and no question of state succession a rises under international law. However, with the creation of a new state on independence, sovereignty will pass to the government of Papua New Guinea. In the circumstances, the government will not necessarily succeed to the Bougainville agreement unless it takes steps to affirm or approve the agreement. State succession thus provides the legal pawn in government's moves towards re-negotiation of the agreement.

Having discussed the constitutional and international law parameters within which the act and the agreement operate, I shall now consider three specific issues -- variation of the agreement, expropriation, and compensation.

IV. *Variation*

The act itself provides in section 5 a specific technique for varying the agreement:[26]

> (1) The Agreement may be varied by a further agreement or agreements between the Minister on behalf of the Government and the Company.
>
> (2) A further Agreement under subsection (1) of this section is of no force or effect until approved by the High Commissioner in Council by notice in the Gazette.
>
> (3) A notice under subsection (2) of this section shall be laid before the House of Assembly within fifteen sitting days after the date of publication of the notice, together with a copy of the further agreement to which it relates.
>
> (4) The House of Assembly may by resolution passed at

---

24 The important issue has often been the nature and manner of compensation, discussed below at text accompanying footnote 37.

25 See Odokang, *op. cit.* 465.

26 Clause 19 provides specifically for variation of leases.

and more recently with the independence of former colonies, this consensus no longer exists.[39] Although most countries agree that there is a right to compensation, it is no longer a definite and universal rule of international law. Moreover, even where the right to compensation is accepted, there is no agreement about a method or standard of computing adequate compensation.

This lack of consensus effectively leaves the settlement of investment disputes to international diplomacy and power politics. The strong developed nation often has, in such a situation, the power to bring the weak under-developed country into line. The stronger nation can use various threats and promises:

(a) diplomatic protest and the breaking off of diplomatic relations;

(b) cutting off aid to the country concerned (a cut in Australian aid to Papua New Guinea, for example, would have very harsh results);

(c) preventing new investment in key economic areas;

(d) reduction of trade quotas or preferences for Papua New Guinea commodities or even trade embargoes;[40]

(e) freezing of assets (this has been used as retaliation for the nationalisation of assets);

(f) military solutions (precedents for this range from direct intervention, as in the case of the Bay of Pigs invasion of Cuba, to more indirect displays of power, such as the coup against Mossadiq after the Iranian oil nationalisation or the coup that overthrew President Allende of Chile after the Kennecott copper mines were nationalised: reactionary elements in the country concerned are often helped to overthrow existing regimes);

---

39 See generally Steiner and Vagts, *op.cit.*, chapter 4.

40 The United States government reduced the Cuban sugar quota in retaliation for Cuban nationalisation of a U.S. oil company. The Cubans replied by nationalising all United States assets in Cuba. The United States then imposed an economic embargo on Cuba and froze all Cuban assets in the United States. This had the result of driving Cuba further into the socialist camp. These events formed the background to the *Sabbatino* case, *supra* at footnote 32. The consequences of an economic war between Australia and Papua New Guinea can be imagined.

(g) legal solutions (the internationally strong often forces the weaker power to arbitrate the question of compensation; thus, the United States government has been successful in obtaining compensation for expropriations by all the Eastern European socialist countries).[41]

The Papua New Guinea government has the right, under both national and international law, to expropriate the company, whether or not the government accepts the obligations set by the agreement. The main difficulties in the way of expropriation are not legal but political. Even here, the key issue in recent years has not been the right to expropriate but the standard of compensation once expropriation has taken place.

VI. *Compensation*

Neither the act nor the agreement provides a scheme of compensation. Therefore, in any case of breach of the agreement or expropriation, the method of compensation will be determined by Papua New Guinea or international law. The common law of contract, which applies in Papua New Guinea, provides a very high rate of compensation for loss of future profits. However, most nationalisation decrees or laws provide expressly for or against compensation. Were Papua New Guinea to enact a nationalisation statute, with compensation provisions, it would become the operative legal rule in all disputes governed by Papua New Guinea domestic law.

The problem arises where the matter is governed by international law. As has been mentioned already, majority opinion and state practice suggest that some form of compensation is necessary, but there is much disagreement over the form and rate. While some Western writers suggest that compensation must be "prompt, adequate and effective," the newly independent states are generally very critical of this standard. They consider it merely an attempt by the economically developed countries to assure the security of property of those of their citizens who wish to invest capital, utilise skills or otherwise do business in the underdeveloped countries.[42] The position of these

---

41 The political strength of the United States has enabled it to obtain better deals for its companies with foreign countries than have been obtained by the relatively weak United Kingdom. Steiner and Vagts, *op.cit.* 332.

42 See Okoye, *op. cit.* 182-3, and Odokang, *op. cit.* 452-456, 502-507.

countries is best represented by Paragraph 4 of the United Nations General Assembly *Resolution on Permanent Sovereignty over Natural Resources:*

> The owner shall be paid appropriate compensation in accordance with the rules in force in the State taking such measures in the exercise of its sovereignty and in accordance with international law. [43]

That is, the standard of compensation ought to be judged by the standard which the expropriating state deems appropriate for its own nationals and in accordance with local laws, regulations and orders.[44]

The difference between the Western standard and Afro-Asian standard, as stated in the U.N. resolution, arises from their different priorities. The Western standard is based on the expected economic return on the capital invested: multiplying the number of years the concession still has to run by the annual expectation of profit, the Western nations require that compensation reflect this estimate of lost future earnings. Thus, even assuming that B.C.P.'s average net profit would not be above $100 million, as in 1973, but somewhere in the region of $20 million over the rest of the concession period of 36 years,[45] the compensation claim would still be on the order of $720 million.

The Afro-Asian standard is based on an estimate of past dealings; the investor is compensated for the capital he has already invested in the country. Applying this standard, the company often ends up in debt to the country concerned, because in the view of the expropriating government, many companies have mad "excessive" profits in relation to the capital invested during the colonial period or during periods when the countries were led by governments submissive to the will of the investors. Therefore, a government believing in economic nationalism feels justified in subtracting "excess profits" from the amount of capital invested.

---

43 *Resolution 1803* (XVII), Dec. 14, 1962; see also *Resolution 1314* (XIII), Dec. 12, 1958.

44 *Asian-African Legal Consultative Committee Reports*, 3rd Session (1961) 43, 46, 49, 141-2.

45 Rights of renewal have not been computed in this estimate. Note also that the present mining operation probably does not have more than a 30-year life span.

The nationalisation of the Belgian copper company, Union Miniere du Haut Katanga, by the Congolese government is a good example. The company claimed 40,000 million Belgian Francs from the government. However, the government claimed that Union Miniere had taken out of the Congo net profits amounting to 200,000 million Belgian Francs, and requested the company to pay the government 7,500 million Belgian Francs. This dispute was ultimately settled by diplomatic action.[46]

A similar case, but with less happy results for the country concerned occurred when Chile nationalised the holdings of Kennecott Copper. The Chilean government determined that while the book value of the company's assets was $365 million, it had made $410 million in excess profits.[47]

The company sued in France, where the government was attempting to sell the copper, and won on the grounds that the expropriation had been invalid because fair compensation had not been provided. But the company's real victory came through political, rather than legal channels, when the Chilean government was overthrown and its President assassinated by right - wing generals.[48]

The situation in Papua New Guinea is different from that in countries such as Congo-Kinshasha (now Zaire) or Chile, as the Bougainville mine is a fairly recent venture. Nevertheless, there would already be a substantial difference in the calculation of compensation according to the two standards considered. As noted

---

46 See Odokang, *op. cit.* at Tanzania's *Building Acquisitions Act 1971* provides a scale of compensation for buildings based on the assumption that an entrepreneur obtains his full return on capital in the course of 10 years.

47 The Company considered its "fair market value' to be something in the order of $1 million. See Lillich, "The Valuation of the Copper companies in the Chilean nationalisations" (1972) 66 Proc.Am.Soc. of Int. Law 213. For a Chilean view, see Vicuna, "Some International Law Problems Posed by the Nationalisation of the Copper Industry by Chile" (1973) 67 A.J.I.L. 711.

The moral to be gained from the various compensation suits seems to be that nationalising governments should not attempt to sell their products in France.

48 The involvement of U.S. firms such as I.T.&T. in illegal political activity in Chile before the coup has become common knowledge because of revelations in U.S. newspapers. There is no direct evidence linking Kennecott with these activities, however K. Clark *Reality and Prospects of Popular Unity* (1973) 97.

above, compensation calculated by Western standards would give the company as much as $720 million, but, if the company were offered today its book value of $370 million, minus a part of its profits of nearly $300 million, then the country would owe less than $100 million, after expropriation.[49]

In the arguments between the company and the country over compensation, both sides consider that their claim is correct.[50] In the end it is more often practical realities than justice that dictate the solution. The deciding factor may be the relative strength of the underdeveloped country and the company. The company often appears stronger, because it is supported by an economically and politically powerful country. It may also have influence over purchasers of its products. The underdeveloped country is economically weak, and it may find that obstructive techniques employed by the company further weaken its position. Yet it may also find allies in countries other than those of the parent company. Thus Italian and Japanese buyers and courts tacitly supported the Iranian oil nationalisation, the Soviet Union supported Cuba, and the British sold buses to Cuba in defiance of the United States embargo on that country.

VII. *CONCLUSION*

The purpose of this paper has been to establish the general legal framework within which the act and the agreement operate. It has been suggested in the course of the paper:

(a) that the agreement is a concession agreement, and international practice establishes such agreements as subject to fairly frequent changes, expecially in favour of the host country;

(b) that there are no legal fetters on the powers of the Papua New Guinea House of Assembly either to amend or repeal the act or to vary or rescind the agreement so as to make these changes legally effective within Papua New Guinea.

---

49 Bougainville Copper Ltd., *Annual Report* (1973); Bougainville Copper Ltd., *Half - Yearly Earnings Statement* (July 1974).

50 Brown, "Compensation for Expropriated Assets -- Justice or Value?" paper delivered at the seventh Waigani Seminar (1973).

(c) that an independent Papua New Guinea will be bound by the agreement under international law only if it takes steps to affirm or approve the agreement under international law rules of state succession;

(d) that one method of varying the agreement is by consensual re-negotiation under section 5 of the act, but this does not prevent unilateral variation by the House of Assembly under section 6(3)(a); the company may in such a case have a right to damages for breach of the agreement under clause 2(c), unless amending legislation specifically derogates from that clause;

(e) that even though expropriation is largely prohibited under clause 17 of the agreement, the House of Assembly may effectively expropriate under Papua New Guinea law, with or without compensation; moreover, the government probably has a right to expropriate under international law, subject to the payment of some form of compensation;

(f) settlement of disputes over expropriation tends to be influenced less by legal considerations than by power politics;

(g) the question of compensation for expropriation under international law is hotly disputed; generally the Western standard is compensation for loss of expected profits, whereas developing countries suggest a standard that takes into account compensation for the value of capital invested in the light of past returns on capital.

It is not the purpose of this paper to suggest that the government take any or all of the measures discussed. It is hoped, however, that this discussion has removed some of the mystification surrounding the legal nature of the agreement so that the political and economic issues involved in the process of re-negotiation can be seen in their proper perspective.