

2.

Challenges Undermining Monitoring and Enforcement

Although most stakeholders agree that monitoring and enforcement are essential to ensuring that mining projects proceed in accordance with the legal framework—and thus that the risks and opportunities of mining projects are distributed appropriately—these important activities are often neglected. Deficiencies in capacity, transparency and government monitoring incentives all contribute to insufficient monitoring and enforcement activities.

While all countries confront capacity, transparency and incentives challenges, they may be more or less pronounced in different places at different moments in time. But wherever and whenever they exist, they should not be considered in isolation. Instead, these challenges operate together, and they must all be confronted to enable effective monitoring. Similarly, government and civil society monitoring should not be looked at in isolation but rather as mutually enforcing and beneficial activities. Governments, civil society and companies must work together in partnership to enhance their monitoring efforts and to confront the challenges discussed in this section.

2.1 Capacity

Perhaps the most obvious challenge to monitoring is lack of capacity. Capacity is not just a matter of training or the wealth of the state. It reflects politics and priorities as well as other factors that contribute to sustainable, effective governance. In this way, capacity challenges are linked with incentives: until those in power have the incentives to devote resources to improving capacity for monitoring and enforcement, the challenges are unlikely to improve.

Governments often lack the capacity to inspect, audit and review companies' operations over the typically very long life of the project. First and foremost, they do not have enough staff to complete the necessary monitoring. Beyond that basic challenge, they may also lack the skills, technology, vehicles and financial resources to conduct that monitoring effectively. Even when skills and technology are available, bad policies or weak overall governance can make it impossible to plan and budget for appropriate monitoring. A 2010 report from the World Economic Forum surveyed 13 countries in three regions and found that "lack of government capacity to ensure compliance through contract monitoring and implementation/enforcement is a frequently cited problem."⁶ In Liberia, participants in the study reported that "[m]onitoring compliance with MDAs is the most important and at the same time most challenging issue, due to lack of government capacity and budget."⁷

Capacity remains a challenge for all governments. For example, lack of capacity has been partially blamed for the 2010 Deepwater Horizon oil spill in the United States. The capacity challenges related to the spill are discussed in Box 1. Canada's capacity challenges in overseeing exploration activities are discussed in Box 2.

6 World Economic Forum, *Stakeholder Perceptions and Suggestions, Responsible Mineral Development Initiative 2010*, 2011, http://www3.weforum.org/docs/WEF_MM_RMDI_Report_2010.pdf.

7 World Economic Forum, 26.

Box 1 | Capacity Challenges in the United States and the Deepwater Horizon Oil Spill

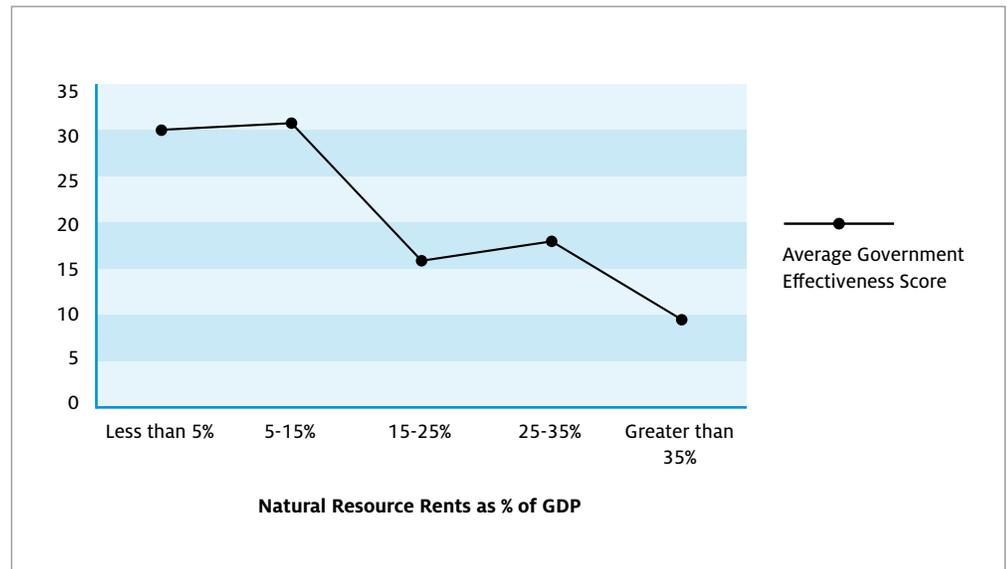
In 2010, the United States experienced a catastrophic oil spill when Transocean’s Deepwater Horizon offshore oil rig exploded in the Gulf of Mexico. The initial explosion killed 11 people. Over the course of the next several weeks, five million barrels of oil spread throughout the gulf, devastating the environment and the ecosystem. A national commission, appointed by the U.S. government to investigate the spill, concluded that the federal government did not lack the authority to control offshore oil exploration and drilling, but that it did lack the resources to effectively exercise that control.

The root problem has . . . been that political leaders within both the Executive Branch and Congress have failed to ensure that agency regulators have had the resources necessary to exercise that authority, including personnel and technical expertise, and, no less important, the political autonomy needed to overcome the powerful commercial interests that have opposed more stringent safety regulation.⁸

Government capacity tends to be particularly weak in countries rich in natural resources. Among poorer countries, those with a higher percentage of GDP coming from natural resource rents tend to have lower government effectiveness. Figure 1, based on data from the World Bank, illustrates the trend. The World Bank Governance Indicators rank countries along a scale of government effectiveness, with each country receiving a percentile rank.⁹ The higher the government effectiveness score, the better the country’s governance.

figure 1:

Natural Resource Rents and Government Effectiveness in Low-Income and Lower Middle-Income Countries¹⁰



Sources: World Bank, Governance Indicators: Government Effectiveness, 2009, <http://info.worldbank.org/governance/wgi/resources.htm>; World Bank, Country and Lending Groups: Income Groups, 2011, <http://data.worldbank.org/about/country-classifications/country-and-lending-groups>; World Bank, Indicators: Total natural resources rents (% of GDP), 2009, <http://data.worldbank.org/indicator/NY.GDP.TOTL.RT.ZS>.

8 National Commission on the BP Deepwater Horizon Oil Spill and Offshore Drilling, *Final Report: Deep Water: The Gulf Oil Disaster and the Future of Offshore Drilling*, 2011, 67, <http://www.oilspillcommission.gov/final-report>.
 9 “Government effectiveness captures perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government’s commitment to such policies.” World Bank, Governance Indicators: Government Effectiveness, 2009, <http://info.worldbank.org/governance/wgi/pdf/ge.pdf>.
 10 Low-income and lower middle-income countries are defined as those with a per capita gross national income of less than \$3,975.

Capacity challenges can be exacerbated by the so-called “revolving door” between government and industry. Once government officials have built up capacity through training and experience, they become attractive hires for the private sector. Because companies can typically offer more generous compensation, government agencies often struggle to retain their best employees. Moving in the other direction, the revolving door can also bring private sector employees into government. Well-connected business leaders may seek government jobs and political appointments in order to gain positions of power and influence in the agencies that oversee their industry. This situation exacerbates many of the incentives challenges discussed in Section 2.3.

Capacity is also a challenge for civil society. Even when laws and contracts are readily available, civil society may lack the skills necessary to analyze and understand the deals that their government has negotiated with companies and the technical and engineering expertise to determine whether those deals are being complied with. Sometimes the problem is not an actual lack of capacity but instead the belief that capacity is lacking. Citizens have been led to believe that they cannot possibly understand laws and contracts, when in reality they can read them and ask many good questions about the commitments and whether they are being met. Appendix 1 provides a list of such questions.

Box 2 | Capacity in Government Oversight of Exploration in Ontario, Canada

In countries with emerging minerals sectors, the capacity of the mining ministries to promptly review and issue exploration permits determines how quickly the private sector is able to get out into the field. Likewise, institutional capacity is essential for governments to be able to track which companies are fulfilling their responsibilities.

Ontario, Canada, demonstrates the difficulty of effective administrative oversight of exploration, even for a developed country. Ontario maintains a system of mining permit assessment auditors to ensure that the parameters of the permits are being followed. Ontario receives about 1,000 assessment reports each year, and, by law, the ministry’s three assessment reviewers must review the listed payments to ensure that they qualify as exploration expenses and, if not, challenge the companies’ payments within 90 days. Even a relatively small mining center with relatively large administrative capacity such as Ontario ends up approving 25 to 40 reports each year without reviewing them. Less than half a percent of the assessment reports are subjected to a detailed review in which the companies have to justify each exploration expenditure. The provincial auditor recommended much stiffer enforcement of the assessment reporting requirements given the likelihood that Ontario is losing out on significant amounts of exploration activity.¹¹

Ministry Staff—Low Staff Numbers and High Turnover

A key challenge for governments is attracting and retaining enough sufficiently trained staff to conduct the monitoring. The required number of inspectors and inspections is driven primarily by the number of active mining projects and the number of workers employed in the industry. A comparison of inspection figures across countries helps illustrate the capacity challenges that some government monitoring agencies face.

In Chile, which is often seen as a model because of the way it has managed revenue from copper to benefit its people, recent events have exposed the weaknesses in its health and safety monitoring. A lack of inspection resources has been cited as one of the factors associated with the accident at the San Jose mine in 2010 in which 33 miners were trapped underground for 69 days.¹² A group of the rescued miners is now suing the Chilean government for negligence, claiming that the National

11 Office of the Auditor General of Ontario, *2005 Annual Report*, sec. 3.09: Ministry of Northern Development and Mines: Mines and Minerals Program, www.auditor.on.ca/en/reports_en/en05/309en05.pdf.

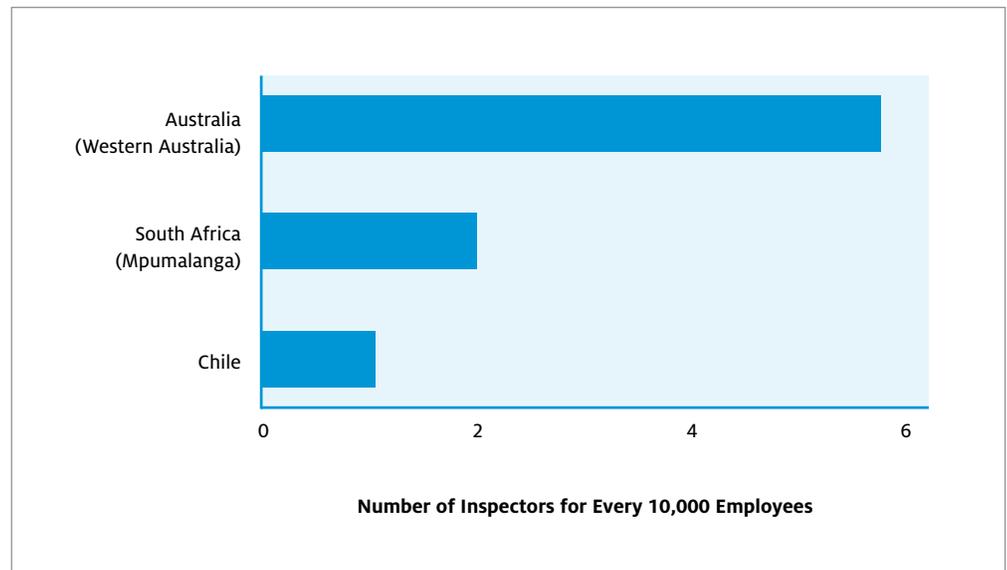
12 Gideon Long, “How safe are Chile’s copper mines?” *BBC News*, Oct. 8, 2010, <http://www.bbc.co.uk/news/world-latin-america-11467279>.

Geology and Mines Bureau failed to conduct proper inspections of the mine before it collapsed.¹³ Until the accident, the bureau had just 18 inspectors responsible for enforcement in an industry that employs 175,000 workers.

South Africa has also struggled to maintain an adequate health and safety inspection staff. One of the major mining regions, Mpumalanga, has 172 registered mines and employs 72,000 people. In the regional office of the Department of Mineral Resources (DMR), the division charged with overseeing occupational health and safety has just 14 inspectors, compared with its target employment of 24. In comparison, in Western Australia, there are 39 appointed inspectors for an industry employing 70,000.

figure 2:

Comparison of Occupational Health and Safety Inspectors in Chile, South Africa and Australia



Beyond mere numbers of inspectors, governments must also ensure that inspection officers have the expertise to conduct their monitoring effectively. In Western Australia, a 2009 review of the Mines Safety and Inspection Act recommended “that the mining engineering discipline remain a core competency for the most senior level in the Inspectorate; [t]hat mining engineering Inspectorate expertise be supported by other specialist and generalist disciplines, more broadly based, as may be required.”¹⁴ The dangers presented by inspectorates without the requisite expertise were highlighted following changes to the appointment of mine inspectors in the Northern Territory under its mining legislation in the 1990s. These changes were prompted by financial considerations and recruitment and retention challenges. The then Mine Management Act was amended to remove the title of “Chief Government Mining Engineer” and any reference to any “Mines Inspectors.” Instead these titles were replaced with the position of “Mine Audit Officer.” The legislation did not provide any essential qualification criteria, only desirable criteria, including a generic health and safety qualification and some mining experience. The 2009 study identified the following factors of the amendments as risks to effective enforcement:

- Audit officers did not necessarily have the qualifications and experience to understand mining concepts, particularly geomechanics, ventilation and other disciplines.

13 Dorothy Kosich, “Rescued Chilean miners sue govt. claiming negligence,” *Mineweb*, July 18, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page72068?oid=131665&sn=Detail&pid=92730>.

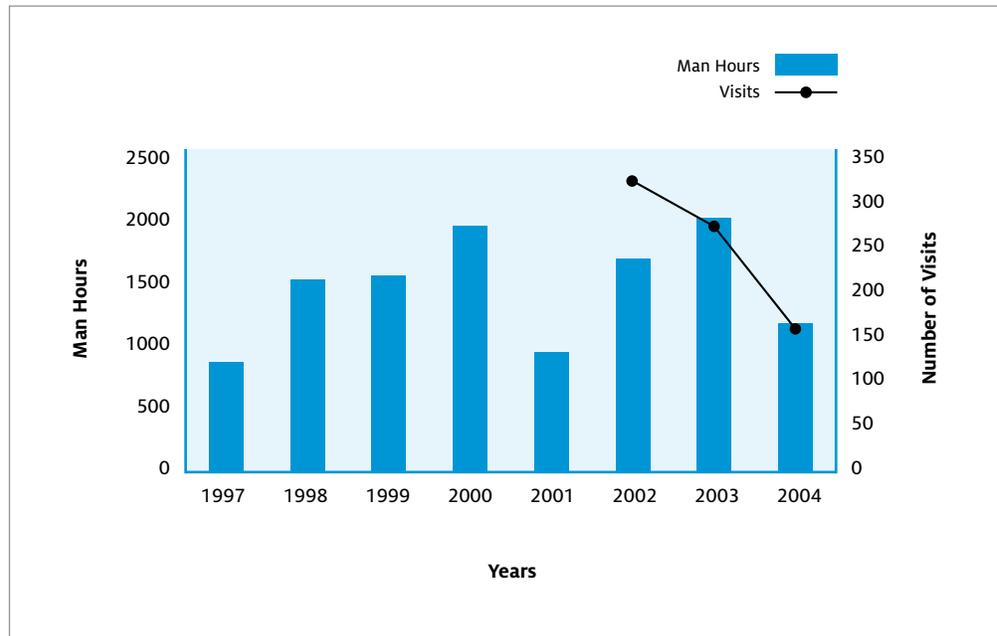
14 Commissioner Stephen J. Kenner, *Review of the Mines Safety and Inspection Act 1994*, Western Australia Industrial Relations Committee, 2009, 82, http://www.dmp.wa.gov.au/documents/Reports/MI_Act_KennerReport.pdf. In this jurisdiction, mines inspectorates comprise personnel from the following disciplines: mining engineering, geotechnical engineering, mechanical engineering, electrical engineering, structural engineering, chemical and process engineering and metallurgy, noise and vibration, chemistry, radiation, occupational hygiene, and occupational health and safety.

- It was much easier for senior management to hide an issue with an inexperienced government official.
- Audit officers were subordinate in their approaches to the mining companies.

Staff retention is also a challenge for many government enforcement agencies. In Botswana, the number of mine inspections and the amount of time spent on them dropped sharply from 2002 to 2004, as illustrated in Figure 3. The Department of Mines attributed this decrease largely to high staff turnover.¹⁵

figure 3:

Botswana: Man-hours Spent On Safety, Health and Environment Visits during 1997-2003
 (Data unavailable for number of visits from 1997-2011)



Source: Botswana Department of Mines, 2004 Annual Report, 13, <http://www.mines.gov.bw/dom%202004%20Annual%20Report.pdf>.

In South Africa, a report on environmental compliance and the performance of the DMR in the Eastern Cape notes that the office staff is unable to conduct inspections to verify compliance with environmental management programme reports (EMPRs); the lack of capacity “has serious implications in terms of regulating the compliance of the mining concerns with their EMPRs. The low level of compliance monitoring can be directly related to staff capacity and logistics problems at the regional office. Environmental management and sustainability cannot be enforced under these capacity constraints.”¹⁶

These ministry capacity deficiencies result in insufficient, inconsistent monitoring of company operations, which can ultimately lead to reduced compliance.

Proliferation of Legal Frameworks

As noted above, a mining company’s obligations within a country may be defined by a variety of legal instruments. In some cases, the company’s obligations are defined primarily in laws and regulations. In those cases, the legal framework that governs the mining industry within a country tends to be uniform across companies, with relatively little variation in the obligations

¹⁵ Botswana Department of Mines, 2004 Annual Report, 12, <http://www.mines.gov.bw/dom%202004%20Annual%20Report.pdf>.

¹⁶ Deidre Watkins, “An Assessment of the Environmental Compliance Monitoring Capacity of the Department of Minerals and Energy, Eastern Cape” (master’s thesis, Rhodes Investec Business School), 2008, ii, eprints.ru.ac.za/1564/1/Watkins_MBA-TR09-90.pdf. EMPRs are the main compliance tool for the mining sector. An EMPR includes information on planned mining operations, how they will impact the environment, how those impacts will be mitigated and managed throughout the mine’s life cycle, and planned monitoring.

from company to company. In other cases, companies sign individual contracts with governments, and those contracts define the majority of the companies' obligations, including taxes, environmental requirements and so forth. Contractual regimes can be problematic for a number of reasons. They leave room for corruption by requiring that deals be individually negotiated, and they tend to lead to worse outcomes for governments because government negotiators make concessions to companies during the negotiating process. They also contribute to a wider variation in the legal frameworks applicable to each company, complicating monitoring efforts.

A hierarchy of legal norms also contributes to the problem. Even in countries that have an established mining code and an otherwise well-developed legislative framework to govern the mining industry, the executive branch may be allowed to conclude contracts that deviate from the general legal framework. For example, Zambia's mining code states: "For the purpose of encouraging and protecting large-scale investments in the mining sector in Zambia, the Minister may, on behalf of the Republic, enter into an agreement relating to the grant of a large-scale mining licence . . . [and the agreement] may contain provisions which notwithstanding the provisions of any law or regulation shall be binding on the Republic . . ." ¹⁷ In this situation, individual contracts can trump the country's laws and regulations.

This proliferation of separate legal frameworks in contractual regimes can make it more difficult for both government and civil society to effectively monitor companies' obligations.

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For example, in a country with eight large mining projects, each subject to its own contract, government monitoring agencies will need to be familiar with all eight legal regimes and will need to tailor their interactions with each project according to the requirements of the contract. Similarly, civil society will need to access and analyze eight different contracts and vary their monitoring activities accordingly.

In a permit regime, on the other hand, a government monitoring official need only learn one legal framework—the uniform framework defined by the country's laws. Civil society's monitoring efforts will also be simplified. Some countries have used model contracts to cut down on the proliferation of legal frameworks. Model contracts are discussed in more detail in Section 3.2.

Monitoring contracts is difficult in the best of circumstances, but the additional challenges of monitoring multiple contractual regimes is further exacerbated by the fact that the same countries that tend to have contractual, as opposed to legislative, regimes also are less capable of monitoring mining projects. Canada's and South Africa's mining industries are each governed by a uniform legal and regulatory framework, whereas the DRC and Liberia rely more heavily on contracts. As a comparison, Canada and South Africa rank in the 97th and 68th percentile for government effectiveness, respectively, while the DRC and Liberia rank in the 2nd and 10th. ¹⁸ This means that the countries with the least capacity more often need to monitor larger and more complicated sets of company obligations.

New contractual structures, such as mineral-backed infrastructure loans, are presenting additional challenges in some countries. Box 3 discusses the unique challenges of monitoring these types of arrangements.

17 Zambia, Mines and Minerals Act, 1995, sec. 9.

18 World Bank, Governance Indicators: Government Effectiveness, 2009, <http://info.worldbank.org/governance/wgi/resources.htm>.

Box 3 | Special Challenges of Monitoring Mineral-Backed Infrastructure Loans

Mineral-backed infrastructure loans may present another challenge to governments and civil society groups attempting to monitor an array of company obligations. The loans represent an additional type of mining contract that governments and civil society may need to monitor. In this model, a country leverages its natural resource wealth to obtain a loan earmarked for infrastructure and development from a wealthy nation, usually China. The exact details of the financing plan will vary based on the agreement, but the recent deal between China and the DRC serves as a good example. In this deal, the DRC government contracted with a consortium of Chinese companies, forming a JV. The consortium agreed to lend the JV a large amount of money to develop infrastructure in the DRC. The JV will also conduct mining exploitation, retaining all profits derived from the concessions, without paying taxes or royalties. When the mining profits repay the loan, the tax holiday ends and the JV will be subject to the DRC's normal taxation regime.

These agreements provide unique challenges for contract monitoring. The challenges can be understood in the following categories:

Monitoring the Quality of the Infrastructure: Because infrastructure represents the primary value a host country receives in these deals, it is important to ensure the quality of that infrastructure. In the China-DRC deal, the Congolese government has committed to hiring external consultants to conduct this monitoring, but the money it initially allocated (2.4 percent for monitoring and administrative costs) has not been enough to hire satisfactory consultants. The government is reportedly planning to increase the allocation to 4 percent, but this still falls short of the 7 percent to 8 percent typically allocated for these kinds of construction projects.¹⁹ This example further illustrates the government's financial capacity limitations with regard to monitoring.

Identifying the Contracting Parties: In order to properly track the exchange of money and prevent transfer pricing, the host country needs to know with whom exactly they are contracting. If related companies are involved in a transaction, there are risks that the companies will inflate their costs to avoid paying taxes. Transfer pricing is discussed in more detail in Box 7 in Section 3.2. Knowing which companies are involved in a transaction is essential to identifying these possible transfer pricing risks.

Determining the Value of the Loan: The loan money is used to contract with companies to build infrastructure in the host country. The actual cost of construction is the total amount of debt the home country must repay with its mineral wealth. Civil society needs to be actively involved in monitoring the actual amount of debt as well as the terms of the construction deals made to build the infrastructure.

Identifying Other Project Benefits: In some countries where these deals are moving forward, a key area of concern may be technology transfer and local content. Citizens and governments may want to increase their own capacity to complete large-scale infrastructure construction projects in the future. As such, some of these deals may include provisions for hiring local workers or contractors, or providing training and knowledge. If these commitments are part of the deal, civil society must be aware of them in order to effectively monitor whether they are being honored. Monitoring local content benefits is discussed in Appendix 1.

Questions for Civil Society to Ask

What value is the host country getting for the deal?

- What infrastructure projects have been or will be undertaken as a part of the contract?
- What is the status of those infrastructure projects?
- What is the value of the infrastructure? What would the infrastructure costs have been if the project had been open for free bidding?

19 "Surveying Sicominex," *Africa-Asia Confidential* 4 (March 2011): 4-5.

Box 3 continued

- How much did the contractor companies receive for the construction? Were the inputs valued at arm's-length prices?
- Does the deal include any local content or training provisions? Have those provisions been fulfilled?

What does civil society require?

- The investment contract
- List of infrastructure projects undertaken in the loan
- Sums disbursed for infrastructure projects
- Status of infrastructure construction
- Assessments of infrastructure quality, or access to construction sites to enable their own assessments
- Value of minerals produced under the contract
- List of local contractors employed in construction and the sizes of their contracts
- Information on training programs for local workers and contractors

Decentralized Government Structures

In response to political pressures, many governments—particularly in Asia—have decentralized aspects of natural resource regulation, using constitutional provisions and statutes to devolve powers formerly held by the central government alone. Decentralized government structures pose many of the same monitoring challenges as centralized government structures. However, the multiple layers of government can exacerbate these challenges, since capacity and transparency may be weaker at the local level. Decentralization also presents additional problems, including coordination across levels of governments, overlapping mandates and devolution of responsibilities without financial or technical support.

The degree of decentralization varies greatly from country to country. Some systems decentralize revenue collection and management only, while others permit local authorities to undertake other types of regulation such as environmental and occupational health and safety regulation. At the most devolved end of the spectrum, advanced economies—including Canada and Australia—give virtually all authority over mining revenues and regulations to the provincial-level governments, the result of mining systems that in some cases pre-date strong central governments.²⁰ Argentina takes a middle road, delegating minerals management to the provinces but setting a national government-imposed cap of 3 percent on the mining royalty rate that the provinces may collect.²¹ Typical of several Asian countries, Indonesia previously had a highly centralized oversight structure but has now decentralized many mining oversight functions.²² Decentralization in Indonesia is discussed further in Box 4. In still other countries, like Gabon, decentralization legislation has been enacted, but implementing regulations have not been promulgated nor has funding been set up so the local governments can have actual control of the mining sector.²³

In the DRC, the country's vast geographical size is an obstacle to effective central administration and monitoring contracts. A new Constitution in 2006 attempted to address this problem by instituting a decentralized system of government, creating new institutions and increasing the power of local authorities. In reality, however, these changes have not taken place with respect to the

20 James Otto et al., *Mining Royalties: A Global Study of Their Impact on Investors, Government, and Civil Society*, World Bank, 2006, 78, http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2006/09/11/000090341_20060911105823/Rendered/PDF/372580Mining0r101OFFICIALOUSEONLY1.pdf.

21 Otto et al., 78.

22 The Indonesian Constitution places authority to regulate natural resources in "the State," which the government has interpreted as authorizing local control. See Indonesia, Constitution, 2002, art. 33, sec. 3 ("The land, the waters and the natural resources within shall be under the powers of the State and shall be used to the greatest benefit of the people").

23 International Monetary Fund (IMF), *Gabon: Report on Observance of Standards and Codes—Fiscal Transparency Module*, Country Report No. 06/388, 2006, 9-10, www.imf.org/external/pubs/ft/scr/2006/cr06388.pdf.

mining industry for at least two reasons. First, the Constitution affirms the national government's continuing authority to sign and monitor mining contracts. Second, the 2002 Mining Code included a provision stating that it could not be revised for at least 10 years, and it has therefore not been brought into harmony with the new Constitution's decentralization mandate. The code and the Constitution conflict, but whereas a constitution should normally take precedence according to the hierarchy of legal norms, this conflict has not been resolved in practice. The central government continues to monitor the mining industry, although the copper-rich Katanga Province has begun imposing its own additional taxes on mining companies.

Countries differ widely in the extent to which their revenue agencies are centrally managed, and whether or not a country's tax administration is centralized or decentralized can influence its effectiveness. Most developing countries have centrally controlled mining tax administrations, including most African nations and Papua New Guinea. In Australia, Canada and Malaysia, the federal government similarly has little role in managing land and resources, and administration of mining taxes is under the purview of provinces or states. But the federal government does have power over strategic minerals, such as uranium. And the government can also exercise power indirectly through control of imports and exports, foreign investment, and environmental and indigenous issues.²⁴

Box 4 | Decentralization in Indonesia

The concept of decentralization was introduced in Indonesia after the fall of the Soeharto regime in 1998.²⁵ As a response, Parliament passed laws authorizing subnational governments to manage natural resources within their territory and introducing fiscal decentralization and a revenue-sharing scheme.²⁶ However, the scheme led to confusion as to which level of government was truly responsible for mining. The 1967 mining law only gave local governments authority over nonstrategic and nonvital resources.²⁷ Although the government issued regulations in 2001 giving local governments the authority to issue mining permits for all reserves, the regulations were enacted under the 1967 law, which had clearly limited their authority.²⁸

Finally, in 2009 Parliament passed a new law, revoking the 1967 mining law and providing a clearer direction on mining corresponding to the decentralization era.²⁹ That same year, Parliament also passed a new law on regional taxes, limiting the types of taxes that can be imposed at the provincial and the district/city level.³⁰ The subnational governments cannot impose any taxes beyond those stipulated in the law, and the national government maintains authority over mining royalties and land rents.³¹

Many localities lack the capacity to effectively monitor mining companies. Decentralization schemes are often politically motivated (perhaps as a response to corruption in the national government) and rolled out “haphazardly” before local government institutions are developed.³² Poorly drafted statutes may lead to confusion as to which level of government is responsible for permitting

24 Otto et al., 76.

25 Indonesia, People's Consultative Assembly Decree (*Majelis Permusyawaratan Rakyat/MPR*) No. XV/MPR/1998 on the Organization of Regional Autonomy. For more information, see Widjajanti I. Suharyo, *Voices from the Regions: A Participatory Assessment of the New Decentralization Law in Indonesia*, United Nations Support Facility for Indonesian Recovery, 2000, http://goodgovernance.bappenas.go.id/publikasi_CD/cd_penerapan/ref_cd_penerapan/download/Lesson%20Learned%20Best%20Practices/Participatory%20Assesment%20Indonesia.pdf.

26 Indonesia, Regional Administration, Law 22/1999, articles 1, 2 (2), and 10 (2); Indonesia, Balanced Budget between Central and Regional Government, Law 33/2004, art. 14(c).

27 Indonesia, Basic Provisions of Mining, Law 11/1967, articles 1 and 47.

28 Indonesia, Government Regulation 75/2001.

29 Indonesia, Mineral and Coal Mining, Law 4/2009.

30 Indonesia, Regional Tax and Retribution, Law 28/2009.

31 Indonesia, Government Regulation 44/2003.

32 World Bank, *Entering the 21st Century: World Development Report 1999-2000*, 2000, 100, http://wdronline.worldbank.org/worldbank/a/c.html/world_development_report_1999_2000/chapter_5_decentralization_rethinking_government.

and oversight in particular substantive areas.³³ Government and civil society actors concerned with making sure decentralized regimes are effective can:

- *Clarify conflicting or overlapping mandates:* Given that the constitutional provisions authorizing decentralization tend to be vague and statutes may overlap, it may be necessary for civil society or local governments to engage in litigation or negotiations to clarify the lines of responsibility in a monitoring regime.
- *Ensure that governments are adequately capitalized:* Hastily constructed decentralization schemes may leave local governments without the financial and human resources to effectively carry out their monitoring responsibilities. Officials and advocates can work to ensure that financial incentives for monitoring are properly aligned at the local level, either via revenue sharing or through direct payment streams from the central governments.

2.2 Transparency

Effective monitoring relies on access to information, and a lack of transparency can be a challenge for both government and civil society monitoring efforts. Transparency is central to monitoring for at least two reasons:

- It is a condition for effective monitoring.
- It creates incentives for all stakeholders (government, companies and communities) to play by the rules.

Within government, not sharing information across departments in the executive branch can hamper monitoring. For other branches of government, particularly parliament, lack of access to critical information inhibits credible monitoring. And for civil society, access to contracts, environmental impact assessments (EIAs), work plans, revenue collection figures and other ongoing project information is essential to monitoring efforts but is often lacking.

Governments and companies should publish all essential information for monitoring mining projects, including:

- Concession agreements, including contracts, permits or licenses
- Laws and regulations
- Project-specific assessments and reports, including EIAs, EMPs, work programs, social impact assessments and local development plans
- Ongoing data on implementation and monitoring, including production figures, tax and royalty payments, and inspection reports

Transparency is always a matter of degree. Peru—which some have lauded for its high level of transparency—does not disclose company-disaggregated data on revenues. In contrast, in the DRC, with its uneven record of disclosure, it is possible to get daily data on exports, disaggregated by company, but it is not possible to obtain EIAs.

The 2010 Revenue Watch Index measures and compares the information that governments disclose about their oil, gas and mining industries, including payments to governments, contracts, regulations and related data. The index covers 41 resource-rich countries and demonstrates which types of information are available in each country.³⁴

Even in the worst of situations, much is still available. Information from laws and regulations, EITI, stock exchange disclosures, company and industry reporting efforts, and government reporting can all assist monitoring efforts, and civil society groups must seek to use the information that is currently available to them—while continuing to push for more transparency when it is lacking. Appendix 3 provides possible sources of information about extractive industry projects.

³³ For example, Indonesia's Regional Autonomy Law has conflicting provisions spelling out which governments are responsible for environmental monitoring. Yuko Kurauchi et al., *Decentralization of Natural Resources Management: Lessons from Southeast Asia*, World Resources Institute, 2006, 9, <http://pdf.wri.org/repisynthesis.pdf>.

³⁴ The Revenue Watch Index is available at <http://www.revenuewatch.org/rwindex2010/index.html?q=rwindex>.

The first step in civil society monitoring is to identify the company's obligations and to determine which of those obligations to monitor. In a contractual regime, this requires access to contracts. Only with this access can civil society analyze the full range of a company's obligations and determine its compliance.

Transparency of Terms and Obligations from Contracts, Permits and Laws

The first step in civil society monitoring is to identify the company's obligations and to determine which of those obligations to monitor. In a contractual regime, this requires access to the contracts: citizens will need to see the individual mining contracts to be able to understand the full range of commitments the company has made in terms of taxes, royalties, social infrastructure, the environment and so on. However, mining contracts remain private in many countries. Revenue Watch's *Contracts Confidential* provides a full analysis of the status and importance of contract transparency.³⁵ Only when civil society has access to the contracts themselves can they analyze the full range of companies' obligations. And only once they understand those obligations can they determine whether or not the companies are complying.

While contract transparency is certainly important, it is neither strictly necessary nor entirely determinative for monitoring efforts. As discussed in the introduction to this report, even countries that rely heavily on contracts define some company obligations in laws and regulations, and those obligations should be publicly available. While civil society may be unable to identify and monitor a company's full set of obligations, they are still able to conduct meaningful, if incomplete, monitoring based on those obligations that are known. Furthermore, not all countries rely equally on contracts. Some manage the mining industry primarily through a legal framework established in laws and regulations, which are publicly available. In those countries, civil society will need to analyze the applicable laws and regulations in order to understand the commitments a company makes when it takes on a mining project.

Finally, mining contracts and terms have been made public in some countries. In those cases, there is a need to focus on analyzing the agreements to understand the commitments the companies have made and on monitoring companies' operations to determine whether those commitments are being fulfilled. If terms are not yet published, there is a need to continue to push for these to be placed in the public domain.

Transparency of Social and Environmental Documents

If understanding a company's obligations is the first step in beginning to monitor the implementation of a mining project, the next step is determining whether those obligations are being met during the company's ongoing operations. And that requires ongoing transparency from companies and governments.

For example, many countries require companies to submit social and environmental impact assessments. In some cases, they may also be required to submit specific plans committing to managing their operations in a particular way to protect the environment, or committing to certain employment targets, training programs or social infrastructure projects. When such assessments and plans are required, the companies also typically are responsible for reporting periodically on their progress. If government and civil society cannot access these documents, they will be unable to identify the commitments the companies have made and to determine whether they are fulfilling those commitments. Of the 41 countries covered in the 2010 Revenue Watch Index, only 15 published reports with assessments of the expected environmental and/or social impact of oil, gas and mining projects.³⁶

South Africa's Mineral and Petroleum Resources and Development Act (MPRDA) requires companies to submit an SLP as part of their application for a mining right and to report annually to the DMR on their progress against the SLP.³⁷ These SLPs define many of the companies' social obligations, including infrastructure and poverty eradication programs, and the annual reports provide information on whether and how those obligations are being fulfilled. However, these plans and

35 Peter Rosenblum and Susan Maples, *Contracts Confidential*, Revenue Watch Institute, 2009, <http://www.revenuewatch.org/files/RWI-Contracts-Confidential.pdf>.

36 Revenue Watch Institute, *Revenue Watch Index*, 2010, appendix 2, sec. 1, question 4, <http://www.revenuewatch.org/rwindex2010/pdf/app2.pdf>. Twenty-five countries do not publish such reports, and the question was not applicable for one country.

37 South Africa, Mineral and Petroleum Resources Development Act, 2002 (Act No. 28 of 2002): Mineral and Petroleum Development Regulations, 2004, art. 42.

their annual reporting instruments present a major problem for civil society monitoring efforts: they are confidential.³⁸ The companies submit their SLPs and annual reports to the DMR, and the DMR reports that it may not release these documents publicly and that they should remain private between the submitting company and the DMR. The companies also fail to release this information publicly. Our research indicates that companies generally fail to provide any specific information on SLPs.³⁹ As of May 2011, AngloGold Ashanti was the only exception, providing a series of annual SLP reports on its website for its Vaal River and West Wits mines.⁴⁰ The rest provide, at most, very general information about social and labor efforts, but no description of any specific commitments they made in the SLPs themselves.

The same is true of EMPs in South Africa. As Tracy Lynn-Humby, a specialist in environmental law at Wits University in South Africa, explains, the EMP is

absolutely key to articulating the mining companies' environmental obligations, the beneficiaries of which are both the communities who live adjacent to the mine and those who live further afield and who are impacted by mining's detrimental effects on environmental services. Although these documents are available well before the company is granted a mining authorization, they are almost never made available to anyone outside the DMR. The public participation process is often a sham, for example when interested and affected parties are given one-page questionnaires with a few questions focusing on how they 'feel' about the proposed operation.⁴¹

This lack of information and participation makes associated monitoring efforts extremely difficult, if not impossible. It seems bizarre that these plans should remain hidden from the intended direct beneficiaries: workers and communities. If these stakeholders cannot know what commitments were made on their behalf, they have no way to determine whether those commitments are being fulfilled in practice.

Transparency Challenges in Decentralized Government Structures

The licensing process at the district level often presents serious challenges, because licenses are issued with little to no transparency or accountability mechanisms in place. Indonesia's central government estimates that district governments have granted around 10,500 licenses for small-scale mining. These licenses are not tracked in any central cadastre system, and even the central government is facing serious difficulties in monitoring these deals. Although the individual deals are small, their combined impact on revenues is significant, as are their potential harms.

Another challenge arises when local government institutions are charged with overseeing large-scale mining projects: they may be unable to access the information they need to fulfill their oversight role effectively. An example from the Philippines demonstrates this challenge. The Aquino government of the late 1980s and 1990s instituted a wide range of decentralization reforms, most notably the 1987 Philippine Constitution that set out four levels of local government: provinces, cities, municipalities and *barangays* (equivalent to urban neighborhoods and rural villages).⁴² The Constitution further provided that "[l]ocal governments shall be entitled to an equitable share in the proceeds of the utilization and development of the national wealth within their respective

38 Despite this lack of transparency, there appears to be confusion among some international actors as to whether the SLPs are public or not. Our independent research found specific SLP information for only one company, AngloGold Ashanti. Meanwhile, government, company and civil society actors in South Africa all confirmed that these reports are typically not shared publicly. Nonetheless, the World Economic Forum's report stated that "social and labour plans, including the community development strategy are all publicly available." World Economic Forum, 30.

39 We searched corporate websites, company reports and Internet search engines for the 10 largest mining companies listed on the Johannesburg Stock Exchange. We researched the following companies, by sector: iron and steel (Kumba); coal (Exxaro Resources Ltd.); general mining (BHP Billiton, Anglo American Corp., African Rainbow Minerals Ltd.); gold (AngloGold Ashanti Ltd., Gold Fields Ltd., Harmony Gold Mining Co. Ltd.); platinum and precious metals (Anglo American Platinum Corp. Ltd., Impala Platinum Ltd.).

40 AngloGold Ashanti, "Mining Charter for the South African Mining and Minerals Industry," <http://www.anglogold.co.za/Sustainability/Other+public+reports/Mining+Charter.htm>.

41 Tracy-Lynn Humby, Aug. 2, 2011, personal email.

42 Philippines, Constitution, 1987, art. X, sec. 1.

areas, in the manner provided by law, including sharing the same with the inhabitants by way of direct benefits.”⁴³

Four years later, the government adopted the Local Government Code (LGC), which further specified the powers devolved to the local governments regarding resource wealth. The LGC specified that the local governments would receive 40 percent of all mining taxes and royalties collected by the central government for concessions in those localities, to be divided among the four subnational units. The LGC also required national government agencies to consult with the relevant local government units before any mining project could commence.⁴⁴

The LGC provisions have allowed several localities to deny consent to large mining projects or to enact decades-long moratoriums on any new large-scale mining activity within the local area. Representatives of the national mining ministry lamented local government moratoriums on mining development as “contrary to national policy” and a “lost opportunity,” since the central government has a strong economic development interest in allowing the projects to proceed. The national government’s attempt to overturn the moratoriums via administrative order has been met with extended litigation and controversy.⁴⁵

A lack of transparency may be partly to blame for the local governments’ resistance to mining. At least one case study indicates that they may not be able to access the results of environmental impact statements, which remain confidential between the national government and the mining company.⁴⁶ Without access to those statements, the local governments reasonably conclude that they will be unable to understand the likely environmental effects of the mine or to carry out their statutory duty to monitor under the LGC.

Transparency Is Necessary But Not Sufficient

While transparency is crucial to both government and civil society monitoring efforts, it alone is not sufficient. The relevant actors must have the capacity to use the information they can access and the proper incentive or desire to conduct effective monitoring. As more information becomes available because of the success of the transparency movement and as more mining projects come online after years of development, it is not surprising that the capacity and sophistication to

deal with this data may take time to catch up. The concern is that there are already situations in which information is available but is not being used. Recent experience in Zambia highlights this point.

Through the Copperbelt Environmental Project, the Environmental Council of Zambia (ECZ) has been working to improve transparency around its EIA process. EIAs are required in Zambia for new mining projects, and the ECZ posts new EIAs to its website for

public comment. This public comment period provides an important opportunity for communities and civil society groups interested in the environmental impacts of mining to voice their concerns and to have a say in the approval of new projects. To facilitate public comment, the ECZ is required to provide copies of an EIA statement to “local government units, parastatals, non-governmental and community-based organisations, and interested and affected parties,” to place copies in public buildings near the proposed site, and to place notifications in newspapers detailing where the documents are available and how citizens can submit public comments.⁴⁷

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43 Philippines, Constitution, art. X, sec. 7.

44 Philippines, Local Government Code, 1991, secs. 2(c), 26-27 and 290, <http://www.pcij.org/blog/wp-docs/LGC1991.pdf>.

45 William N. Holden and R. Daniel Jacobson, “Mining Amid Decentralization: Local Governments and Mining in the Philippines,” *Natural Resources Forum* 188 (2006): 192-93.

46 Holden and Jacobson, 194 (“However, the Philippine environmental impact assessment process views all environmental impact statements submitted by the mining project proponent to the Government as confidential; disclosure of such information rests on the discretion of the national Government.”).

47 Zambia, Environmental Protection and Pollution Control (Environmental Impact Assessment) Regulations, 1997, art. 16(1), <http://www.necz.org.zm/cap204/Regulations/eia.html>.

However, an employee in the ECZ reports that the council rarely receives public comments on EIAs for mining projects. Although communities may have concerns about the project, they often do not take notice until it is already under way, by which time the EIA has already been approved. Even in situations when information is available, citizens can do more to use all the information at their disposal to have a meaningful impact on making decisions and enforcing laws and contracts.

2.3 Incentives

Incentives explain why many government monitoring and enforcement efforts fall short. The interests of those in positions of influence and authority often do not align with the effective fulfillment of these functions. This is true for several reasons:

- *The political value of discretion:* Strong systems by definition curtail the discretion of individuals. In resource-rich countries, especially poorer ones, control over the resource sector is one of the most politically valuable assets available. Leaders hesitate to relinquish this discretionary control to process or to bureaucrats in case they need to be able to manipulate its operations in the future. This is particularly true in environments that feature high levels of political competition or factionalism. Just as giving out money is a form of patronage and buying influence, so is lax enforcement of contractual or legal obligations.
- *Time horizons:* The benefits of robust monitoring and enforcement activities are realized only over time, although they require significant devotion of resources in the present and the future. However, most top officials will be in office for only a finite period of time, and they must face the political realities of regular election cycles. Politicians tend to favor resource allocations that improve near-term political and economic standing over those that generate benefits only in the future.
- *Institutional conflicts of interest:* Mining ministries are often charged with both promoting new investment and regulating ongoing investment, which creates conflicts of interest. First, in terms of enforcement, enforcing laws and provisions against companies can be seen as competing with the goal of promoting investment in the mining sector. Second, with regard to monitoring, some laws and contracts commit government ministries to respond to company applications or reports, such as new mining applications, environmental assessments or proposed work programs, within a short period of time in order to reduce delays and promote investment. Both companies and ministry officials hold ministry workers closely to those deadlines. But while those same workers are often responsible for monitoring ongoing company operations, they receive no similar pressure to monitor companies over time. State-owned oil and mining companies may also present conflicts of interest, particularly when the national company is both an operator and a regulator.⁴⁸
- *Personal conflicts of interest:* Some public officials have private interests in the mining sector and favor companies that are controlled by themselves, their friends and family, or their political allies. Monitoring the costs of subcontracts, for example, can be undermined if the official has an interest in a certain subcontractor receiving a valuable (and possibly inflated) contract. Another personal conflict of interest can arise when mid-rank officials create a bottleneck through a reporting or approval process, establish themselves as the gatekeeper, and collect a “rent” from companies to pass through it. Local content compliance is one example: Companies have to get sign-off, and they must pay or otherwise reward the gatekeeper to get it. The incentive for the gatekeeper becomes capturing the rent rather than enforcing the rules.

Levels of capacity and transparency, discussed in the previous sections, are symptoms of the prevailing incentive environment. Even in very poor countries, capacity can be built if the political

48 However, a recent report finds that separating commercial and regulatory functions is not necessarily a prerequisite to success. See Mark C. Thurber, David R. Hults and Patrick R.P. Heller, “Exporting the ‘Norwegian Model’: The Effect of Administrative Design on Oil Sector Performance,” *Energy Policy* 39 (2011): 5366-78.

leadership values that particular function. Angola’s national oil company, Sonangol, is one example. Developing a functioning oil sector and effectively collecting petroleum taxes served the interests of the country’s political elite, and Sonangol became “an island of competence thriving in tandem with the implosion of most other Angolan state institutions.”⁴⁹ Although many international donor and other assessments frame governance problems as a “lack of capacity,” capacity development remains a choice. And someone in power is making that choice.

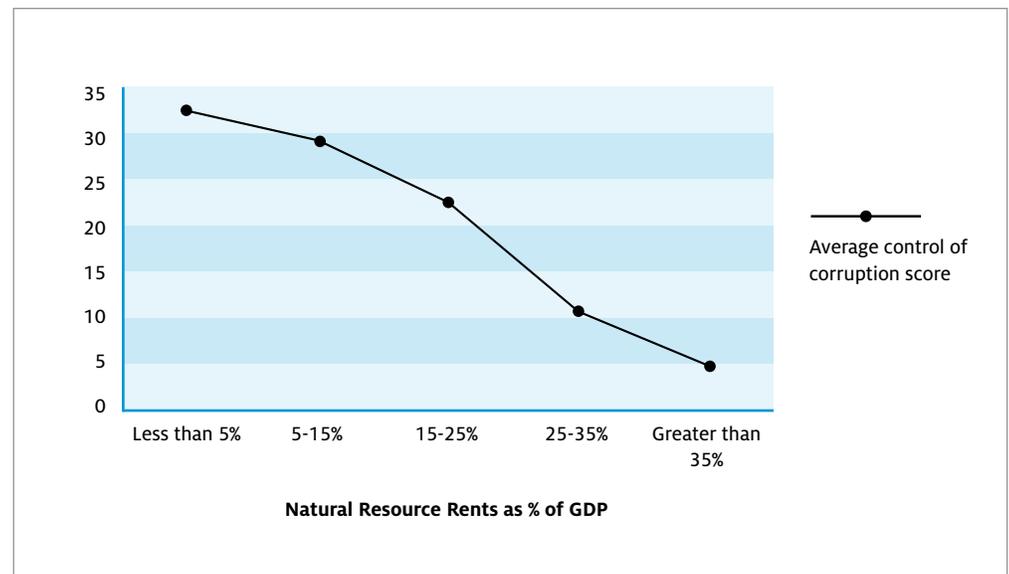
Corruption

Corruption is a common manifestation of these incentive problems. It can take several forms from the solicitation of a bribe by an inspector to the uneven tax collection that favors political allies. Although corruption risks are highest when mining rights are being awarded (an issue not covered in this report), there are still risks during the implementation of a deal. For example, bribery may “occur in attempts to weaken monitoring efforts, or to avoid sanctions if detected and prosecuted.”⁵⁰

Corruption challenges can be particularly acute in resource-rich countries. Figure 4 shows a correlation between corruption and natural resources in low- and lower middle-income countries. The World Bank Governance Indicators rank countries along a scale of control of corruption, with each country receiving a percentile rank. The higher the country’s percentile rank, the better the country’s control of corruption. Countries with a higher percentage of GDP from natural resource rents tend to have lower scores.⁵¹

figure 4:

Natural Resource Rents and Control of Corruption in Low- and Lower Middle-Income Countries



Sources: World Bank, Governance Indicators: Control of Corruption, 2009, <http://info.worldbank.org/governance/wgi/resources.htm>; World Bank, Country and Lending Groups: Income Groups, 2011, <http://data.worldbank.org/about/country-classifications/country-and-lending-groups>; World Bank, Indicators: Total natural resources rents (% of GDP), 2009, <http://data.worldbank.org/indicator/NY.GDP.TOTL.RT.ZS>.

49 Ricardo Soares de Oliveira, “Business Success, Angola-Style: Postcolonial Politics and the Rise and Rise of Sonangol,” *Journal of Modern African Studies* 45 (2007): 595.
 50 Farouk Al-Kasim, Tina Søreide and Aled Williams, *Grand Corruption in the Regulation of Oil*, U4 Anticorruption Resource Centre, 2008, 23, <http://www.cmi.no/publications/file/3034-grand-corruption-in-the-regulation-of-oil.pdf>.
 51 “Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as ‘capture’ of the state by elites and private interests.” World Bank, Governance Indicators: Control of Corruption, 2009, <http://info.worldbank.org/governance/wgi/pdf/cc.pdf>.

In addition to corruption, our research has identified some specific incentive problems that are particularly relevant to mining regulation and oversight: tensions between approving new mining rights versus monitoring existing rights and revenue collection by agencies other than the tax agency.

Tensions between Approvals and Monitoring

Many government employees have multiple responsibilities, some of which may conflict with each other—particularly when it comes to determining how employees should allocate their time. Ministry staffs tend to be stretched thin due to capacity constraints, and they may be forced to prioritize their responsibilities. This can become a problem for monitoring efforts when the same staffers are responsible for approving new mining permit applications and for monitoring ongoing mining operations. Such a situation creates an institutional conflict of interest in that many government agencies favor getting new mining projects off the ground over effectively monitoring existing ongoing projects. The agencies typically have defined time frames in which they must approve applications for new permits, often defined in laws or regulations. Government supervisors and industry hold staff accountable to those time frames. In fact, a government's relative attractiveness to investors is measured partially by how long it takes to have a new permit or application accepted.

However, no one is holding those same government employees accountable for conducting ongoing monitoring. No such similar time frames or targets exist on the monitoring side. As a result, staffers with responsibility for both functions tend to spend more time approving new mining applications and less time monitoring existing operations.

For example, South Africa's MPRDA requires the DMR to accept or reject applications for prospecting rights within 14 days. This means someone in the department must review the application to determine whether the requested land is available for prospecting and whether the applicant has provided adequate financial assurance for the work. DMR staff had reportedly been spending so much time reviewing applications for new prospecting permits that they did not have enough time to monitor whether existing permit holders were fulfilling their ongoing obligations. The DMR had fallen so behind in its monitoring that the minister called for a moratorium on applications for new prospecting rights and a massive audit of the country's prospecting operations, as discussed in Box 11 (p. 61). As a result of the audit, the DMR plans to make some changes to its internal processes, including providing separate dedicated staff to monitor ongoing operations to eliminate the conflicting incentives.

The DMR faces the same challenge in its review of EMPRs. A study found that environmental staff in one region spent 18 percent of their time monitoring compliance and 82 percent of their time evaluating EMPRs. Although this time allocation allowed the staff to keep up with their mandate in terms of EMPR evaluation, it was at the expense of ongoing compliance monitoring. As the office lost staff members, the time allocation shifted even more dramatically: only one staff member remained, and she spent all of her time evaluating EMPRs and none on inspections.⁵²

Similarly, government officials in Canada reported that they are held accountable for application turnaround times but not to ongoing monitoring requirements. Whether an agency has approved a permit within the required turnaround time is easy to measure, and the benefits are immediately apparent: an investor is able to begin operations quickly. Monitoring's benefits, on the other hand, are more difficult to measure.

The juxtaposition of pressure to approve new mining rights versus the lack of pressure to monitor ongoing mining operations also highlights another tension for some government mining institutions: simultaneously promoting and regulating the industry. When the same government entity that promotes mining investment is also charged with enforcing the country's laws and regulations against companies, there can be a conflict of interest. The ministry is establishing relationships with companies and is working hard to incentivize companies to invest in the country. But it is also auditing the companies' operations and may be assessing fines or even canceling

52 Watkins, 61-62.

permits. Although these functions are not necessarily in direct conflict, the different nature of them can lead to some serious challenges and questions in the way the ministry should be run and the relationships ministry staff work to develop with mining companies, which are simultaneously clients and regulated entities.

Revenue Collection by Agencies Other than the Tax Agency

Some countries have allowed agencies that manage the mining industry to collect certain mineral fees to support those agencies' budgets. These arrangements provide financial support for agencies that are otherwise underfunded through the state budget. However, while they look good on paper, they can raise some challenges that policymakers should look out for.

For example, in Sierra Leone, an agency was responsible for overseeing mining companies' compliance with their exploration obligations. To support these monitoring efforts, the agency collected annual surface rent fees. While some form of financial support was essential to ensure that the agency could complete its work, the arrangement created a perverse incentive: the agency needed to collect the surface rents in order to operate, so it had an incentive not to withdraw exploration rights, even when companies were not conducting their required exploration activities. The agency would let companies maintain their rights as long as they paid their surface rents on time, even if the companies conducted little or no exploration activity. This situation created long-term risks for the country (insufficient exploration of its natural resources, which could lead to insufficient mining development, and ultimately fewer taxes collected) for the sake of collecting much smaller surface rent fees.

This story imparts a useful lesson for policymakers in other countries: when a monitoring agency is required to collect some tax or fee to support its functioning, policymakers should ensure that the agency's enforcement and sanctioning responsibilities do not conflict with its ability to collect those taxes or fees. A better practice is for the country's tax administration to collect mineral taxes instead of the agency that provides and withdraws licenses, due to the further conflicts of interest that can arise when the same agency that controls access to concessions also controls some form of revenue collection. Even more problematic are instances when the state company is responsible for collecting resource rents—and when it may also be an operating partner of private companies.