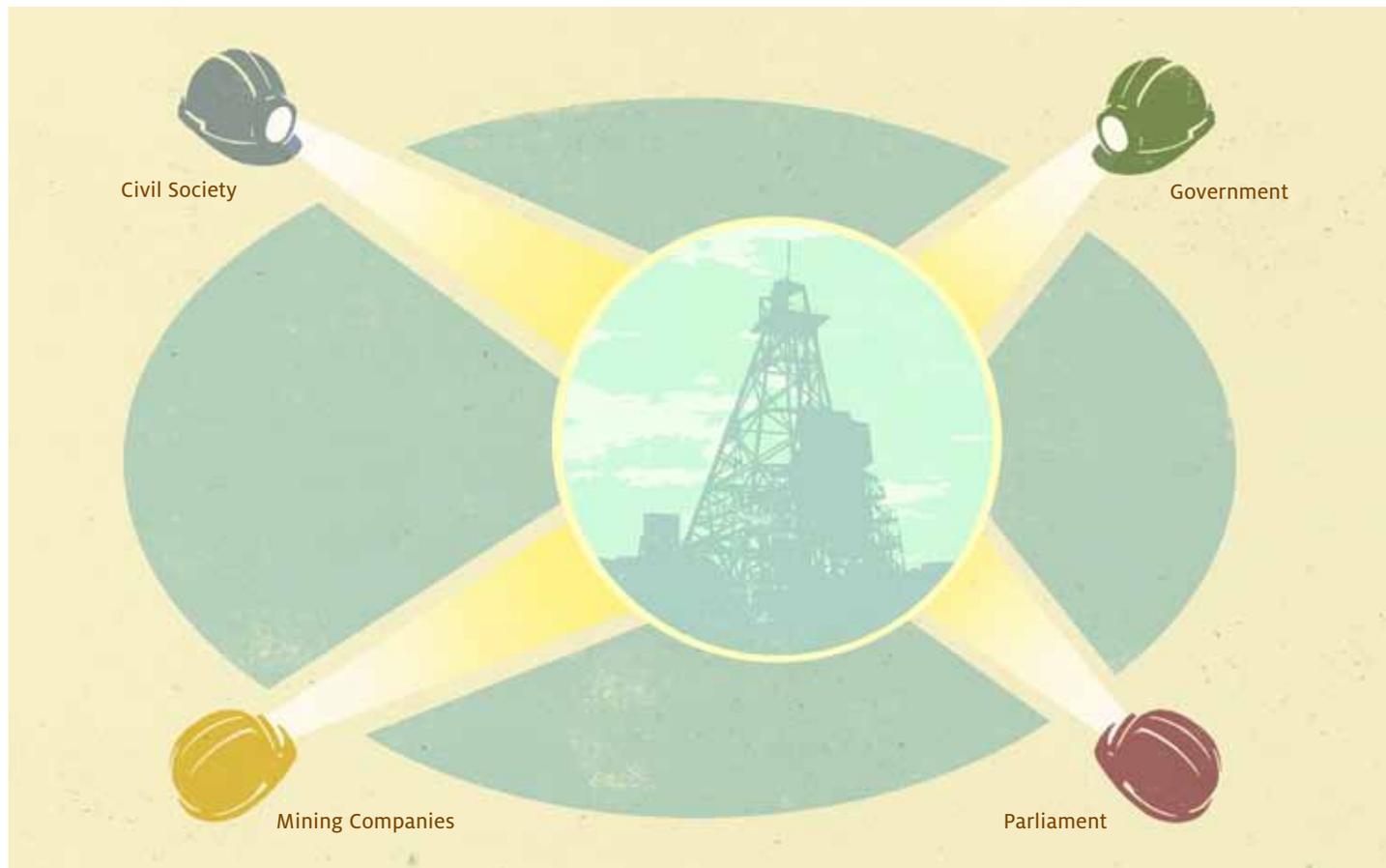


GOVERNMENT AND CITIZEN OVERSIGHT OF MINING

# Enforcing the Rules

By Erin Smith  
with Peter Rosenblum



#### **REVENUE WATCH INSTITUTE**

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Revenue Watch Institute

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2011

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## LIST OF ABBREVIATIONS

ASRC	Azerbaijan Social Review Commission
BP	British Petroleum
CAO	Compliance Advisor/Ombudsman
CFPOA	Corruption of Foreign Public Officials Act (Canada)
CSR	corporate social responsibility
DENR	Department of Environment and Natural Resources (Philippines)
DMR	Department of Mineral Resources (South Africa)
DRC	Democratic Republic of Congo
DTA	double taxation agreement
ECZ	Environmental Council of Zambia
EIA	environmental impact assessment
EITI	Extractive Industries Transparency Initiative
EMP	environmental management plan
EMPR	Environmental Management Programme Report (South Africa)
EPA	Environmental Protection Agency (United States)
FCPA	Foreign Corrupt Practices Act (United States)
FIDH	International Federation for Human Rights
FPIC	free, prior and informed consent
HDSA	historically disadvantaged South African
HRW	Human Rights Watch
IBA	impact and benefit agreement (Canada)
ICMM	International Council on Mining and Metals
IFC	International Finance Corporation
ILO	International Labour Organization
IMF	International Monetary Fund
IWA	Integrity Watch Afghanistan
JV	joint venture
LGC	Local Government Code (Philippines)
LTU	large taxpayer unit
MCM	Mopani Copper Mines (Zambia)
MDA	mineral development agreement
MPRDA	Mineral and Petroleum Resources Development Act (South Africa)
NCP	National Contact Point (in relation to the OECD's Guidelines for Multinational Enterprises)
NGO	nongovernmental organization
OECD	Organisation for Economic Co-operation and Development
OEFA	Organismo de Evaluación y Fiscalización Ambiental (Peru)
OSINERGMIN	Organismo Supervisor de la Inversión en Energía y Minería (Peru)
SAI	supreme audit institution
SARA	semiautonomous revenue agency
SLP	Social and Labour Plan (South Africa)
TIEA	tax information exchange agreement
TIKA	Turkish International Cooperation and Development Agency
TSX	Toronto Stock Exchange
VAT	value-added tax
VPs	Voluntary Principles on Security and Human Rights
ZRA	Zambian Revenue Authority

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## EXECUTIVE SUMMARY

In recent history, mining has failed to deliver many of the benefits citizens expect, particularly in poorer nations rich in natural resources and high in hopes. Many of the reasons remain unclear. In some cases, the problem is linked to bad deals with mining companies. But no matter the quality of the deal, other problems arise from failure to effectively monitor and enforce the existing obligations. This report examines the monitoring of mining obligations, characterizes the main gaps, identifies policy options and good practices, and proposes practical ways for both government and civil society to improve monitoring and enforcement.

Monitoring is the process through which government and civil society track compliance. It is the only means of determining if the deals struck with companies are the same deals implemented on the ground. But while mining has boomed over the past decade, monitoring and enforcement have not kept pace.<sup>1</sup> This monitoring gap is especially acute in developing countries. Emerging states with weak regulatory systems—many of which are undergoing major transitions from war, repressive rule or single-party states—face a series of dramatic changes. Many have adopted new mining laws, implemented new fiscal regimes and privatized state enterprises while also entering into billion-dollar deals.

Companies and governments are facing—and increasingly responding to—growing pressures to become more transparent and participatory, while civil society organizations are striving to scrutinize deals and respond to threatened harms. Although the surge in mining deals and the pressure for better implementation have yielded important results, including more publicly available information, capacity-building efforts and scrutiny of individual deals, they have also placed tremendous burdens on government, companies and civil society.

It is impossible to measure the full extent of losses from failure to monitor and enforce mining obligations, but the evidence that does exist speaks for itself. In royalties and taxes alone, billions of dollars are regularly lost to tax evasion or fraud. A parliamentary investigation in the Democratic Republic of Congo (DRC) identified \$450 million in lost revenue for 2008.<sup>2</sup> An anticorruption official in India reported \$400 million was lost in the iron-rich state of Karnataka during 2009-10.<sup>3</sup> This is just a fraction of the \$160 billion per year that Christian Aid estimates is lost in tax revenue to developing states each year.<sup>4</sup> And revenues are only one part of the story. Monitoring is also necessary to prevent potential harms to workers, the environment and the social peace fundamental to a sustainable mining industry.

Problems with official government oversight exist in every country with a substantial mining sector, including the United States, Australia, South Africa and Canada. One of the most striking findings of this report—based on a broad study with field research in Canada, Peru, South Africa, Zambia and the DRC—is that some countries are far worse off than others. While no country has

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1 Iron ore production has doubled in less than a decade; copper and aluminum are not far behind. Thomas D. Kelly and Grecia R. Matos, "Historical Statistics for Mineral and Material Commodities in the United States," U.S. Geological Survey, World Production, <http://minerals.usgs.gov/ds/2005/140/#data>.

2 Commission d'Enquête sur le Secteur Minier, *Rapport*, République Démocratique du Congo, Sénat, 2009.

3 "Ministers 'stole millions in Karnataka mining scam,'" BBC News, July 21, 2011, <http://www.bbc.co.uk/news/world-south-asia-14229386>.

4 Andrew Hogg et al., *Death and Taxes: The True Toll of Tax Dodging*, Christian Aid, 2008, 2, <http://www.christianaid.org.uk/images/deathandtaxes.pdf>.

mastered the challenges, the situation in many developing countries is far more urgent. Problems in Canada pale in comparison with the DRC or Zambia. Often, the problem is attributed to staffing or capacity, but there is an underlying problem of incentives. In the developed and developing world, political forces have often favored strong promotional mechanisms and weak oversight. Checks and balances may be written into the rules, but unrewarded in practice.

Civil society organizations have their own constraints. For them, the problem is less one of incentives than one of means and, in certain countries, personal risks. In some contexts, their freedom of speech may be curtailed, their capacity low, and their resourcing insecure. They will never replace government and industry, but they play an essential role as watchdogs.

Despite the challenges, good practices are emerging in a number of countries:

- **Clear rules and good administrative architecture** facilitate monitoring by reducing variables and separating promotion from enforcement.
- **Financial and regulatory independence** have been important to the creation of oversight and enforcement mechanisms in a number of countries.
- Many of the most effective approaches involve **partnerships** in which government agencies, industry and civil society work together to address monitoring needs and challenges.
- When monitoring efforts identify gaps in compliance, **government enforcement and civil society advocacy** mechanisms can work to correct these gaps and improve future compliance.

This report calls on governments, civil society and companies to devote increased and continuing attention to monitoring and enforcement programs. By taking advantage of the information generated by increased transparency and the industry's growing engagement in sustainability, they can help states and their populations get the most from their resources while also preventing the worst harms.

# 1. Introduction

This report is intended to help government and civil society actors understand the challenges and good practices associated with effective oversight and enforcement in the mining industry. To monitor, mining obligations must first be identified, but they are not always obvious.

**Part 1** addresses this issue and makes the distinction between contractual regimes and permit regimes. It will help readers situate themselves and their respective countries within a broader global context to learn how the mining industry operates in different countries and what is required to fully understand a company's legal obligations in these different settings.

**Part 2** identifies the obstacles to effective monitoring, in particular the lack of capacity and transparency and the issue of misaligned incentives.

**Part 3** presents areas of good practice to facilitate and enhance monitoring. While no single set of best practices exists to perfectly optimize monitoring efforts, the policy options presented can provide direction.

**Part 4** ends with recommendations for a variety of stakeholders who play a role in ensuring effective, sustainable management of the world's natural resources.

This report also includes three appendices to support civil society monitoring efforts. Appendix 1 is in this report, while Appendices 2 and 3 are available online at [www.revenuewatch.org/enforcingtherules](http://www.revenuewatch.org/enforcingtherules).

- **Appendix 1** presents a civil society monitoring toolkit. It covers five broad categories of company obligations (financial, social, environmental, occupational health and safety, and operational and production requirements) and presents sample obligations, possible sources of information for monitoring implementation, and questions civil society can ask to determine whether a company is fulfilling its obligations.
- **Appendix 2** provides background information on the five categories of company obligations in Appendix 1, including additional sample provisions for each obligation.
- **Appendix 3** identifies sources of information on the fulfillment of mining companies' obligations, including company and industry reports, government reporting, the Extractive Industries Transparency Initiative (EITI) and freedom of information laws. Although this is intended primarily for civil society, governments may also benefit from the sources.

## 1.1 Contextual Framework

Activity around mining companies' obligations can be roughly divided into the following three stages:

1. *Awarding concessions*: Governments grant concessions to mining or oil companies. This may occur through public auctions, a negotiation process or an application process. At the end of this stage, a company has gained the right to mine or to extract oil. This right can take the form of a license, permit or contract depending on the legal framework in the country (see Section 1.2). Government and civil society want to ensure that the terms of the deal are fair and that the overall investment is favorable to the country.
2. *Review and analysis of concessions granted*: Relevant actors within government and civil society seek access to the signed agreement (contract, license or permit) and the opportunity to analyze its terms. Because mining permits and contracts are not always released publicly, civil society will need to demand transparency in order to achieve this step.
3. *Monitoring and enforcement*: In this stage—the primary focus of this report—a company has launched its operations, and government and civil society monitor these operations to ensure that the company is complying with the terms of the concession agreement. The executive branch of government has primary responsibility for enforcing the terms of the deals, but civil society and other government entities will also monitor to hold both the company and the executive branch accountable.

## 1.2 What Must Be Monitored and Enforced?

Mining companies are subject to a range of obligations that can be grouped broadly into (i) fiscal terms (including taxes and royalties), (ii) operational commitments (e.g., work programs), (iii) environmental obligations, (iv) worker health and safety, and (v) social commitments. More information on these types of mining company obligations is provided in Appendix 2.

How and where these obligations are defined varies across countries, and sometimes within the same country. They may be based in law or contract. And with respect to contracts, the terms may be separately negotiated or based on a model contract with specified exceptions. The more variation there is in different companies' obligations, and the more varied the sources of those obligations, the more difficult it is to determine them with certainty and to monitor them effectively.

In a pure contractual regime, little is defined in generally applicable law, so the primary document governing the investment is a contract (sometimes referred to as a mineral development agreement or MDA) negotiated by the government and the investor. It is typically a long document defining the entire range of company obligations, including tax and royalty rates. It may also cover additional obligations relating to local content, social infrastructure, environmental protection, health and safety, and so on. Individually negotiated agreements of this kind are increasingly frowned upon because of the discretion and complexity they generate, but there are many that are still in effect or in negotiation.

Alternatively, in a pure permit regime, all of the major obligations applicable to mining operations are established through legislation and regulations. Rather than signing contracts with individual companies, the government establishes a system for companies to apply for permits or licenses to mine particular areas of land, and those permits or licenses are subject to generally applicable legislation regarding taxes, royalties, environmental requirements and so on. Companies' permits and licenses contain identical obligations.

In reality, however, no legal system relies purely on contracts or purely on laws to dictate the full range of company obligations. Instead, most countries operate somewhere on a continuum with varying degrees of reliance on individually negotiated project obligations and generally applicable obligations that apply equally across all companies. The DRC, South Africa and Peru help illustrate this continuum.

Problems with government oversight exist in every country with a large mining sector. While no country has mastered the challenges, the situation in many developing countries is far more urgent. If these nations take advantage of the information generated by increased transparency and the industry's growing engagement in sustainability, they will eventually get the most from their resources and prevent the worst harms.

The DRC is primarily a contractual regime, in which individually negotiated contracts define significant company obligations. The 2002 mining code was intended, in part, to bring uniformity to the mining sector. The code defines a general tax and royalty regime as well as significant environmental provisions that apply, in theory, to all companies. But it has had limited success, and there is no model contract under the code. In Katanga Province, the historical center of industrial mining, most mining projects are joint ventures (JVs) negotiated by the DRC's parastatal copper and cobalt company, Gécamines. The JV contracts define a range of obligations that go beyond the code and are particularly significant with respect to financing, governance and management. Companies also typically need to develop individual work programs that define many of their operational and production requirements. Some contracts entered into before 2002 remain in effect, further complicating the determination of obligations.

South Africa, on the other hand, operates a permit regime in which the word "contract" almost never appears.<sup>5</sup> Companies apply for mining rights, subject to generally applicable laws and regulations. But there are significant obligations that are subject to individual negotiation. Each company must develop and submit a project-specific Social and Labour Plan (SLP), an environmental management plan (EMP) and a work program. The company and the government must agree on the particular social, environmental and operational concerns of that project and on how the company should address them. The structure and format of the documents are defined in law, and their general contents are thus standardized across projects. Their specific contents, however, vary depending on the project's particular impacts and needs, and, as noted below, they remain largely unavailable to the public or direct stakeholders.

Peru operates across the middle of this continuum. It has generally applicable mining legislation, and companies are required to apply for mining permits, the terms of which comport with the country's legislative framework. On its face, this arrangement looks much like a pure permit regime (although the law actually refers to a "contract" as part of the licensing process); but Peru's mining sector has two unique arrangements that more closely resemble contractual regimes. The first is a stabilization contract. Once a company has a mining permit, it can apply for this type of contract, which freezes the company's tax and royalty structure so the company is not required to comply with tax or royalty increases passed after the contract takes effect. The stabilization contracts themselves do not vary greatly, but they create a situation in which the legal framework applicable to a particular contract depends on whether the company has a stabilization contract and, if so, when it came into effect. Second, some mining projects are still subject to negotiated contracts rather than the country's permit regime. When the country's mines were privatized, some that had been publicly managed were granted through a contracting process.

One of the lessons from this continuum is that focusing too heavily on the contract artificially limits monitoring efforts in contractual regimes, while looking only to laws and regulations in permit regimes leaves out important company obligations that should be examined. In fact, many significant obligations may not be found in the law or in a contract. Those include, in some cases, EMPs, work programs, social impact assessments, local development plans and other project-specific commitments. There are challenges to identifying the most significant obligations in every jurisdiction, though regimes that depend on individually negotiated contracts have historically posed the most significant problems. There, the variations among companies are further complicated by a history of secrecy that is only beginning to break down.

Nevertheless, while varying among countries, increased transparency, legal reform and the disclosure obligations of listed companies have created circumstances in which it is increasingly possible to identify the obligations of companies and to monitor them. This is discussed in more detail later in this report, including the issue of proliferation of legal frameworks in Section 2.1 and the issue of contract transparency in Section 2.2.

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<sup>5</sup> South Africa moved to a mining permit regime fairly recently as part of its post-apartheid reform efforts. The current regime is defined in the Mineral and Petroleum Resources Development Act of 2002.

## 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."<sup>6</sup> 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."<sup>7</sup>

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.

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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](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**

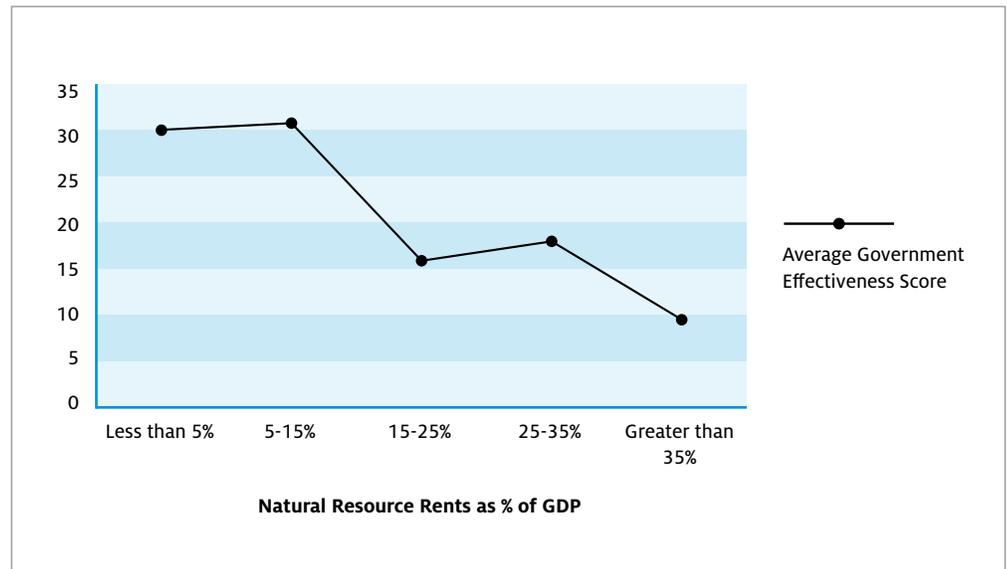
In 2010, the United States experienced a catastrophic oil spill when Transocean’s Deepwater Horizon offshore oil rig exploded in the Gulf of Mexico. The initial explosion killed 11 people. Over the course of the next several weeks, five million barrels of oil spread throughout the gulf, devastating the 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.<sup>8</sup>

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.<sup>9</sup> 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 Countries<sup>10</sup>**



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.<sup>11</sup>

#### 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.<sup>12</sup> 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](http://www.auditor.on.ca/en/reports_en/en05/309en05.pdf).

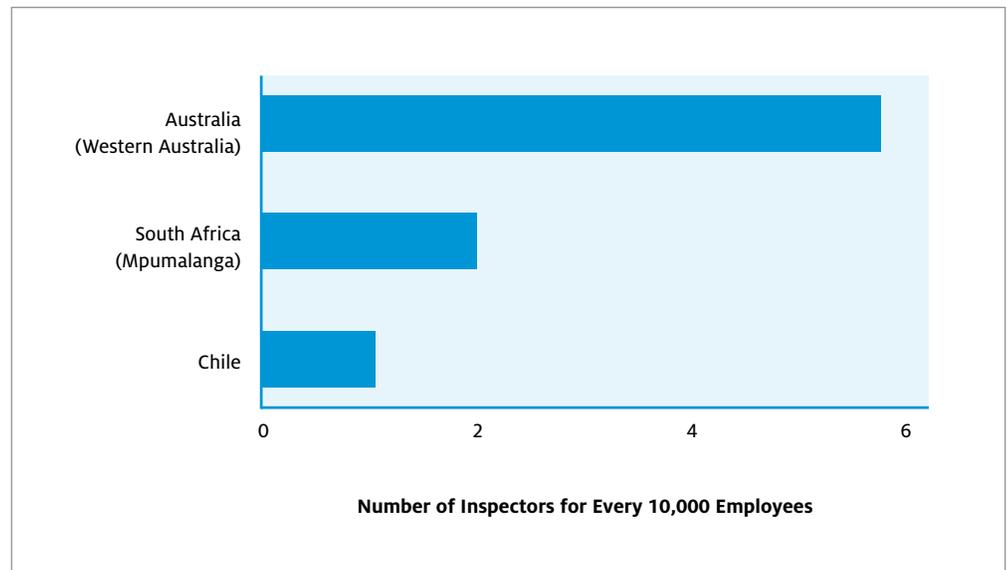
12 Gideon Long, “How safe are Chile’s copper mines?” *BBC News*, Oct. 8, 2010, <http://www.bbc.co.uk/news/world-latin-america-11467279>.

Geology and Mines Bureau failed to conduct proper inspections of the mine before it collapsed.<sup>13</sup> 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.”<sup>14</sup> 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>.

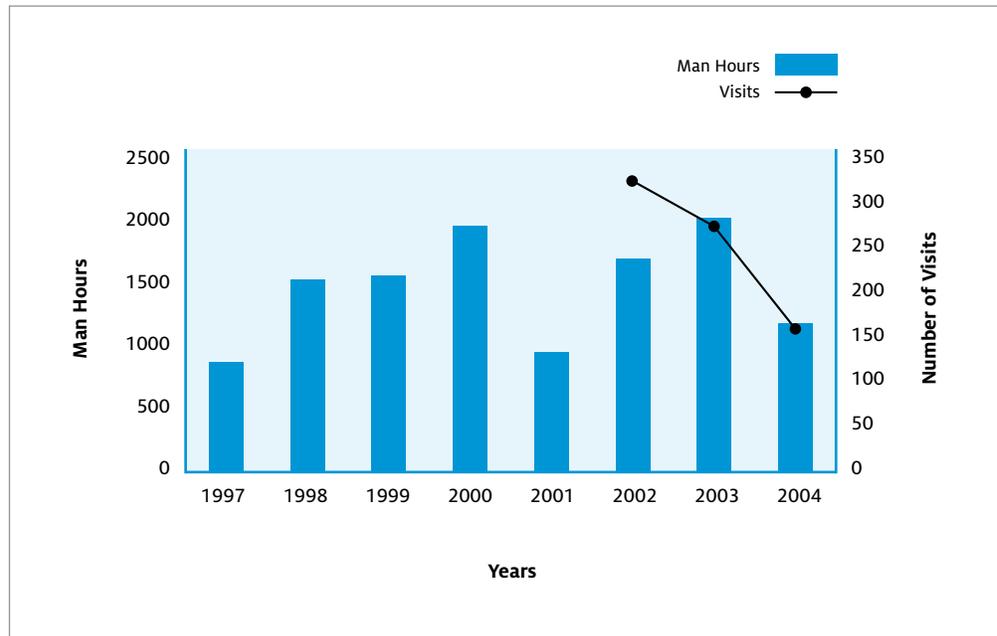
14 Commissioner Stephen J. Kenner, *Review of the Mines Safety and Inspection Act 1994*, Western Australia Industrial Relations Committee, 2009, 82, [http://www.dmp.wa.gov.au/documents/Reports/MI\\_Act\\_KennerReport.pdf](http://www.dmp.wa.gov.au/documents/Reports/MI_Act_KennerReport.pdf). In this jurisdiction, 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.<sup>15</sup>

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.”<sup>16</sup>

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

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

<sup>16</sup> 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](http://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 . . ." <sup>17</sup> 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.

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

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. <sup>18</sup> 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.<sup>19</sup> 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.<sup>20</sup> 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.<sup>21</sup> Typical of several Asian countries, Indonesia previously had a highly centralized oversight structure but has now decentralized many mining oversight functions.<sup>22</sup> 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.<sup>23</sup>

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](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](http://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.<sup>24</sup>

#### Box 4 | Decentralization in Indonesia

The concept of decentralization was introduced in Indonesia after the fall of the Soeharto regime in 1998.<sup>25</sup> 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.<sup>26</sup> 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.<sup>27</sup> 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.<sup>28</sup>

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.<sup>29</sup> 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.<sup>30</sup> 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.<sup>31</sup>

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.<sup>32</sup> 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](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](http://wdronline.worldbank.org/worldbank/a/c.html/world_development_report_1999_2000/chapter_5_decentralization_rethinking_government).

and oversight in particular substantive areas.<sup>33</sup> 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.<sup>34</sup>

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.

<sup>33</sup> 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>.

<sup>34</sup> 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.<sup>35</sup> 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.<sup>36</sup>

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.<sup>37</sup> 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.<sup>38</sup> 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.<sup>39</sup> 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.<sup>40</sup> 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.<sup>41</sup>

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).<sup>42</sup> 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

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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.”<sup>43</sup>

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.<sup>44</sup>

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.<sup>45</sup>

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.<sup>46</sup> 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.<sup>47</sup>

*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.*

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.<sup>48</sup>
- *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.”<sup>49</sup> 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.

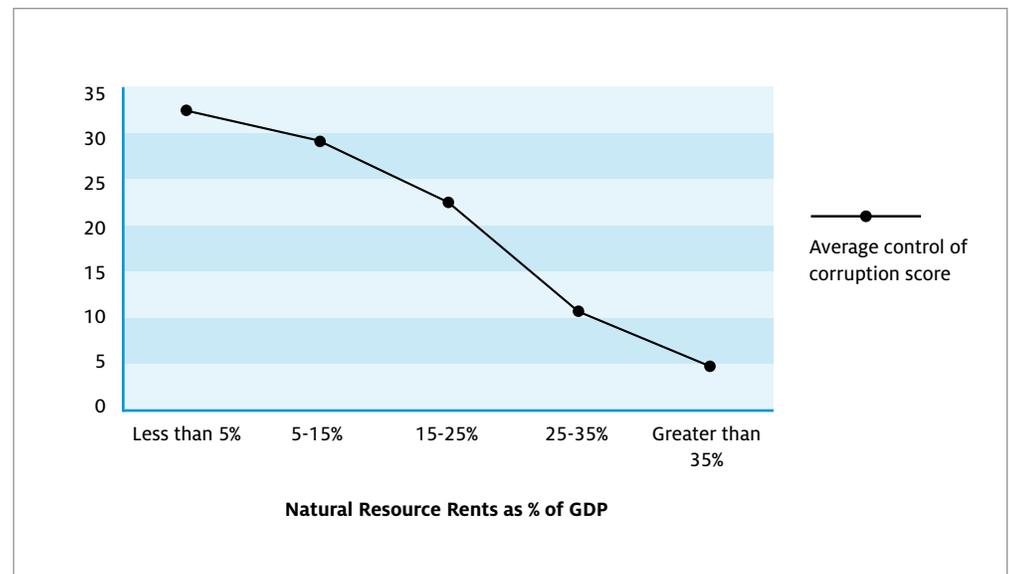
### Corruption

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.”<sup>50</sup>

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.<sup>51</sup>

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.<sup>52</sup>

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

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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.

### 3.

## Areas of Good Practice

Despite the many challenges associated with monitoring the mining industry, there are some strategies governments and civil society groups can use to help improve their efforts. This section presents policy options and areas of good practice that have been proposed or implemented in resource-rich countries throughout the world. Section 3.1 discusses how government agencies can structure their administrative architecture to achieve better monitoring. Section 3.2 discusses how legal frameworks—including laws, contracts and regulations—can be written to enable better monitoring throughout the life of the project. Section 3.3 discusses the role government oversight institutions can play in conducting their own monitoring of the extractive industries and in reviewing the executive branch’s monitoring. Sections 3.4 and 3.5 discuss the value and importance of various monitoring partnerships, both within and outside of government. Finally, Section 3.6 reviews a series of options for how governments and civil society can use the information obtained through monitoring efforts to support better company compliance in the future.

### 3.1 Administrative Architecture

Government agencies have the primary responsibility for monitoring companies’ operations to ensure they are fulfilling their obligations under the country’s laws, regulations and contracts. These institutions must be structured in a way that encourages and allows effective monitoring to take place. In response to capacity and incentive challenges, some new administrative structures have been proposed and implemented, such as providing dedicated monitoring staff that are not involved in fulfilling other ministry functions. In tax and revenue collection, several countries have experience implementing innovative new administrative structures, including the creation of specialized large taxpayer units and semiautonomous revenue authorities. These policy options and examples of how they have been implemented are discussed in the following sections.

#### Separating Monitoring and Enforcement from Other Ministry Activities to Avoid Conflicts of Interest

As noted above in Section 2.3, government staff often face conflicting priorities in pursuing their work, and monitoring activities may take a back seat to investment promotion activities, such as permit approvals. To combat this problem, distinct functional groups may be established so no overlap exists between staff responsible for approving new permit applications or reviewing mining plans and the staff responsible for monitoring ongoing mining operations and compliance with legal obligations. Providing separate staff helps ensure that monitoring will take place and that important monitoring resources will not be pulled away for other priorities. After a recent audit of prospecting operations in South Africa, DMR officials report that they plan to provide separate dedicated staff for compliance monitoring to reduce the problem of having individual staff members spending too little time on monitoring when their other responsibilities conflict.

## Box 5 | Change Management Challenges

Policymakers should note that making changes to administrative architecture might not always be entirely straightforward. Ministry leadership and staff may be resistant to change and may not want to share information or coordinate with other ministries. Furthermore, when changes are made, policymakers should make sure that the appropriate staff, information and resources are in place before transitioning monitoring responsibilities into new departments. Peru's experience with environmental monitoring highlights this point.

Peru transferred responsibility for environmental monitoring of the mining industry to a new government agency, the Organismo de Evaluación y Fiscalización Ambiental (OEFA), in June 2010. OEFA gained three responsibilities during this transition period: evaluation, supervision and oversight/control. In light of the close link between environmental harms and social conflict, OEFA's creation was widely celebrated. But its responsibilities were ill-defined, as was its authority vis-à-vis other government agencies. Furthermore, OEFA has not been given the resources to conduct meaningful environmental monitoring. Not only is OEFA underfunded, but also the Organismo Supervisor de la Inversión en Energía y Minería (OSINERGMIN)—the organization that previously managed environmental monitoring—reportedly refused to transfer staff or even case files to OEFA as part of the transition, at least partly because OSINERGMIN did not want to give up its staff to OEFA. Furthermore, although OSINERGMIN receives a percentage of what citizens pay for electricity, it also refused to transfer any of these funds to OEFA. So the results have been a disappointment. Despite hope for reform, for some the situation exacerbates a cynical perception that the government and mining sector will not tolerate serious encroachments on the industry's power.

## Devoting Specialized Resources to Large Taxpayers to Maximize Returns

Traditionally, many revenue agencies were organized by “type of tax,” meaning there were separate departments for each tax (e.g., corporate income tax, property tax, etc.), and the departments operated independently of each other. But recently there has been a trend, at least in developed countries, to organize the agency based on taxpayer segment.<sup>53</sup> As part of this move, some countries have created specialized large taxpayer units, or LTUs.<sup>54</sup> Many countries also specialize within their LTUs by industry, so that auditors can become familiar with the unique fiscal instruments and tax avoidance risks a particular industry presents.<sup>55</sup> Australia has an Energy and Resources Group for coal, gold, nickel, petroleum and gas companies; Ireland has a Mining & Energy Business Unit; and the United States has a department for Natural Resources and Construction.<sup>56</sup>

Creating specialized LTUs lets tax authorities devote special attention to some of the unique characteristics of large taxpayers, including:<sup>57</sup>

- *Revenue Concentration:* Large taxpayers can account for 30 to 70 percent of a country's fiscal revenues due to the large size of their operations and the multiple tax types they are required to pay.<sup>58</sup> As such they are an important source of revenue—and they also have a strong incentive to exploit tax loopholes wherever possible.
- *Complex businesses and tax arrangements:* Large taxpayers may have complex organizational structures, multinational transactions and complex financing arrangements.
- *Professional or dedicated tax advisors:* Because of the size of their businesses and their potential tax obligations, many large taxpayers employ professional tax advisors, while

53 Forum on Tax Administration, *Tax Administration in OECD and Selected Non-OECD Countries: Comparative Information Series (2008)*, OECD, 2009, 34, [www.oecd.org/dataoecd/57/23/42012907.pdf](http://www.oecd.org/dataoecd/57/23/42012907.pdf).

54 A 2010 OECD survey reported that around 84 percent of revenue bodies surveyed had established a dedicated unit for large taxpayers. Forum on Tax Administration, *Tax Administration in OECD and Selected Non-OECD Countries: Comparative Information Series (2010)*, OECD, 2011, 40, [www.oecd.org/dataoecd/2/37/47228941.pdf](http://www.oecd.org/dataoecd/2/37/47228941.pdf).

55 Forum on Tax Administration, 2011, 56.

56 Forum on Tax Administration, 2009, 47.

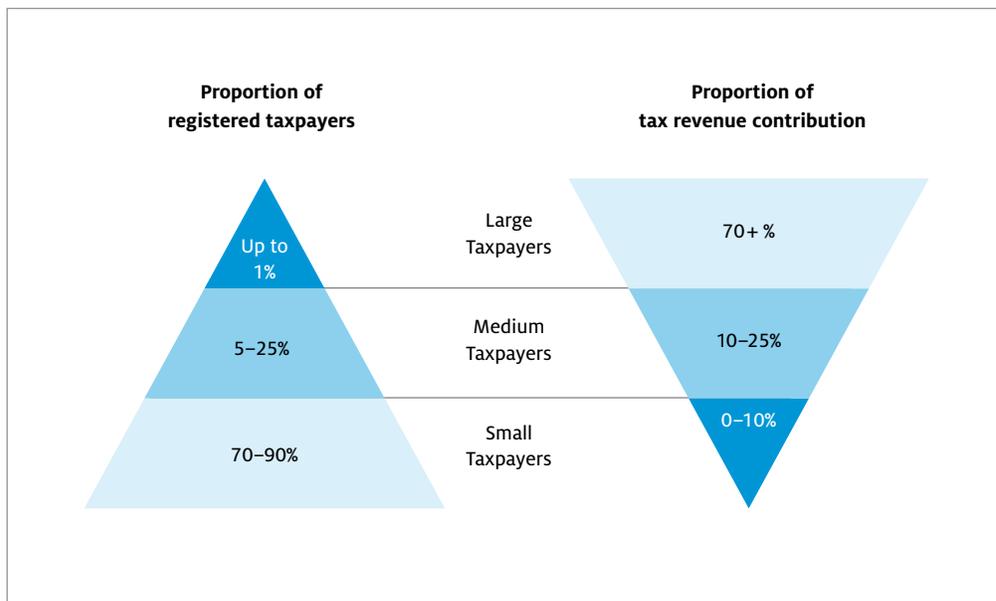
57 Forum on Tax Administration, 2011, 54-55.

58 Junaid Limalia, “The Role of Large Taxpayer Units,” *African Tax Administration Newsletter*, May 6, 2011, <http://ataftax.net/news/newsletters/ataf-newsletter-articles/the-role-of-large-taxpayer-units.aspx>.

others have dedicated in-house tax organizations. These advisors sometimes push the companies they advise toward aggressive tax structures, which require closer government monitoring to prevent potential abuses.

LTUs have several benefits, including improving compliance among the largest taxpayers, improving speed of collection, and improving the business climate by providing more sophisticated tax administration services for large companies.<sup>59</sup> Although there are typically only a small number of large taxpayers, their relative contribution to tax revenues is high. For example, 1.2 percent of Ghana's taxpayers contributed 63 percent of its tax revenue in 2009.<sup>60</sup> Figure 5 below illustrates this phenomenon. Establishing an LTU allows countries to devote auditing resources specifically to the largest taxpayers and to train auditors to specialize in the unique challenges of taxes for large companies. Because of the scale of large taxpayers' contribution to tax revenues, even a small increase in their tax compliance can have a large impact on revenues.

figure 5:  
**Taxpayer Segments and Relative Contributions to Tax Revenue**



Source: David Kloeden, *Revenue Administration Reforms in Anglophone Africa Since the Early 1990s*, International Monetary Fund (IMF), Working Paper WP/11/162, 2011, 26, [www.imf.org/external/pubs/ft/wp/2011/wp11162.pdf](http://www.imf.org/external/pubs/ft/wp/2011/wp11162.pdf).

In some resource-rich countries, there may be only handful of active, large-scale mining projects. For example, Zambia currently has eight large mining companies. An official in the Mining Unit of the Large Taxpayer Office of the Zambian Revenue Authority (ZRA) reports that they have gotten to know the companies well because of the frequency of interaction. This arrangement is helpful not only in developing good relationships with company counterparts, but also in identifying potential transfer pricing issues. Because there are only a small number of companies, the auditors know them and their corporate structures well. This allows the auditors to more easily identify related party transactions that they should scrutinize more closely for transfer pricing-related concerns.

59 William McCarten, *Focusing on the Few: The Role of Large Taxpayer Units in the Revenue Strategies of Developing Countries*, 2004, 12, [aysps.gsu.edu/isp/files/0444\\_McCartenv2.pdf](http://aysps.gsu.edu/isp/files/0444_McCartenv2.pdf).

60 David Kloeden, *Revenue Administration Reforms in Anglophone Africa Since the Early 1990s*, IMF, Working Paper WP/11/162, 2011, 26, [www.imf.org/external/pubs/ft/wp/2011/wp11162.pdf](http://www.imf.org/external/pubs/ft/wp/2011/wp11162.pdf).

The DRC provides a counterexample. Rather than a centralized organization, multiple agencies are responsible for tax collection. The Office des Douanes et Accises (OFIDA) collects customs, duties and export taxes; the Direction Générale des Recettes Administratives, Domaniales et de Participations (DGRAD) collects mining royalties, various fees and surface rents on behalf of the Ministry of Mines; the Direction Générale des Impôts (DGI) is responsible for assessment and administration of the value-added tax (VAT) and taxes on profits and dividends. Moreover, other smaller agencies collect other fees and smaller taxes.<sup>61</sup> These authorities do not have the resources or capacity to conduct their tax collection effectively. A 2009 study by a commission of the Congolese Senate identified more than \$450 million in lost revenues in the mining sector alone.<sup>62</sup> While consolidating tax collection within a single unit is neither inherently good nor bad, the division of scarce resources across multiple agencies may further exacerbate capacity constraints.

### Creating Semiautonomous Revenue Authorities to Increase Accountability and Improve Performance

One major consideration for countries is how their tax departments are organized with respect to the rest of the government institutions. In a few developed countries, the tax administration is a semiautonomous body, or collection of bodies, within the ministry of finance and is responsible not only for tax collection but also for customs administration.<sup>63</sup> In a significant number of Organisation for Economic Co-operation and Development (OECD) countries, unified, semiautonomous departments are responsible for administering taxes. These bodies report directly to a government minister and can have a formal management or advisory board.<sup>64</sup> Other characteristics include hiring personnel outside the traditional civil service and making the department independent or self-financing. The financing can often come from a percentage of gross collections.<sup>65</sup> This model has also been adopted by many developing countries, including Malaysia, Ghana, South Africa, Tanzania, Zambia and Bolivia.<sup>66</sup>

This model of semiautonomous revenue agencies, or SARAs, tries to shield the tax administration from public and political pressure, and can contain its own accountability system. Accountability can be a particularly acute problem in countries where staff appointments are made as a result of political patronage, which tends to result in under-qualified staff, corruption and high turnover rates. For example, an estimated three quarters of Bolivia's internal revenue agency staff was replaced after a change in government in 1997.<sup>67</sup> Semiautonomous revenue systems are also attractive because they can be funded independently, rather than receive funding as part of a government ministry.<sup>68</sup>

Another benefit is in hiring professional employees; tax agencies contained within the general civil service may be unable to hire the specialized professionals needed for tax administration. A related benefit is that SARAs can help prevent situations in which revenue agencies are also partially responsible for oversight of other aspects of the mining project. This conflates the tax administrators' duties with those of other government regulators and further complicates an already difficult job.<sup>69</sup>

61 World Bank, *Democratic Republic of Congo: Growth with Governance in the Mining Sector*, 2008, 25, <http://siteresources.worldbank.org/INTOGMC/Resources/336099-115695107170/drcgrowthgovernanceenglish.pdf>.

62 Commission d'Enquête sur le Secteur Minier, 96, 98-99.

63 Open Society Institute of Southern Africa et al., *Breaking the Curse: How Transparent Taxation and Fair Taxes can Turn Africa's Mineral Wealth into Development*, 2009, 43-44, <http://documents.twnafrica.org/breaking-the-curse-march2009.pdf>.

64 Forum on Tax Administration, 2009, 9.

65 Arthur J. Mann, *Are Semi-Autonomous Revenue Authorities the Answer to Tax Administration Problems in Developing Countries? A Practical Guide*, Fiscal Reform in Support of Trade Liberalization Project, 2004, 1, [pdf.usaid.gov/pdf\\_docs/Pnadc978.pdf](http://pdf.usaid.gov/pdf_docs/Pnadc978.pdf).

66 Robert Taliercio Jr., *Designing Performance: The Semi-Autonomous Revenue Authority Model in Africa and Latin America*, World Bank, 2004, 2, [http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2004/10/27/000160016\\_20041027132024/Rendered/PDF/wps3423.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2004/10/27/000160016_20041027132024/Rendered/PDF/wps3423.pdf).

67 Taliercio, 5-6.

68 Taliercio, 4.

69 Jack Calder, "Resource Tax Administration: The Implications of Alternative Policy Choices," in *The Taxation of Petroleum and Minerals: Principles, Problems, and Practice*, ed. Philip Daniel et al., (New York: IMF and Routledge, 2010), 329-30.

One study has found that revenue agencies' performances improve most when the level of autonomy is relatively high and stable, and it cites Peru, Kenya and South Africa as prime examples.<sup>70</sup> According to the study, greater agency autonomy has had the most positive effect on human resource management. Pre-reform agencies had tremendous trouble attracting, training and retaining high-caliber staff, which can be a problem for countries trying to enforce complex mining taxes. Salaries for tax employees have increased, sometimes dramatically, though this can often be coupled with harsh downsizing. Another difficulty has been somewhat higher turnover as a result of "poaching" from the private sector. But improvements in performance have not resulted in substantially higher costs; rather, collection costs are comparable to, or less than, those of nonautonomous tax agencies in developing countries. Most SARAs have also been successful in increasing tax revenues, though the reasons for this are difficult to measure.<sup>71</sup>

Implementing SARAs frequently results in the creation of advisory boards, comprised of nontax professionals. The idea is to create an additional level of oversight and independent guidance. For example, the Canada Revenue Agency (CRA) is overseen by a board of management, which has most of its members nominated by the provinces and territories. The board oversees organization and management, including development of the agency's business plan and management of policies related to resources, services and personnel.<sup>72</sup>

Australia, the United States and others rely on special bodies independent of the revenue agency to report on and oversee tax administration. The Inspector-General of Taxation is an independent agency responsible for reviewing the Australian Taxation Office's administration of the tax laws. The agency's purpose is to report and recommend improvements to the government.<sup>73</sup>

However, despite some success stories, the overall effect of autonomy is difficult to measure, and studies differ as to how much of a country's recent improvements can be attributed to the establishment of a SARA. It is clear that autonomy by itself is not sufficient to solve a country's tax and auditing problems and that autonomous agencies may present their own challenges.<sup>74</sup> For example, some have argued that treating the tax agency differently could have negative impacts on other parts of government by causing other civil servants to resent the tax authority, which may create challenges for cooperation.<sup>75</sup> Furthermore, the ultimate goal of the model is to develop the revenue authority's autonomy from the ministry of finance, which can be difficult to achieve. Finance ministers tend to retain power and influence in several key areas, including making appointments to the revenue authority's board, determining tax policy, and providing funding.<sup>76</sup>

### 3.2 Legal Frameworks

The legal frameworks that determine mining companies' obligations, whether legislative, regulatory, contractual or a combination of all three, must anticipate how those obligations will be monitored and enforced in practice. Uniform legal frameworks help simplify monitoring by providing a single set of rules applicable to all companies operating in the sector. Government accountability for monitoring different types of obligations should be established in the legal frameworks. When those responsibilities are not defined up front, effective monitoring will be less likely to take place over the course of the project. Companies' obligations should also be clearly defined so government and civil society monitoring agents can determine whether an obligation has been fulfilled or not: clearly defined rules will be easier to enforce than vague standards. By considering these factors before granting mining rights, governments can improve their chances of successfully managing the mining sector in the future.

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70 Taliercio, 11-12. The study does note, however, the difficulty in evaluating tax administrations: "It is difficult to measure with precision the marginal impact of tax administration reform on outcomes like revenue and debt collection, as many exogenous factors exert causal influence on these and other related outcomes." Even measuring autonomy itself is tricky.

71 Taliercio, 13-30.

72 Forum on Tax Administration, 2009, 19-20.

73 Forum on Tax Administration, 2009, 20.

74 Mann, 59.

75 Taliercio, 9.

76 Kloeden, 12-13

### Defining a Uniform Set of Obligations to Simplify Monitoring Efforts

As noted above, the proliferation of multiple legal frameworks within a country's mining industry can make monitoring even more difficult because government and civil society monitoring actors must analyze each company's agreement individually to identify that company's obligations. By contrast, establishing a uniform framework for all mining projects simplifies monitoring efforts. Under a uniform legal framework, government and civil society monitoring actors must learn one common set of company obligations.<sup>77</sup> Establishing a company's obligations in law, rather than in individually negotiated contracts, is one way to establish a uniform legal framework. Using model contracts is another.

#### **Model Contracts**

Some countries have adopted model contracts that aim to improve the stability and uniformity of extractive contracts by limiting the number of contract terms that are open to negotiation. These contracts are most commonly used in the petroleum sector, but are increasingly being used by governments to regulate the mining sector as well. While they are not a substitute for a clear, effective mining code, model contracts offer potential improvements to the stability, transparency and equity of a country's extractive sector.

There is considerable variation in the way that these model agreements are drafted and what their roles are in the country's overall regulatory scheme. In countries where the mining sector is

*Some countries have adopted model contracts that aim to improve the stability and uniformity of extractive contracts by limiting the number of contract terms that are open to negotiation.*

well regulated by a thorough, effective mining code, a model contract can be a short licensing document that provides a few project-specific terms and reaffirms the existing fiscal and dispute resolution mechanisms. At the other end of the spectrum are countries whose model contracts are lengthy documents that spell out every detail of a prospective mining or drilling operation. Because they uniformly establish many of the

important terms of an agreement, model contracts can aid efforts to monitor mineral projects even when the actual contracts are not publicly disclosed.

Additionally, the way in which model contracts are incorporated into a legal system varies from country to country. In many cases, they are not formally adopted by the country's parliament, but instead are developed as a matter of policy by the mining ministry. In other rarer cases, model contracts are established through specific legislation that introduces the model agreement and lays out the rules and requirements for its use. The relationship the model contract has with the existing mining code and other regulations varies as well, though ideally when the contract is passed via legislation, the implementing legislation will specify when the model contract explicitly overturns existing legislative and regulatory provisions. Generally, the model contract will address only certain aspects of the regulation and will work in combination with the existing mining code to propound a complete regime.

For example, Mauritania adopted its model mining agreement by passing Law No. 2002/02, which sets out the economic, customs, fiscal and foreign exchange rules for mining projects, but does not change any of the titling, renewal or transfer provisions of the mining code of 1999. It also allows a company to revert to the fiscal terms established in the code at any time. In contrast, some countries' model contracts can add confusion to the regulatory regime by making no reference to the previous code and neglecting to clarify any ambiguity between the old and the new rules.

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<sup>77</sup> Note that some project-specific obligations, such as those defined in EMPs, will always remain, as discussed in Section 1.2.

### *How Do Model Contracts Improve Monitoring?*

As discussed in Section 1.2, the legal context for extractive projects can vary considerably in complexity and variability, ranging from regimes in which the national mining code dictates most of the terms of an agreement and restricts derogations, to a model contract with one fiscal term as a variable, to lengthy mineral development agreements in which all terms are negotiable. In countries where a well-developed mining code is lacking or ineffective, model contracts provide increased uniformity of agreements. They also have the related benefits of improving transparency and reducing the cost and technical challenges of oversight for governments and civil society.

#### *Uniformity Improves Oversight and Reduces Transaction Costs*

In contrast to legal regimes in which each contract defines a separate and unique legal framework—thereby creating as many legal regimes as there are mining projects—model contracts offer some uniformity and clarify the terms and governing framework for the sector. This uniformity makes it easier for governments and civil society to monitor the contracts because it removes the need to make sense of and monitor multiple regimes.

Because they leave fewer terms open to negotiation than ad hoc contracts, model contracts can also reduce transaction costs. Negotiating complex mining agreements can require significant government resources, but having a model contract as the basis for negotiations reduces this toll and frees up government staff time for other activities, such as monitoring.

#### *Transparency Enables Better Public Monitoring*

When model contracts are publicly disclosed and reviewed by legislatures, as they should be, they can also play an important role in improving transparency. Model contracts that are available to the public and have very few variables left open to negotiation can provide most of the information relevant to monitoring efforts, such as the length of the contract period, fiscal terms, dispute resolution mechanisms and other key provisions. By setting the majority of the terms of present and future agreements and making them public, model contracts can also reduce opportunities for and suspicion of corruption in government negotiations. Conversely, significant deviations from the model agreement in actual contracts, while not conclusive evidence of corruption, may raise suspicions that special favors were negotiated.

### **Establishing Clear Monitoring Roles and Responsibilities to Increase Accountability**

Government roles and responsibilities for monitoring and enforcement must be clearly defined. If no one is assigned to monitor the implementation of particular types of obligations, they are likely to slip through the cracks in terms of government oversight. This challenge is especially pronounced in MDAs, or large-scale contracts that define a range of company obligations with respect to a project, including social obligations. For example, Liberia's MDA with China-Union contains a section requiring the company to provide medical care. The full text of the contractual obligation is provided in Box 6. Although the mining, health and labor ministries are all possible candidates to monitor China-Union's compliance with this obligation, it is unclear who is ultimately responsible. Unless the Ministry of Health and Social Welfare was directly involved in the contract's negotiation, it is unlikely to even be aware of this provision, let alone be able to set aside sufficient resources to monitor its implementation.

#### Box 6 | Sample Contract Provision Requiring Company to Provide Medical Care

During its Operations, the Concessionaire shall maintain and operate or cause to be operated, health facilities to ensure the availability in each Production Area of medical treatment, care and attention in accordance with applicable Law, and such other improved standards as may be agreed between the parties. Such treatment, care and attention shall be free of charge for the Concessionaire's employees and their resident spouses and dependents. Government officials and/or employees assigned to and regularly employed in the Production Area in an official capacity, and resident in or adjacent to the Production Area, and their resident spouses and dependants, shall, during the time of such assignment, employment and residence, also be entitled to receive medical care on the same basis as Concessionaire employees. The Concessionaire shall further provide reasonable access to such health facilities to members of local communities for ambulatory or emergency care. It is understood that "reasonable access" may include the imposition of fees that are reasonable in light of the economic level of such communities, it being understood that such fees are unlikely to cover the cost of service.

Source: Mineral Development Agreement between the Government of the Republic of Liberia, China-Union (Hong Kong) Mining Co. Ltd. and China-Union Investment (Liberia) Bong Mines Co. Ltd., 2009, Section 10—MEDICAL CARE, [http://www.leiti.org.lr/doc/Bong\\_Range\\_Signed\\_MDA\\_and\\_Schedules.pdf](http://www.leiti.org.lr/doc/Bong_Range_Signed_MDA_and_Schedules.pdf).

In these situations, it is unlikely that the communities, employees and government officials intended to benefit from the provision will see its full impact. This risk is particularly acute for a contract that remains confidential because the intended beneficiaries of the provision will be unaware that it exists and therefore unable to supplement government monitoring responsibilities with their own pressure for the company to fulfill its obligation. Wherever a company's obligations are defined—whether in laws, contracts or regulations—the government should also clearly identify which government ministries will be responsible for ensuring compliance with particular obligations.

#### Providing Clearly Defined Rules to Simplify Monitoring and Enforcement

Government and civil society monitoring and enforcement are made even more difficult when a company's legal obligations are vague or unclear. For example, while it will be relatively easy to determine whether a company has submitted a required report (they have either submitted it or they have not), it will be much more difficult to determine whether a company has provided "reasonable access" to medical care to communities surrounding a mine, as is required in the provision from Liberia's China-Union contract in Box 6 above.

Clearly defined rules composed of objective factors can be easier to monitor and enforce. Although such rules will not always be feasible, they can be implemented effectively in many situations. For example, Peru recently passed maximum permissible limits and environmental quality standards, which are expected to improve air quality and water pollution problems, along with citizens' quality of life. The World Bank reported that the prior lack of standards had hindered effective environmental monitoring and enforcement.<sup>78</sup> Clear limitations on pollution levels will allow the government to determine whether a company has complied with the law or not.

One of the biggest monitoring challenges for many countries is transfer pricing, defined in more detail in Box 7. The scale of the problem is enormous. Christian Aid estimates that developing countries lose \$160 billion each year to transfer mispricing and false invoicing.<sup>79</sup> To combat some of the problems associated with monitoring transfer pricing, some countries have established clear, specific rules addressing how companies can calculate costs and prices for the purposes of calculating taxes and royalties. Using reference prices that both companies and governments agree on helps ensure more equitable tax calculations. Table 1 presents some transfer pricing challenges and rules that have been enacted to combat them.

78 World Bank, *Program Document for a Proposed Environmental Development Policy Loan in the Amount of US\$330 Million to the Republic of Peru*, 2009, 53, <http://imas2010.files.wordpress.com/2010/07/program-document-wb-environmental-governance-loan.pdf>.

79 Hogg, et al., 2.

## Box 7 | Transfer Pricing and Its Monitoring Challenges

Large multinational companies often consist of groups of associated subsidiary companies located in different countries. These companies conduct transactions with each other, buying and selling minerals, providing services, lending money and so on. Transfer pricing refers to the “price, adopted for book-keeping purposes, which is used to value transactions between affiliated enterprises integrated under the same management.”<sup>80</sup>

These transactions are a normal part of conducting cross-border business. However, transfer pricing becomes a concern for governments because it affects how much profit multinational companies report in the jurisdictions where they operate, and therefore the taxes the governments are able to collect. Abusive transfer pricing, in which companies set prices at artificially high or low levels in order to avoid paying taxes in higher tax jurisdictions, can result in large losses of revenue.

Transactions between related companies should comply with the arm’s-length principle, which means that the “conditions of commercial and financial transactions between associated enterprises should not differ from the conditions that would be made between independent enterprises in comparable circumstances.”<sup>81</sup> However, subsidiary companies may conduct cross-border transactions at distorted prices in order to make less profit in high-tax jurisdictions and more profit in low-tax jurisdictions thus reducing the overall tax burden of the multinational company.<sup>82</sup>

Similar problems can arise in transactions between companies and their subcontractors. Companies have incentives to artificially inflate subcontractor prices in order to reduce their tax liabilities. Because many companies and subcontractors are repeat players in the industry, they can collude to agree to higher than arm’s-length prices for the subcontracts while working out private side agreements between themselves to represent a fairer allocation of the subcontract’s true cost.

In the following excerpt, an OECD task force identifies the difficulties faced by developing countries in monitoring transfer pricing:

- in building tax administration expertise and experience in transfer pricing to enable them to carry out effective audits—especially when faced with experienced and well-advised taxpayers. The difficulty is likely to be particularly acute in applying transfer pricing rules to complex transactions, such as those involving intangible assets or some forms of services;
- with applying rules that require taxpayer and tax administration discretion in application. Transfer pricing is not an exact science and audits in practice may have to be resolved through negotiation and compromise settlement;
- in obtaining the information needed from taxpayers in order to select cases for audit or carry out an effective audit. Access to data on intra-group transactions, including the respective functions of the parties to those transactions, and their economic and commercial context, is vital to carrying out a reliable transfer pricing analysis. Tax administrations typically obtain such information through transfer pricing documentation, return requirements or information powers (which may be specific to transfer pricing or of more general application). Obtaining this type of information may be problematic for developing countries, especially in the context of an audit of a domestic company that is a subsidiary of an international group;
- in obtaining public information on arm’s length conditions i.e. the conditions (for example, price or profit margin) in place for independent enterprises conducting comparable transactions under comparable circumstances. This is an issue that is repeatedly cited by developing countries as a significant difficulty to the implementation of transfer pricing rules.<sup>83</sup>

80 OECD, “Glossary of Statistical Terms: Transfer Price,” <http://stats.oecd.org/glossary/detail.asp?ID=2757>.

81 Informal Task Force on Tax and Development, *Draft: Objectives of the Sub Group on Transfer Pricing*, OECD, 2011, 5, <http://www.oecd.org/dataoecd/56/26/47521605.pdf>.

82 Informal Task Force on Tax and Development, 5-6.

83 Informal Task Force on Tax and Development, 7-8.

TABLE 1 | RULES TO ADDRESS TRANSFER PRICING CHALLENGES

Transfer Pricing Challenges	Possible Solutions	Examples
<p>A parent company finances a local project with an unduly high amount of debt. The interest payments on the debt reduce the local company's taxable profits.</p>	<p>Limit the percentage of project capital that can be financed through debt.</p>	<p>"Where a foreign controlled resident company has a foreign debt-to-equity ratio in excess of 3 to 1 at any time during the year of assessment, the amount of interest paid by the resident company during that year on that part of the debt that exceeds the ratio shall be disallowed as a deduction and an amount so disallowed shall be treated and taxed as a dividend."</p> <p>Botswana, Income Tax Act, 1995, 12th Schedule, paragraph 6.</p>
<p>A local company sells minerals to an affiliated company at a low price, reducing the value of the mineral for royalty calculations.</p>	<p>Calculate royalties based on international market price for a mineral, rather than the price at which the company sold the mineral.</p>	<p>"The base for calculating mining royalties is the gross sales value. The gross sales value is understood to be the amount that results from multiplying the weight of the refined mineral or metal content by its official price quote listed in U.S. dollars.</p> <p>"The official price quote is the bi-weekly average determined by the Executive based on the lowest daily price for spot transactions recorded on the London Metal Exchange, or, in its absence, on international metals exchanges or other exchanges, or in specialized publications of recognized international prestige, according to the regulations.</p> <p>"In the absence of official quotation for any mineral or metal, the gross sales value is the value stated in the bill of sale, Single Export Declaration, or equivalent document."</p> <p>Bolivia, Law No. 3787, 2007, Article 97.</p>
<p>A parent company charges a local company a significant amount of money for administrative services provided by the parent company, reducing the local company's taxable profits.</p>	<p>Limit the amount that can be deducted for home office costs.</p>	<p>"For the purpose of computing the chargeable income for any year of assessment of a holder of a mineral right there shall be deducted all outgoings and expenses which are exclusively and necessarily incurred by the holder for the purpose of exercising his rights under the mining lease and which are allowable deduction under the Income Tax Act calculated in the manner provided under that Act:                      Except that                      (a) in the case of head office expenses such expenses shall not exceed 1.5% of sales."<sup>84</sup></p> <p>Sierra Leone, Mines and Minerals Decree, 1994, Article 103.</p>

84 A better practice is to limit head office expenses to a percentage of costs, rather than to a percentage of sales. When the limit is based on sales, a company's allowable head office charges increase as its sales increase even though the head office expenses have not grown.

The provisions in Table 1 can be contrasted with more general transfer pricing provisions, which typically state that a commissioner can recharacterize transactions to reflect arm's-length prices. It is much easier for a tax official or a citizen to determine whether a company has charged more than a legally specified percentage of its costs for home office expenses than it is for those same individuals to determine whether a particular charge for home office expenses reflects arm's-length prices. Although these rules may be imperfect approximations of a fair arm's-length price, any errors at the margin are a small price in comparison with the certainty and enforceability they provide.

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**Additional resources on transfer pricing and tax advocacy:**

- *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010*, [www.oecd.org/ctp/tp/guidelines](http://www.oecd.org/ctp/tp/guidelines).
  - Christian Aid and SOMO, *Tax Justice Advocacy: A Toolkit for Civil Society*, 2011, [www.christianaid.org.uk/images/completetaxadvocacytoolkit.pdf](http://www.christianaid.org.uk/images/completetaxadvocacytoolkit.pdf).
  - Open Society Institute of Southern Africa et al., *Breaking the Curse: How Transparent Taxation and Fair Taxes can Turn Africa's Mineral Wealth into Development*, 2009, <http://documents.twnafrica.org/breaking-the-curse-march2009.pdf>.
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### **Requiring Company Self-Reporting to Reduce Government Monitoring Burdens**

Company self-reporting has become a common part of government monitoring structures. Instead of government agencies gathering all of the required monitoring information themselves, the government requires mining companies to calculate their own tax payments, conduct their own investigations, and to report to the government on their operations and compliance with their obligations. Government agencies then review the information the companies have provided and conduct any necessary follow-up. However, in order to enable meaningful monitoring, governments should require that these reports be:

- Based on internationally accepted reporting standards
- Regular and timely
- Transparent
- Open to auditing and requests for additional detail

The conditions listed above help ensure that governments have access to the information they need with the level of detail and in the format they need, at the appropriate points in time. For example, for tax and royalty figures, governments must ensure they have enough detailed information to make their own calculations about what a company owes. In order to identify and correct transfer pricing issues, auditors will want to know which companies were involved in particular transactions, what goods or services were involved in the transactions, and what prices were paid. Aggregate financial figures will not permit these kinds of calculations. When government inspectors need access to particular types of information, they should ensure that their reporting requirements reflect those needs. This may include detailed financial reporting as well as copies of contracts for significant transactions between related parties.

Another good practice is requiring companies to publicly disclose production volumes, costs and sales by mine, on a monthly basis. This detail should be provided for transactions that involved affiliated companies and those that did not. Such disclosure allows the public to monitor transfer pricing issues and makes it easier to expose manipulation.

Internationally accepted reporting standards, such as the Mining and Metals Sector Supplement to the Global Reporting Initiative's G3 Guidelines, are available to guide companies and governments in these efforts. The G3 Guidelines provide reporting principles and performance indicators for economic, social and environmental indicators. To support transparency, the EITI provides a framework for companies and governments to publicly disclose their tax payments and receipts.

Governments may also ask companies to report on areas of particular concern to enable better monitoring and tracking of high-risk issues. For example, in response to a rise in mine deaths, South Africa's DMR began requiring mining companies to provide health and safety reports.<sup>85</sup>

### ***Third-Party Verification of Company Reporting***

Although company self-reporting is a useful tool to assist with government monitoring, it does not eliminate the need for government agencies to rigorously review company reports and conduct independent investigations. There are two potential risks when companies report on themselves:

- The information provided may not be accurate.
- The reported information may not indicate compliance with the company's legal obligations.

Requiring third-party verification of company reports helps address both of these challenges. Governments can require that a third party verify the results of the company's report before it is submitted to the government. The government may also enlist the help of these third parties to ensure company reports are in the format and contain the level of detail the government needs in order to reduce time spent reviewing these reports. The government can specify what kinds of third parties are acceptable and may require certain certifications or credentials of the individuals or companies that verify results. Requiring particular credentials helps ensure that the third parties will provide meaningful, quality reviews, and requiring certification provides increased incentives to the third-party reviewers to act professionally and ethically since their certifications can be withdrawn for cases of malpractice.

Stock exchanges require third-party verification of securities disclosures to help ensure accuracy to protect investors. The scandal that helped lead to the third-party verification requirement for the Toronto Stock Exchange (TSX) is summarized in Box 8.

#### **Box 8 | The Bre-X Scandal and Expert Verification of Reports on the Toronto Stock Exchange**

In the mid 1990s, the Canadian company Bre-X Minerals Ltd. claimed it had found the world's largest gold deposit in Indonesia. Bre-X was publicly listed on the TSX, and investors flocked to get a piece of the company; the company's share prices nearly quadrupled in four months. But before production could even begin, the public discovered that the company had falsified samples and that its concession area in Indonesia contained only insignificant amounts of gold. It was one of the biggest stock market scandals in Canadian history. Bre-X stock plummeted, and investors lost billions of dollars.

The fact that the company had been able to raise significant amounts of money on the stock exchange—based on false information—alarmed investors. The TSX was a crucial market for junior mining companies to raise the money necessary for mineral exploration, and its value to the industry appeared to be in jeopardy.

To help protect investors, and ultimately the mining industry as well, National Instrument 43-101 established standards of disclosure for mining projects, including how mineral resources and reserves can be reported. The new rules required that mining company reports under the new instrument be written by or under the supervision of a "qualified person" who has no ties to the company. This requirement helps ensure that mining companies are not reporting false information about their mineral reserves. Investors do not have the time or resources to verify the information that companies provide via their stock exchange disclosures, but private third-party verification helps do so.

85 Ruona Agbroko, "SA to require miners to submit health and safety reports," *Mineweb*, April 21, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page504?oid=125571&sn=Detail&pid=92730>.

figure 6

# The Process and its Players

Monitoring the mining industry includes several actions, each linked to the others. They include:

- reviewing laws and contracts to understand companies' obligations,
- monitoring companies' activities to determine compliance with those obligations,
- communicating information to address any areas of non-compliance, and
- enforcing laws and contracts when companies fail to comply.

For the process to work, monitoring requires participation and cooperation from a range of actors throughout the life of a mining project. By working together, companies, civil society, parliament and government can effectively conduct the oversight necessary to avoid potential social and environmental harms.

All actors must examine contracts and laws to understand companies' obligations. Governments and companies must share information including not only contracts, but also ongoing project details, such as cost, revenue and production figures. Civil society and parliament can improve governance by scrutinizing the activities of both companies and the government.

Not least, all parties must communicate to see that companies fulfill their legal obligations and the countries involved fully benefit from their resource wealth.



**COMMUNICATING**



**Government**



**ENFORCING**



**REVIEWING**



**Parliament**

## Designing Tax Regimes to Maximize Returns and Ease Enforcement

Certain tax systems are better suited for developing countries trying to maximize the value of their mining resources. Different taxes include: corporate income tax; progressive profit tax; resource rent tax; import duties; VAT; royalties; and various nontax instruments. Some of these are easier to administer and thus can be more attractive to countries with limited auditing capabilities. But ease of administration should not be the dominant policy; if the potential gains from a complex tax system outweigh the losses from inefficiencies in the administration of such a system, it should still be strongly considered.<sup>86</sup> There are a number of factors for governments to consider, including the specificity and uniformity of the tax regime; ease of administration and reduced costs; and ways to limit opportunities for corruption.<sup>87</sup> Whatever tax regime a country chooses, a uniform regime eases the administrative burden.

The standard corporate income tax has substantial benefits in terms of ease of administration. This is largely because it does not require a separate tax regime, so tax officials will already be familiar with the framework and administrative procedures. However, other considerations may predominate; for example, since many mining ventures operate as projects rather than as firms, ring-fencing has to be taken into account.<sup>88</sup> With this tax, corporations also find it easy to avoid tax liability through techniques such as transfer pricing.<sup>89</sup>

Some tax regimes include a progressive profit tax, which allows countries a greater share in the upside of highly profitable mining projects. However, since these are often done on an ad hoc basis and require additional oversight, it can increase the burden on the tax administration. Part of the difficulty lies in calculating which revenues are applicable—determining whether to include

ancillary income, financial income, gains on disposal of license interests and so on. Further complications involve determining applicable costs, for example, how depreciation should be calculated.<sup>90</sup>

The same can be said of resource rent taxes, which effectively act as a back-loaded tax on profitability over and above an investor's return on investment.<sup>91</sup> While implementation of such a tax can be burdensome on

unsophisticated revenue agencies, this should not be automatically disqualified. Furthermore, the basic skills for enforcing a resource rent tax are comparable to those required for a basic income tax. Administrative burdens can be minimized by measures that simplify the auditing process. These include consolidation of tax sub-regimes, use of standardized contracts, reliance on familiar industry and accounting standards, coordination of various tax rules, and simplification and reduction of particular provisions in the tax code.<sup>92</sup>

VATs have frequently been introduced. Since they generally target domestic consumption, various mechanisms, such as refunds, have been used to ensure that export-oriented industries, including mining, are shielded from the VAT burden. However, monitoring and implementing these mechanisms can be burdensome on under-funded or under-staffed revenue agencies, which may be unable to pay refunds in a timely fashion. VAT refunds can be quite substantial, particularly during investment periods. Faced with such administrative hurdles, some countries often take shortcuts in granting exemptions, which create loopholes for companies to exploit.<sup>93</sup>

*In designing a tax regime, officials should consider the specificity and uniformity of the tax regime, ease of administration and reduced costs, and ways to limit opportunities for corruption.*

86 Calder, 324.

87 Otto et al., 10-12.

88 Ring-fencing is the practice of taxing separate mining projects individually rather than allowing a single company to combine all of its projects within a country for tax purposes. Ring-fencing is beneficial to the government because it prevents a mining company from writing off costs of one project against revenues from another in order to pay lower overall taxes.

89 Thomas Baunsgaard, *A Primer on Mineral Taxation*, IMF, Working Paper WP/01/129, 2001, 6, [www.imf.org/external/pubs/ft/wp/2001/wp01139.pdf](http://www.imf.org/external/pubs/ft/wp/2001/wp01139.pdf).

90 Baunsgaard, 7-8; Calder, 321.

91 Baunsgaard, 8.

92 Calder, 326-27.

93 Baunsgaard, 11.

Royalties are an important method for governments to recoup the value of the country's natural resources. Royalties are fees based on the quantity of material produced, or its value. Royalties guarantee income up front, even if the project is not profitable. With regard to administration and auditing, many types of royalties are easy to administer and difficult to evade because revenue agencies are able to determine a company's liability based only upon a company's total sales or amount of production. This has the benefit of lowering administrative costs—including those associated with higher expertise—as well as reducing corporations' incentives to attempt to shirk responsibility. The simplicity of calculating royalties can also limit opportunities for corruption.<sup>94</sup>

Royalties can take different forms. The *ad valorem* form, which takes a percentage of a mineral's value, is presently the most popular. However, unit-based royalties, which set a fixed charge per unit, are often applied to industrial minerals. Some countries with more competent revenue agencies have been moving toward profit- or income-based taxes. For example, nearly all Canadian provinces have replaced traditional royalties with adjusted income taxes. The U.S. state of Nevada and the Northern Territory in Australia have made similar moves.<sup>95</sup>

However, these types of royalties may not be best for countries with less administrative ability. Unit and *ad valorem* taxes do not require cost accounting and are therefore easier to enforce and less vulnerable to manipulation than systems based on profits or net income. For example, calculating the profit base can be very complicated, especially since this profit can be different from financial accounting profit; thus, companies can be required to keep a separate set of accounts and accounting systems, which can be conducive to error or intentional misrepresentation. This in turn creates additional labor-intensive work for auditors, and potentially heightened legal costs as a result of more litigation. Meanwhile, unit-based royalties may be more appropriate for low-value bulk commodities, which have less price volatility. By the same token, *ad valorem* royalties may be preferable for higher-value commodities, or large-volume operations.<sup>96</sup>

An additional element of taxation regimes is the form in which payments are accepted, particularly the distinction between in-kind and cash payments. Some governments accept royalties in kind, meaning royalties paid in resources—typically oil or gas—as opposed to cash payments. Payments in kind present additional administrative and auditing challenges in that the resources received must be carefully measured and accounted for, a requirement that caused serious concern in the United States's royalty in-kind program. It was discontinued in 2010 as part of a “commitment to ensuring that royalty collection on behalf of the American people is conducted transparently, accurately and fairly.”<sup>97</sup> In-kind payments also raise transparency concerns; the payments are often the subject of special contracts between industry and government, which are rarely released for public scrutiny.<sup>98</sup>

### 3.3 Government Oversight Institutions

Nonexecutive branch government officials can and should play a significant role in ensuring that the mining industry is managed effectively. Parliaments, supreme audit institutions, ombudsmen and human rights commissions have all taken on monitoring roles in various countries. Their reports and advocacy efforts can help provide more information to civil society and to improve executive branch monitoring effectiveness by calling attention to concerns and shortcomings.

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94 Baunsgaard, 10; Otto et al., 1, 11.

95 Otto et al., 37.

96 Otto et al., 38, 66-70.

97 “Interior Completing Close-Out of Royalty in Kind Program” (press release), U.S. Department of the Interior, Sept. 24, 2010, <http://www.doi.gov/news/pressreleases/Interior-Completing-Close-Out-of-Royalty-in-Kind-Program.cfm>. On the challenges with the U.S. royalty in kind program, see Project on Government Oversight, *Drilling the Taxpayer: Department of Interior's Royalty-In-Kind Program*, 2008, <http://pogoarchives.org/m/nr/rik/report-20080918.pdf>.

98 Testimony of Danielle Brian before the House Committee on Natural Resources, Sept. 17, 2009, <http://www.pogo.org/pogo-files/testimony/natural-resources/nr-rik-20090917.html>.

## Parliament: Increasing Transparency and Accountability

Parliaments in resource-rich countries can play an important role in working to increase accountability in how the executive branch manages the extractive sector. Members of parliament can push for more transparency and can share the information they have with citizens who are leading monitoring efforts. In some cases, parliaments have also conducted special investigations to understand governance concerns in their countries' natural resource sectors, with the ultimate goal of improving how they are managed.

### *Democratic Republic of Congo—Scrutinizing the Executive Branch*

Following the presentation of the DRC's budget in 2008, the country's senate noted that the government's receipts from mining had been quite weak. As a result, the senate created a special commission to investigate the mining industry with an ultimate goal of improving revenue collection to bolster the country's budget. The commission, headed by Sen. David Mutamba, collected information and statistics, carried out investigations, and conducted surveys and interviews to identify and understand problems in the country's mining industry. Through its investigation, the commission made several interesting findings, including:

- **Underreporting of production volumes**, which affects taxes and royalties: In a one-month period, the mineral quantities reported on transport documents were systematically reduced by 10 times for certain exporters compared with the quantities reported in loading documents.<sup>99</sup>
- **Undercollection of surface rents**: The government collected only 31.37 percent of all surface rents and therefore missed out on more than \$30 million.<sup>100</sup>
- **Insufficient statistics**: Government ministries did not collect necessary statistics; therefore they could not identify the operators active in the country or the volume and quality of their mineral production.<sup>101</sup>
- **Illegal tax breaks**: Mining and finance ministers reduced tax rates illegally, in violation of the Constitution and to the detriment of the treasury.<sup>102</sup>

The Mutamba Commission's mandate and ability to access information about the mining ministry allowed it to bring to light some alarming problems facing the country. Armed with this information, parliamentarians and citizens can work to hold their executive branch officials accountable for their shortfalls in monitoring and managing the mining industry.

### *South Africa—Parliamentary Questions*

South Africa's Constitution gives the national assembly authority for passing legislation and scrutinizing and overseeing the executive branch.<sup>103</sup> Officials in the executive branch must answer questions they receive from Parliament, and, because Parliament's activities are public, this mechanism is an important way of holding the executive branch accountable to the people.<sup>104</sup> Parliamentarians can use this oversight mechanism to monitor the executive branch's management of the mining sector and to ensure it is enforcing companies' obligations. For example, in May 2011, the Minister of Water and Environmental Affairs received a question about a coal mining company's environmental transgressions, whether the company had been fined, and whether the company had paid any relevant fines. The Department of Environmental Affairs responded to the question in writing, noting that the company had been fined more than 9 million rand and that the payment had been received.<sup>105</sup>

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99 Commission d'Enquête sur le Secteur Minier, 41.

100 Commission d'Enquête sur le Secteur Minier, 37.

101 Commission d'Enquête sur le Secteur Minier, 126.

102 Commission d'Enquête sur le Secteur Minier, 127.

103 South Africa, Constitution, 1996, art. 42(3).

104 Parliament of the Republic of South Africa, "Oversight," [http://www.parliament.gov.za/live/content.php?Item\\_ID=27](http://www.parliament.gov.za/live/content.php?Item_ID=27).

105 South Africa, Department of Environmental Affairs, "Question 1405," May 2011, <http://www.environment.gov.za/ParliamentUpdate/2011/may/question1405.pdf>.

One official in the DMR noted that citizens can go through their representatives to use this parliamentary question mechanism to get information about the mining industry, and that this method may be faster and more reliable than using the country's access to information law.

### **Judiciary: Enforcing Obligations in Situations of Noncompliance**

Capacity challenges within government are not solely a problem for the executive branch. In the judiciary, judges, prosecutors and magistrates all must be educated and empowered to actively oversee the extractive industries. Zambia's Copperbelt Environmental Project, which works to improve how the government manages the environmental impacts of the country's mining sector, has included trainings for the judicial branch to ensure that environmental violations are taken seriously and are prosecuted effectively.

Lack of this sort of training can have a serious impact. One region in South Africa had no successful prosecutions for health and safety violations in the last eight years even though the lead inspector recommended 13 cases for prosecution in 2010 alone. This low rate could be attributed to having prosecutors assigned to the DMR located in another province and lacking the technical experience necessary to understand the nature of mine accidents.

To partner effectively with the judiciary, government agencies must also train their own staff on legal issues. DMR inspection engineers with technical background and knowledge of relevant legislation would be better able to identify incidents when someone from the mining company may be liable and to gather sufficient information during their inquiries to support a later legal prosecution.

Government agencies that want to improve enforcement of mining companies' obligations should consider the judiciary as a partner in this process and can train judges, magistrates and prosecutors to help achieve this goal. Civil society groups can also work with the judiciary to help its members better understand the unique aspects of the mining industry to improve overall enforcement.

### **Supreme Audit Institutions: Investigating Government's Management of the Mining Sector**

Supreme audit institutions (SAIs) conduct independent audits of governmental bodies. They typically investigate the use of public resources, which often involves analyzing the efficiency of government agencies and the quality of their work, including the government's management of the natural resources sector. Since SAIs often publish the reports of their findings publicly, their conclusions and the information they gather through their investigations are available to the government ministries audited and to the public at large. The investigations can help improve how the government manages the mining sector by giving government agencies an independent assessment of their work and recommendations for areas for improvement, and by publicizing the results, allowing citizens to understand shortcomings in the government's management of the sector and to demand better government accountability.

A 2005 report by the auditor general of the Canadian province of Ontario looked into the provincial government's mines and minerals program. One of the audit's objectives was to determine whether the Ministry of Northern Development and Mines had adequate procedures in place to ensure compliance with provincial policies and legislation. The resulting audit report identified several problems with the management of the mineral sector and made corresponding recommendations for how the ministry could improve its performance in the future. The report also included the government's response to each recommendation.<sup>106</sup>

INTOSAI, the International Organization of Supreme Audit Institutions, has formed a working group on environmental auditing to encourage SAIs to examine concerns related to environmental protection and sustainable development. The group recently produced a report specific to mining

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106 Office of the Auditor General of Ontario, 184-85.

that includes stories of institutions that have audited environmental concerns related to mining.<sup>107</sup> One of the stories was about Indonesia's SAI, which conducted an audit of two tin companies to ensure they were fulfilling their legal and contractual obligations. The SAI based the audit on the government's mining and environmental laws, and found that both companies had failed to conduct appropriate reclamation efforts at some of their mining sites.<sup>108</sup>

### Human Rights Commissions and Ombudsman Offices: Providing a Voice for Citizens

Human rights commissions and ombudsman offices can help protect communities from negative impacts of mining. Commissions often hear complaints from citizens, and will work with companies and citizens or communities to help resolve the underlying concerns. In Zambia, for example, the human rights commission hears a large number of complaints related to employment concerns in the mines. The commission investigates each complaint and identifies appropriate remediation strategies. In Peru, where mining is the number one cause of social conflicts, the country's ombudsman hears and helps mediate many complaints that communities file against mining projects every year.

Besides investigating and mediating individual complaints, human rights commissions may also make recommendations to other government agencies based on their investigations. The Philippines' Commission on Human Rights recently recommended that the government withdraw OceanaGold Ltd.'s mining right due to violations of indigenous people's rights. Loretta Ann Rosales, the head of the commission, reported that the company had violated indigenous peoples' rights to adequate housing and freedom of movement, as well as their right to culture and identity.<sup>109</sup>

## 3.4 National and Government Partnerships

Partnerships can help address some of the challenges created by problems of capacity, transparency and incentives. Partnerships can draw from the capacities or resources of the better endowed partner—typically industry—to shape a mechanism intended to allow the other partners to develop capacity and confidence in the process. Partnerships can also involve would-be competitors. Some governments require oil companies to operate in JVs with each other so minority company partners can monitor the operating partner's operations, including for transfer pricing issues that can be extremely difficult for governments to monitor effectively. Involving communities and civil society organizations offers an opportunity to confront contrasting interests and incentives.

To be effective, the checks and balances in partnerships must be carefully calibrated and monitored over time to ensure that potential benefits are reached. Otherwise, partnerships can be undermined when one partner dominates, or can lose legitimacy for other reasons. National and government partnerships are addressed in this section, while local and community partnerships are presented in Section 3.5.

### Partnering with Private Sector to Enhance Public Sector Capacity

When government ability to monitor is weak, some countries, including Zambia and Angola, have asked private companies for assistance.

#### *Private Financial Audit in Zambia*

In 2009, the Zambian government hired Grant Thornton LLP and Econ Pöyry to conduct financial audits of mining companies, including Mopani Copper Mines (MCM), which is jointly owned by Glencore and First Quantum Minerals.<sup>110</sup> The MCM audit, which was leaked, identified several irregularities in MCM's tax payments. Most notably, the mine's costs had increased significantly

107 Working Group on Environmental Auditing, *Auditing Mining: Guidance for Supreme Audit Institutions*, INTOSAI, 2010, <http://www.environmental-auditing.org/LinkClick.aspx?fileticket=Ffb%2f3zmeZ8%3d&tabid=128&mid=568>.

108 Working Group on Environmental Auditing, 47.

109 Manny Mogato, "Govt. should consider withdrawing OceanaGold's mining rights—rights commission," *Mineweb*, Jan. 17, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page504?oid=118629&sn=Detail&pid=110649>.

110 Ed Stoddard and Chris Mfula, "Tax issues at Konkola Copper Mines, First Quantum—Zambian Finance Minister," *Mineweb*, June 17, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page67?oid=129525&sn=Detail>.

between 2005 and 2007, and many of these increases could not be explained, including \$50 million in increased labor costs. The overall costs in 2007 were \$381.21 million higher than what the auditors estimated costs should have been based on 2005 figures and estimated increases based on production figures and index prices.

In addition to identifying particular areas of concern in MCM's accounting, the auditing companies made the following recommendations to the Zambian parliament and the ZRA:

- The pilot audit has shown that there is a great need for a determined effort at collecting the taxes that are assessed under the laws implemented by the Zambian parliament.
- The pilot audit has shown that ZRA needs the Ministry of Mines to follow up production volumes . . . on a more consistent and comprehensive basis in order for the calculation of royalty to be reliable.
- The pilot audit has shown that there is a high need for implementing punitive measures against
  - companies that do not pay their taxes on time
  - companies that does [sic] not cooperate with the ZRA and make audits more expensive and lengthier than needed.<sup>111</sup>

The reasons behind the government's decision to conduct private audits are not known, and indeed the results of the MCM audit are known only because the report was leaked. It seems likely that the government either had particular suspicions about the companies, or it wanted to conduct random or systematic audits of mining companies to supplement its own ongoing monitoring efforts. In either case, the MCM audit uncovered several important issues, and the Zambian government is reportedly now working to recover the taxes identified.<sup>112</sup>

Spending time and money on tax auditing is a wise investment that can improve the government's ability to collect tax revenues, providing more resources in the future. When governments have reason to be suspicious of a company, they can normally conduct their own in-depth audits. However, when a government agency suspects wrongdoing but does not have the time or the resources to investigate further, hiring a private auditor may be a useful solution.

### ***Private Inspections in Peru***

Peru's OSINERGMIN is responsible for, among other things, monitoring health and safety issues in the mining industry. OSINERGMIN uses private companies that work exclusively with the agency to conduct its health and safety inspections. The mining companies pay the costs of these private audits through OSINERGMIN, so there have not been financial constraints on the agency's ability to conduct the necessary inspections. OSINERGMIN identifies the mines for inspection, and the private companies create a budget. OSINERGMIN sends this to the mining company, which is required to pay the full costs to the agency. If the company does not pay on time, OSINERGMIN has the authority to withdraw the company's authorizations to mine.

The private companies that conduct the inspections are selected based on merit, as determined through a public contest. The companies are required to take tests on subject areas for which OSINERGMIN requires inspections, and one company is chosen for each inspection subject area.

Officials in OSINERGMIN report that this system has been very effective in providing high quality, professional inspections. Having the mining companies cover the costs of the inspections should reduce the financial pressure on the agency. And having the companies pay inspection costs directly to OSINERGMIN should reduce risks of corruption or payoffs.

This arrangement has its critics. They suggest that OSINERGMIN may have gone too far in its effort to distance itself from substantive engagement with monitoring. According to one informed lawyer, the cost structure still leads to hasty, insubstantial audits, frequently without site visits.

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111 Grant Thornton and Econ Pöyry, *Pilot Audit Report—Mopani Copper Mines Plc*, 2010, 9.

112 Chris Mfula, "Zambia asks Glencore subsidiary for 'underpaid' mining taxes," *Mineweb*, June 7, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page72068?oid=128735&sn=Detail&pid=72068>.

Requiring companies to disclose more information about their tax payments across jurisdictions can help countries better monitor financial obligations. Understanding where a company pays taxes and how large its tax commitments are in various jurisdictions can help government auditors and civil society monitoring groups identify potential areas of concern.

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### ***Private Tax Collection Assistance in Angola***

The government of Angola has been working with Aupec, a private economic consulting firm, since 2001 on its tax administration and financial planning for the oil sector. Part of Aupec's involvement included working in the petroleum unit of the country's income tax administration to help monitor companies and collect taxes. To do this, the firm participated directly in the ongoing tax administration and trained Angolan officials to take over tax administration in the future. Angola also hired Deloitte & Touche, a large international accounting and auditing company, to conduct tax audits and to train Angolan tax officials in auditing techniques.<sup>113</sup> This arrangement provided Angolan officials top-notch, on-the-job training to improve the country's capacity and performance for the future—while also improving monitoring and tax collection in the present.

### **Partnering Internationally to Combat Transfer Pricing**

When companies operate in multiple countries, they may be able to shift costs and profits between jurisdictions to minimize their tax burden. Transfer pricing is discussed in more detail in Box 7 in Section 3.2. As noted there, some of the key challenges for monitoring transfer pricing issues are capacity and access to information.

International partnerships among governments can help address some of the information challenges associated with transfer pricing and multijurisdictional tax questions. International tax treaties that facilitate sharing information across jurisdictions and a recent multinational cooperative audit of a brewing company are both discussed below.

In addition to agreements among country governments, home country disclosure requirements can also contribute to financial monitoring efforts. The recent Dodd-Frank Wall Street Reform Act in the United States requires U.S.-listed companies to disclose project-by-project revenue data through their stock exchange disclosures. More information on the disclosures that act requires is provided in Appendix 3.

Other countries are considering similar measures. Requiring companies to disclose more information about their tax payments across the jurisdictions in which they operate can help countries better monitor the financial obligations. Understanding where a company pays taxes and how large its tax commitments are in various jurisdictions can help government auditors and civil society monitoring groups identify potential areas of concern. As these requirements become more common, stock exchange disclosures are likely to become an increasingly important source of information.

### ***Sharing Information Internationally***

Some types of international treaties provide for sharing information for tax purposes: double taxation agreements (DTAs) and tax information exchange agreements (TIEAs). DTAs are agreements between two states that prevent profits from international business activities from being taxed in both countries (i.e., they prevent the same profits from being taxed twice). These agreements are primarily intended to attract foreign investment, but they also facilitate the monitoring of taxation issues across borders.<sup>114</sup> The OECD has created the Model Convention with Respect to Taxes on Income and on Capital that serves as the basis for many DTAs. Its information-sharing provision is provided in Box 9. TIEAs are focused exclusively on sharing tax information and are thus narrower than DTAs. They typically provide rules and procedures for how tax information will be shared.<sup>115</sup> The OECD has also developed a model TIEA, the Agreement on Exchange of Information on Tax Matters.<sup>116</sup>

113 Patrick Heller, "Turning Wealth into Development: Comparison of Angola and Nigeria" (paper presented at Oil Dependent Producer States conference at the Center for Democracy, Development and the Rule of Law, Stanford University, May 2007), 51-52.

114 Tax Justice Network, *Tax Information Exchange Agreements*, 2009, 1, [http://www.taxjustice.net/cms/upload/pdf/TJN\\_0903\\_Exchange\\_of\\_Info\\_Briefing\\_draft.pdf](http://www.taxjustice.net/cms/upload/pdf/TJN_0903_Exchange_of_Info_Briefing_draft.pdf).

115 Tax Justice Network, 2.

116 Global Forum Working Group on Effective Exchange of Information, *Agreement on Exchange of Information on Tax Matters*, OECD, 2002, [http://www.oecd.org/document/37/0,3746,en\\_21571361\\_43854757\\_44270949\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/37/0,3746,en_21571361_43854757_44270949_1_1_1_1,00.html).

Article 26

EXCHANGE OF INFORMATION

1. The competent authorities of the Contracting States shall exchange such information as is foreseeably relevant for carrying out the provisions of this Convention or to the administration or enforcement of the domestic laws concerning taxes of every kind and description imposed on behalf of the Contracting States, or of their political subdivisions or local authorities, insofar as the taxation thereunder is not contrary to the Convention. The exchange of information is not restricted by Articles 1 and 2.
2. Any information received under paragraph 1 by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State and shall be disclosed only to persons or authorities (including courts and administrative bodies) concerned with the assessment or collection of, the enforcement or prosecution in respect of, the determination of appeals in relation to the taxes referred to in paragraph 1, or the oversight of the above. Such persons or authorities shall use the information only for such purposes. They may disclose the information in public court proceedings or in judicial decisions.
3. In no case shall the provisions of paragraphs 1 and 2 be construed so as to impose on a Contracting State the obligation:
  - a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State;
  - b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State;
  - c) to supply information which would disclose any trade, business, industrial, commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (*ordre public*).
4. If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall use its information gathering measures to obtain the requested information, even though that other State may not need such information for its own tax purposes. The obligation contained in the preceding sentence is subject to the limitations of paragraph 3 but in no case shall such limitations be construed to permit a Contracting State to decline to supply information solely because it has no domestic interest in such information.
5. In no case shall the provisions of paragraph 3 be construed to permit a Contracting State to decline to supply information solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.

OECD, *Articles of the Model Convention with Respect to Taxes on Income and on Capital*, 2008, <http://www.oecd.org/dataoecd/43/57/42219418.pdf>.

Although many TIEAs and DTAs are currently in force, creating the potential for widespread sharing of tax information, there are several problems with the implementation of these agreements and with their effectiveness. As explained in the Tax Justice Network's briefing paper on TIEAs, these problems include:

- Because these agreements are signed between states, they do not cover all jurisdictions: information must be shared only between countries that have signed an agreement with each other.
- Developing countries tend to get left out of these agreements because they do not have enough leverage to strike good deals with large developed countries.
- Information is not exchanged automatically. Instead, governments must request specific information from other governments, and there are strict conditions on the form such requests must take. These rules and technicalities make it difficult to exchange information.

- Relevant information may be unavailable or difficult to collect. Jurisdictions do not collect uniform information on tax payments and underlying data, and the information requested may not be available from the jurisdiction that would need to provide the information.<sup>117</sup>

Governments should work to improve the information-sharing procedures already in place through existing DTAs and TI EAs in order to help enhance their ability to monitor transfer pricing issues. Given the current challenges, the Tax Justice Network recommends moving toward automatic multilateral information exchanges.<sup>118</sup>

### ***Multinational Audit—SABMiller in Africa***

Extractive companies are not the only multinational entities that create transfer pricing challenges. A 2010 report from ActionAid UK called attention to potential tax evasion by SABMiller, a multinational brewing company based in England.<sup>119</sup> According to the report, the cost to governments could be as high as £20 million per year, or more than \$32 million. In May 2011, the African Tax Administration Forum announced its intention to coordinate a multinational, five-country audit of the brewer's operations across Ghana, Mauritius, South Africa, Tanzania and Zambia.<sup>120</sup>

This multinational audit represents an innovative step in the battle against transfer mispricing. The tax administrations in the five countries will be able to work together to share information and to build mutual capacity for auditing transfer pricing issues. While it is too early to know where this audit will lead, the idea of multinational partnerships for auditing may be interesting to pursue in the extractive sector as well.

### **Partnering with Unions to Improve Health and Safety Monitoring**

Unions can be valuable partners in monitoring ongoing operations at mining sites, particularly with regard to occupational health and safety requirements. Union representatives are already at the sites, and they have an interest in ensuring safer working conditions for their members.

In South Africa, union representatives reportedly accompany government health and safety inspectors during their visits to the mines but are not always able to independently identify safety issues. Furthermore, they may not feel empowered to raise their concerns to government inspectors, or they may fear that doing so could put their jobs in danger.

Governments can work to realize the benefits of partnering with unions by:

- Training union representatives on health and safety standards, and how to identify potential risks and violations.
- Providing a mechanism for union representatives to report possible violations to government health and safety inspectors, and following up by inspecting the reported concerns.
- Protecting union representatives against reprisals for reporting possible health and safety violations.

Companies can also partner with unions to improve health and safety monitoring. In 2008, steel company ArcelorMittal worked together with unions to form the Joint Global Health and Safety Committee to respond to concerns about workplace fatalities. The agreement “recognise[d] the key role that trade unions can play in addressing health and safety issues and encourage[d] union management partnerships to improve standards and participation in order to raise health and safety

117 Tax Justice Network, 2-4.

118 Tax Justice Network, 5-6.

119 Martin Hearson and Richard Brooks, *Calling Time: Why SABMiller Should Stop Dodging Taxes in Africa*, ActionAid UK, 2010, [http://www.actionaid.org.uk/doc\\_lib/calling\\_time\\_on\\_tax\\_avoidance.pdf](http://www.actionaid.org.uk/doc_lib/calling_time_on_tax_avoidance.pdf).

120 Ethel Hazelhurst, “Global brewer under tax lens,” (South Africa) *BusinessReport*, May 6, 2011, <http://www.iol.co.za/business/companies/global-brewer-under-tax-lens-1.1065154>. The African Tax Administration Forum, established in 2009, “is a platform to promote and facilitate mutual cooperation among African Tax Administrations and other relevant and interested stakeholders with the aim of improving the efficiency of their tax legislation and administration. The Forum brings together Heads of African Tax Administrations and their representatives to discuss the progress made, challenges faced and possible new direction for African tax policy and administration in the 21st Century.” African Tax Administration Forum, “Overview,” <http://www.ataftax.net/about-us/overview.aspx>.

standards.”<sup>121</sup> It required each work site to meet certain standards, including the establishment of a joint health and safety committee, comprised of both management and workers, to follow up on accidents, perform regular inspections, and identify training needs for workers. The joint approach has had a positive impact on the number of workplace accidents, and fatalities have been reduced by one-third.<sup>122</sup>

### **Partnering within Government to Combat Capacity Shortages**

In cases of reduced government capacity, partnering across government agencies may provide some benefits. As an initial step, agencies can ensure they are sharing necessary information with their counterparts to enable better monitoring across all parts of government. When this is not already taking place, agencies can communicate to identify their information needs, what information they already collect, and how to implement regular processes for sharing useful information among agencies.

Beyond sharing information, however, agencies can also coordinate inspections or other enforcement work. For example, government agencies in Zambia report that they share information across agencies about when they will visit mine sites. Coordinating visits to the mines may allow inspectors from different agencies to travel together, reducing the challenge of insufficient vehicles. Such coordination may be particularly valuable when a government agency has only one central office but is required to visit mining sites throughout the country. The Zambian agencies have improved their coordination through joint patrols and joint monitoring, in which multiple agencies visit the same mine site all at once. If not all agencies are able to participate in an inspection, they can submit particular questions or information requests for the other agencies’ inspectors to look into while they are on site. Although joint inspections may not be feasible in all cases and individual agency inspectors tend to be stretched to capacity even without taking on additional work from other agencies, such ideas are worth considering and discussing as there may be opportunities for saving time and resources in the future through improved coordination.

In addition to its inter-ministerial coordination efforts, the ECZ has partnered with local water utilities. It installed simple pH meters on the water utility pumps so they shut off if the pH level gets too low, i.e., if the water becomes too acidic. This partnership helps the water utility ensure it is getting clean water and also helps the ECZ monitor the acid levels in water.

Furthermore, ministries might consider partnering on areas of shared concern. South Africa formed an Inter-Ministerial Committee on acid mine drainage, which included personnel from the ministries of mineral resources, water affairs, science and technology, and national planning.<sup>123</sup> Forming a joint committee allows the different agencies to share information and to approach shared problems jointly and strategically.

### **Requiring Company Partnerships to Create Private Monitoring Incentives and Increase Government Access to Information**

Some governments have reported that requiring companies to form joint ventures has resulted in improved government monitoring. This approach has been used in the hydrocarbons sector in Angola, Norway, and Trinidad and Tobago.

In Trinidad and Tobago, the hydrocarbons sector had some ventures that were run by a single operator, while others were run by a primary operating company in conjunction with other nonoperating partner companies. The government noticed that the financial reports from joint ventures provided more comprehensive information than the reports from the single operator ventures, particularly on financial issues. The minority companies in the joint ventures demanded more information from the operating company in order to protect their own investment. This additional

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121 ArcelorMittal et al., *Agreement on Minimum Requirements for Plant Level Joint H&S Committees*, 2008, <http://www.imfmetal.org/files/08060311121679/AgreementArcelorMittalOHS.pdf>.

122 International Metalworkers’ Federation et al., *Together for Safety: Global Scope—Local Impact: Joint Global Health and Safety Committee Review Report*, 2011, [http://www.imfmetal.org/files/11081515505779/ArceloMittal\\_IMF\\_Report\\_HS\\_En.pdf](http://www.imfmetal.org/files/11081515505779/ArceloMittal_IMF_Report_HS_En.pdf).

123 “Inter ministerial committee report on acid mine drainage and mine water management in the Witwatersrand Goldfields,” *Environment*, Feb. 28, 2011, <http://www.environment.co.za/acid-mine-drainage-amd/inter-ministerial-committee-report-on-acid-mine-drainage-and-mine-water-management-in-the-witwatersrand-goldfields.html>.

information allowed the government to monitor the joint ventures' operations more closely. It also showed the government, which was relatively inexperienced in the hydrocarbons sector at the time, the kinds of information it might expect or demand of all the oil sector projects in the country. An additional benefit was that the nonoperating partners conducted their own monitoring of the venture's operating partner, helping to police and improve transfer pricing issues, even without the government's interventions. Because the minority partners wanted to ensure their investment was profitable, their incentive lined up with the government's incentive to ensure that the local venture was profitable.<sup>124</sup>

To help realize these improved monitoring benefits, the government established a joint venture in the late 1980s with three multinational companies. It selected the nonoperating partners for their experience in the sector and their ability to monitor and audit the operating partner. The companies shared the results of the audits with all partners in the venture, including the government.<sup>125</sup>

Having companies monitor operating partners in joint venture arrangements is not a substitute for careful, engaged government monitoring, but the experience of Trinidad and Tobago demonstrates that it can help strengthen government monitoring efforts. By requiring companies to form partnerships, the government aligned the minority partners' interests with its own. To reduce opportunities for companies to collude in such partnerships, governments can select the partner companies themselves rather than allowing the companies to select their own partners.

### Multi-Stakeholder Monitoring Partnerships

Multi-stakeholder monitoring partnerships have also been gaining ground in the extractive industries. These allow governments, companies and civil society to work together, and to share information and concerns to address issues jointly. Government, company and civil society actors offer different skill sets and access to different kinds of information, and multi-stakeholder partnerships can benefit from the sharing and collaboration that occurs among these diverse stakeholders.

Perhaps most notably, EITI requires implementing countries to constitute a multi-stakeholder group that includes members from government, companies and civil society. The group helps guide the implementation of the EITI process in the country, including determining what information

is included in EITI reporting templates and selecting the organization that reconciles the reports. More information on EITI is available in Appendix 3.

In 2010, the World Bank Institute, together with the World Bank Africa Region, convened a working group on contract monitoring. They have conducted multi-stakeholder workshops in West and East Africa to identify pilot projects to improve the monitoring of government contracts, including those in the extractive industries. Companies, government officials

and civil society advocates have all participated in these workshops. One of the pilot project ideas is a national public contract monitoring mechanism in Sierra Leone that would bring together government, media, civil society and companies to monitor and report on the implementation of mining projects. The project is projected to last three years.

*Having companies monitor operating partners in joint venture arrangements is not a substitute for careful, engaged government monitoring, but the experience of Trinidad and Tobago demonstrates that it can help strengthen government monitoring efforts.*

### 3.5 Local and Community Partnerships

Communities often have specific concerns when it comes to mining projects taking place near their homes. They will most often be interested in those aspects of the mining operations that have the largest direct impact on them, which typically includes the companies' social and environmental

<sup>124</sup> Neal Richardson, *Making Equity Work: Structuring State Ownership in the Mining Sector*, Revenue Watch Institute, 2010, 8-9.

<sup>125</sup> Richardson, 8-9.

obligations. Therefore, community monitoring partnerships tend to focus more on monitoring social and environmental commitments. Particularly with respect to these two areas, communities bring to a monitoring process the advantages of incentive and access. They have the incentive to monitor the operations that affect their lives and livelihoods. Their proximity to the mine gives them access to information about those operations: they can see whether mine construction is taking place or whether a school has been built, and they can walk to nearby water sources to observe and measure pollution levels.

Companies have long recognized the necessity of engaging with communities, building good relations, and obtaining their support. Increasingly, they recognize that these efforts must be linked with aspects of monitoring—ongoing processes to collect and exchange information, and to enable the community to voice concerns. For many, this is an essential element in efforts to mitigate tensions and prevent conflict.

There are a variety of ways in which community partnerships can meet monitoring needs:

- Companies can partner with communities to identify areas of concern to the community and to jointly monitor the companies' efforts to address those concerns.
- Governments can train community monitors to gather and pass along information that the government needs in order to effectively oversee companies' operations.
- Communities can independently monitor areas of concern and can report their findings to the company or government to seek to improve areas of noncompliance.

These three models are currently being used in Canada, Peru and Afghanistan, respectively. While the value of community monitoring is clear, it remains a delicate subject. As the World Resources Institute noted in a 2009 guide, "There are numerous examples of community engagement gone wrong or not existing at all. Companies and financial institutions are often hesitant to put forth their projects as examples of good practices because of the increased scrutiny that this attracts."<sup>126</sup> The examples below suggest possible avenues without underestimating the complexities involved in building trust and meeting the multiple concerns of a community.

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#### **Additional Resources:**

The International Council on Mining and Metals (ICMM) has developed the *Mining: Partnerships for Development Toolkit*, which provides a detailed methodology for evaluating the social and economic effects of mining projects.<sup>127</sup> It is a useful guide for companies and civil society advocates interested in exploring partnerships to monitor the impacts of mining. The toolkit urges partnerships and identifies the following six partnerships themes:

1. mining and poverty reduction
2. mining and economic development: revenue management
3. mining and economic development: regional development planning
4. mining and economic development: local content
5. mining and social investment
6. mining and dispute resolution

Another useful resource is the World Resources Institute's *Breaking Ground* report on community consultation. It includes recommendations for community consultation and contains a section on participatory monitoring by local communities.<sup>128</sup>

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### **Impact and Benefit Agreements in Canada**

Some mining companies in Canada have signed impact and benefit agreements (IBAs) with aboriginal communities surrounding mining sites. An IBA is a contractual agreement in which an aboriginal community consents to mining operations in its traditional territory, and a company

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<sup>126</sup> Kirk Herbertson et al., *Breaking Ground: Engaging Communities in Extractive and Infrastructure Projects*, World Resources Institute, 2009, 5, <http://www.wri.org/publication/breaking-ground-engaging-communities>.

<sup>127</sup> ICMM, *Mining: Partnerships for Development Toolkit*, 2011, [www.icmm.com/document/1945](http://www.icmm.com/document/1945).

<sup>128</sup> Herbertson et al.

makes commitments to the community in exchange for that consent. An IBA is separate from the permits and licenses the company must get from the government in order to conduct its mining operations; it is a private agreement between the community and the company.

The content of IBAs varies depending on what an individual community and company agree to, but typical provisions include economic incentives for the community (e.g., cash transfers or profit sharing arrangements) as well as commitments related to hiring local workers and contracting firms, education, environmental protection and cultural protection.

IBAs may also contain provisions addressing how implementation of the agreement will be monitored over time, or the parties may form a separate agreement related to monitoring the company's commitments in the area. For example, the Diavik diamond mining project in Canada's Northwest Territories included a socioeconomic monitoring agreement, which was signed by the company, the government and the affected aboriginal communities.<sup>129</sup> Under this agreement, the parties established an advisory board, which included representatives from the company, the Northwest Territories government and five aboriginal groups. The advisory board works together to monitor employment, training and other socioeconomic commitments.<sup>130</sup> Diavik releases annual reports indicating its compliance with the community agreements.<sup>131</sup>

The Diavik monitoring structure is an interesting model for other communities that want to partner more directly with mining companies in order to realize the benefits mining can bring to the area. The structure has encouraged more transparency around the company's social and economic commitments to the communities, and the advisory board structure has encouraged the partners to talk to each other. This model demonstrates that communities can become engaged partners in monitoring the implementation of commitments the mining company has made.

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#### Additional Resources on IBAs

- Ginger Gibson and Ciaran O'Faircheallaigh, *IBA Community Toolkit*, 2010, <http://www.ibacommunitytoolkit.ca/index.html>.
- Peter Siebenmorgen, "Developing an Ideal Mining Agenda: Impact and Benefit Agreements as Instruments of Community Development in Northern Ontario" (master's thesis, University of Guelph), 2009, <http://www.impactandbenefit.com/kr/One.aspx?objectId=10486936&contextId=677979&lastCat=10486919>.
- IBA Research Network, <http://www.impactandbenefit.com/home/>.

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### Social Monitoring in Azerbaijan

As part of its operations in Azerbaijan, British Petroleum (BP) established the Azerbaijan Social Review Commission (ASRC) to advise the oil company on its social performance within the country. The ASRC is made up of local and international academics and civil society leaders. They produce a report each year that addresses issues such as BP's operational impacts, community programs and engagement with Azerbaijan society. BP responds to each annual report. Both the ASRC reports and BP's responses are available via BP's website.<sup>132</sup> BP helps the ASRC make annual visits to the regions affected by the company's operations. This structure increases transparency in BP's operations and encourages civil society to act as an engaged partner in BP's operations in the area. BP's website also includes reports from national nongovernmental organizations (NGOs), along with the company's responses to each report.<sup>133</sup>

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129 A copy of the agreement is available online at <http://www.atns.net.au/agreement.asp?EntityID=1877>.

130 *Diavik Diamonds Project Socio-Economic Monitoring Agreement*, 1999, art. 2.1.2(c), <http://www.atns.net.au/agreement.asp?EntityID=1877>.

131 The reports are available at [http://www.diavik.ca/1131\\_reports\\_and\\_publications.asp](http://www.diavik.ca/1131_reports_and_publications.asp).

132 British Petroleum, "Azerbaijan Social Review Commission," <http://www.bp.com/genericarticle.do?categoryId=9006625&contentId=7037156>.

133 British Petroleum, "Monitoring by National NGOs," <http://www.bp.com/genericarticle.do?categoryId=9006625&contentId=7013552>.

## Participative Monitoring with Communities in Peru

Peru's experience with community monitoring demonstrates both the opportunities and the difficulties of establishing credible participative monitoring. Although its mining law includes provisions for community monitoring of environmental impacts, there are no details on how this should take place.<sup>134</sup> Social conflict has been a serious problem for mining throughout Peru. One recurrent issue has been the impact of mining on land use and, in particular, the quality and supply of water. Beginning in about 2000, there have been more than half a dozen significant multi-stakeholder initiatives to mediate disputes, identify sources of emerging conflict, and engage communities in ongoing monitoring.

A number of participative monitoring efforts have taken the form of a *mesa de dialogo* (table or platform for dialogue), and civil society, industry and some other stakeholders have participated. They all involve some combination of international and domestic NGOs working with companies and local communities. The Compliance Advisor/Ombudsman (CAO) of the International Finance Corporation (IFC) has been involved in some of these initiatives. While municipal governments have also been involved, the central and regional governments have played a much less significant role.

One of the most well-regarded mechanisms has been the *mesa de dialogo* of the Tintaya copper mine in the Cusco region.<sup>135</sup> The process was initiated by local NGOs acting through Oxfam Australia—based in the same country as the mine's initial owners, BHP Billiton, which later sold its share to Xstrata. Over the years, the mesa's committees have investigated and helped settle claims related to land, environment, human rights and sustainability. At the same time, the mesa has not erased tensions with the community. There have been periods of discord with the owners and eruptions of violence that have required intensive efforts to sustain the process. Nevertheless, the mesa survives with support from the company and active engagement from a range of community actors.

The story of community monitoring at the Yanacocha mine in Cajamarca has been more problematic. Yanacocha, one of the world's largest gold mines, is owned primarily by Newmont Mining Corp. The CAO became involved after receiving complaints from local community groups about the mining project, in which the IFC was a minority investor. From 2000 to 2006, the CAO worked through the *Mesa de Dialogo y Consenso-CAO Cajamarca* to mediate complaints and, increasingly, to implement a participative water monitoring project. But independent studies and interviews conducted for this report suggest that the company and the CAO never gained the community's trust, nor were they able to overcome suspicions about the integrity of water monitoring. The CAO ended its involvement in the mesa in 2006. Yanacocha's continued efforts to involve the community in monitoring and responding to water-related problems are now dismissed by local government and NGOs, who see it as an effort to co-opt rather than collaborate with the community. In addition to historical issues of mistrust, observers also note problems related to the monitoring itself: the absence of scientific rigor, limited access to sites around the mine and the absence of independent lab analysis.<sup>136</sup>

Community distrust has been the result of many factors, some of which were beyond the immediate control of the company. But it has been exacerbated by poor relations with the company. At the outset of Newmont's review of community relations, the company realized that it had failed

134 Peru, *Decreto Supremo* (Supreme Decree) No. 028-2008-EM, *Reglamento de Participación Ciudadana en el Sub Sector Minero* (Regulation of Citizen Participation in the Mining Sector); Peru, *Resolución Ministerial* (Ministerial Resolution) No. 304-2008-MEM/DM, *Aprueban Normas que regulan el Proceso de Participación Ciudadana en el Subsector Minero* (Approved Rules governing the Process of Public Participation in the Mining Sector).

135 Isabelle Anguelovski, "Understanding the Dynamics of Community Engagement of Corporations in Communities: The Iterative Relationship between Dialogue Processes and Local Protest at Tintaya Copper Mine in Peru," *Society and Natural Resources* 24 (2011): 384-99; Oxfam Australia, "Tintaya, Peru," <http://www.oxfam.org.au/explore/mining/our-work-with-communities/tintaya-peru>.

136 A number of these issues are addressed in the CAO's 2008 Advisory Note on participatory water monitoring, which draws on the CAO's experience in Cajamarca and seven other locations in Peru and elsewhere, although it does not discuss those experiences directly. Office of the Compliance Advisor/Ombudsman, *Participatory Water Monitoring: A Guide for Preventing and Managing Conflict*, 2008, <http://www.cao-ombudsman.org/howwework/advisor/documents/watermoneng.pdf>.

to keep track of its own commitments to the community.<sup>137</sup> The long-term situation in Cajamarca remains fraught, and a major source of social tension stems from the community's fear of environmental damage from expanded mining. Efforts to engage the community and monitor conditions remain urgent.

One lesson from these two experiences—which is noted both in the studies commissioned by Newmont and in the work of the CAO—is that building trust with the community is an essential element and can easily be undermined by external factors and the conduct of the company. Balancing community involvement with methodically convincing environmental analysis has been difficult as well.

### Community Infrastructure Monitoring in Afghanistan

Integrity Watch Afghanistan (IWA) has developed a community-based monitoring program to monitor reconstruction projects throughout the country. The program does not relate to mining, but it does demonstrate a possible community approach to monitoring the infrastructure components of some mining deals. It relies on volunteers from communities to gather information on reconstruction projects and to report back to the community, the construction company, local government and IWA on their findings.<sup>138</sup>

For example, in east Afghanistan's Nangahar Province, IWA trained two local people to monitor the construction of a new school building. They learned basic engineering standards, and IWA provided technical assistance to support the monitoring efforts. The Turkish International Cooperation and Development Agency (TIKA) was funding the construction and agreed to give the monitors access to the site. There, the monitors noticed two issues: electrical wires were not covered or protected, which would lead to increased maintenance costs, and the project used poor-quality bricks, thus reducing the life expectancy of the school by 80 percent. The monitors shared their findings with the project's head engineer, who was receptive. Even with limited training, these two community members were able to make suggestions that improved the standards of the building and contributed to the students' welfare.<sup>139</sup>

IWA's experience reflects the monitoring challenges addressed earlier in the report:

- *Capacity:* Even with a small amount of training, community members can make valuable contributions through their monitoring efforts.
- *Transparency:* TIKA's willingness to provide access to the construction site enabled the community monitoring efforts. Communities must be able to access information in order to monitor effectively.
- *Incentives:* Community members were willing to volunteer to monitor the construction projects because they had a vested interest in local development.

## 3.6 Enforcement and Advocacy Mechanisms

Government and civil society have a number of tools available to improve compliance when information obtained through monitoring efforts indicates that a company may not be fulfilling its obligations.

### Government Enforcement Mechanisms

Governments can enforce compliance through a variety of methods that range in severity from reporting noncompliance and ordering improvement up through revoking permits and filing criminal charges.

Penalties and sanctions against a company that is not abiding by the laws not only punish that individual company but also deter all companies from failing to comply in the future. A report by the U.S. Environmental Protection Agency (EPA) notes that penalties and sanctions “play an

137 Newmont Mining Corp., *Building Effective Community Relationships: Final Report of the Advisory Panel to Newmont's Community Relationships Review*, 2009, appendix 1E: Minera Yanachocha, Peru, <http://www.beyondthemine.com/2010/pdf/CRRAdvisoryPanel-EnglishFINAL.pdf>.

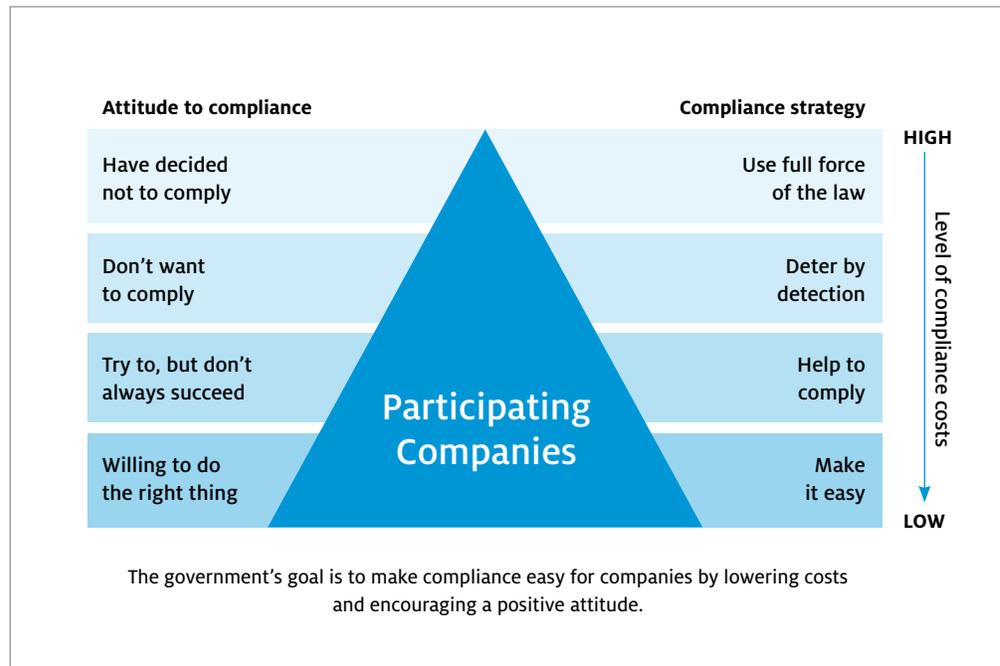
138 Integrity Watch Afghanistan, “Community Based Monitoring,” [http://www.iwaweb.org/community\\_based\\_monitoring.html](http://www.iwaweb.org/community_based_monitoring.html).

139 Integrity Watch Afghanistan, *Case Study: Community Mobilisation—Succeeding in Impacting Your Future*, 2011, <http://www.iwaweb.org/Doc/CBM/CaseStudies/CBM%20-%20CS11%20-%20Community%20Mobilisation.pdf>.

important role in an effective enforcement program by creating deterrence. Deterrence of non-compliance is achieved through: 1) a credible likelihood of detection of a violation, 2) a timely enforcement response, 3) the likelihood and appropriateness of the sanction, and 4) the perception of the first three factors within the regulated community.”<sup>140</sup>

Australia’s Taxation Office has developed a compliance model to help identify responses that are appropriate to the causes of noncompliance, the level of cooperation the agency receives, and the nature and level of risk involved (see Figure 7). As the model demonstrates, the taxation office uses more cooperative approaches with companies that are willing to pay their taxes and a more penal approach with companies that do not comply.

figure 7:  
Compliance Model



Source: Australian Government, *Large Businesses and Tax Compliance*, 2010, 6, <http://www.ato.gov.au/content/downloads/bus338o2nat8675o62o1o.pdf>.

Figure 7 illustrates how different approaches to enforcing laws, regulations and contracts against mining companies may differ depending on the company and the circumstances. It also illustrates that government’s goal is to encourage companies to move toward voluntary compliance.

### Review Company Reports and Assessments

Government agencies should review company reports and assessments to ensure the company’s self-reported information indicates compliance with its obligations and that assessments meet the country’s required standards.

Under Ontario’s mining act, companies must meet certain exploration expenditure targets in order to maintain their exploration claims in good standing, and they must submit assessment reports indicating their compliance with this requirement. The 2005 auditor general’s audit found that in 2004, the ministry received more than 1,000 assessment reports. Under the act, the ministry has 90 days to review each report and to reject any reported costs it deems invalid, or to request additional information. Reports not reviewed in that time frame are deemed to have been approved.

<sup>140</sup> Steven A. Herman, *Oversight of State and Local Penalty Assessments: Revisions to the Policy Framework for State/EPA Agreements*, U.S. Environmental Protection Agency, 1993, 1, [www.epa.gov/compliance/resources/policies/state/oversgt-penal-mem.pdf](http://www.epa.gov/compliance/resources/policies/state/oversgt-penal-mem.pdf).

The auditor general found that while most of the reports were reviewed within the 90-day time frame, typically 25 to 40 of them were approved each year without anyone reviewing them. In an audit of those reports, the auditor general found that several contained unreasonable costs or insufficient information to comply with legal requirements.<sup>141</sup> The following excerpt from the report provides recommendations to address these concerns:

- develop procedures to ensure that all assessment files are reviewed for reasonableness;
- review the adequacy of the number of files selected for detailed expenditure verification, and consider implementing a random selection process;
- assess whether the current level of inspections and prosecutions provides an effective deterrent to filing false information to retain mining rights; and
- consider disqualifying holders of forfeited claims from re-staking the same land until an appropriate period of time has passed.<sup>142</sup>

As the Ontario case demonstrates, deemed approvals can present a challenge for many countries, particularly when there are not enough staff to review reports within the allotted time frames. Many codes and regulations specify time frames within which company reports and assessments must be reviewed, and the documents are deemed to have been approved at the end of that period regardless of whether government officials have reviewed the reports. Deemed approval mechanisms help speed the process of granting new mining rights, and they can also reduce corruption in cases when government officials may have demanded payment in order to approve an application or to approve it within a reasonable time frame. However, they also create a risk that government officials will be unable to review some documents at all. The time frame must be adequate to allow officials to carefully review documents. For example, in the same Ontario audit, the auditor general noted that the ministry has just 45 days to review closure plans, “which is an extremely short time frame, given the complex nature of many closure plans and the numerous steps required to process these plans.”<sup>143</sup>

Report and assessment reviews are also important to ensure companies are adequately planning for the unique needs and risks of a particular project. In South Africa, the government reported that some prospecting work plans and even environmental impact assessments had clearly been copied and pasted from other mining projects: they referred to waterways, wildlife and geographical features that were not even present on the proposed mining site. Such bogus reports present serious risks if governments are unable to adequately assess the environmental and social risks or the likely mineral reserves implicated in the project. Anecdotal evidence indicates that other countries have received similarly bogus company reports.

Having companies report on themselves is useful to assist with a government’s monitoring efforts. However, it is only a first step in assuring compliance. Governments must also ensure that the reported information indicates compliance with a company’s obligations and that the reported information accurately reflects how operations are proceeding.

### ***Investigations***

Government investigations help assess whether a company is complying with its obligations in its ongoing operations at the mine. Government inspectors across disciplines—tax, occupational health and safety, and environment—should visit mining companies regularly to supervise their operations and to identify possible gaps in compliance.

There is no established guidance on how often mine sites should be inspected, but most sources recommend a regular schedule, ensuring each mine is inspected at least once during

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141 Office of the Auditor General of Ontario, 184-85.

142 Office of the Auditor General of Ontario, 186.

143 Office of the Auditor General of Ontario, 194.

a specified time frame. Some countries use a risk-based approach to determine how often particular mines should be inspected, visiting higher risk mines more frequently and lower risk mines less frequently.

Box 10 provides an excerpt from the auditor general of Ontario's audit of the Mines and Minerals Program, highlighting some of the key priorities for investigations of mine rehabilitation and closure activities.

**Box 10 | Excerpt from Office of the Auditor General of Ontario's Report on Investigations by the Province's Mines and Minerals Program**

We reviewed the Ministry's monitoring and inspection of ongoing mine-rehabilitation and mine-closure activities. . . . [W]e noted a number of areas where the monitoring and inspection process could be improved:

- A ministry report indicated that more than 200 inspections or site visits had been performed over the past five years. However, we noted that the Ministry's list of the work that had been done was neither accurate nor complete. An accurate list of inspections and site visits is a valuable tool to enable management to monitor overall inspection activity.
- The Ministry informed us that it attempts to inspect every site over a two-to-three-year period. We noted that, based on the information provided, almost half the sites had not been inspected in the past five years.
- The Ministry employed an informal risk-based approach to selecting mine sites for inspections. A more formal approach would ensure that all sites are inspected at least once over a specified time frame and that inspection efforts are directed to those sites that pose the greatest risk to public health and safety and the environment.
- Inspection documentation needs to be improved to demonstrate to ministry management that inspections have considered all the requirements of the Mine Rehabilitation Code. In addition, there was insufficient evidence that all the concerns noted during inspections were followed up on and resolved.<sup>144</sup>

The results of government investigations should be communicated to the company, with particular attention to areas of noncompliance. Governments should then conduct follow-up inspections to ensure areas of concern have been addressed.

In recognition of a failure to effectively monitor mining company compliance on a consistent and ongoing basis, some countries have recently announced or conducted mass industry-wide audits of mining permits to determine the state of compliance with laws. For example, Indonesia's finance minister announced in May 2011 that the country would audit more than 8,000 existing mining permits to ensure compliance with mining and environmental laws.<sup>145</sup> Timor-Leste has recently enhanced its scrutiny of foreign oil companies and discovered tens of millions of dollars in unpaid taxes. It has begun demanding back pay from a number of multinational corporations, including ConocoPhillips, Inpex and Santos.<sup>146</sup> These large-scale audits demonstrate recognition of deficiencies in existing monitoring structures and the dangers caused by a lack of monitoring. At the same time, they represent a commitment to improving monitoring and enforcement going forward. Audits in South Africa and the Philippines are discussed in Box 11.

<sup>144</sup> Office of the Auditor General of Ontario, 194.

<sup>145</sup> Rieka Rahadiana and Adriana Nina Kusuma, "Indonesia to review all existing mining permits as new mining regulations passed," *Mineweb*, May 23, 2011, <http://www.mineweb.com/mineweb/view/mineweb/en/page72068?oid=127699&sn=Detail&pid=110649>.

<sup>146</sup> "Making the Oil Companies Pay What They Owe," *La'o Hamutuk* (Timor-Leste Institute for Development Monitoring and Analysis), Dec. 10, 2010, <http://www.laohamutuk.org/Oil/tax/10BackTaxes.htm>.

### South Africa

In 2010, South Africa’s Minister of Natural Resources Susan Shabangu issued a moratorium on new applications for prospecting rights in order to conduct a massive audit of all prospecting rights granted since South Africa’s MPRDA took effect in 2002.<sup>147</sup> The audit uncovered a series of challenges in the granting of rights and in the ongoing monitoring and management of mining activities, including an “inability to conduct proper compliance inspections to ensure compliance with undertakings and commitments of right holders” and an “increase in complaints from communities arising in part from the failure by some mining companies to implement their Social and Labour Plan commitments.”<sup>148</sup>

Preliminary results of the audit found:

- Companies that were not complying with their obligations to begin prospecting activities within 120 days.
- Applicants who were not serious about mining and did not even know where their rights were geographically located.
- Applicants who had engaged in extensive drilling without amending their work programs or financial provisions, thus exposing the government to increased financial risk.
- Occurrences of illegal drilling, leading to increased hazards to communities and landowners.<sup>149</sup>

The DMR indicated that it would notify rights holders of cases of noncompliance and would follow procedures to cancel rights in those cases.<sup>150</sup>

In March 2011, Minister Shabangu discussed the ongoing reform efforts within the DMR and highlighted the following areas that require attention:<sup>151</sup>

- Clarifying the consultation process that must take place before applicants can submit applications for mineral rights and before the DMR can grant such rights.
- Streamlining of the application process, including through the launch of an online cadastre system.
- Strengthening provisions that sanction noncompliance.
- Strengthening provisions to improve working conditions.

### The Philippines

In January 2011, the government of the Philippines suspended all large-scale mining applications while the government reviews pending and inactive mining claims. The government’s new Environment and Natural Resources Secretary Ramon Paje promised to “clean the process of mining claims.” He quickly ordered all regional directors of the Mines and Geosciences Bureau to stop accepting and processing new mining applications. He also began canceling existing permits.<sup>152</sup>

At the time of Paje’s accession, there were 2,800 mining claims. After immediately canceling about 500 permits that were inactive or incomplete, he set deadlines for regional officials of Feb. 20, 2011, to “cleanse” their regions of 50 percent of pending and inactive mining applications, and December 2011 to cleanse the remaining 50 percent. This first deadline was met: 1,150 mining applications

*Continued on next page*

147 South Africa, Department of Mineral Resources, “Minister Susan Shabangu’s Statement on the New Electronic Mineral Management System and Its Implications for the Regulatory Environment,” Feb. 7, 2011, [http://www.dmr.gov.za/Media\\_Room/Documents/Speeches/Speech%20Mining%20Indaba%20Online%20Apps.docx](http://www.dmr.gov.za/Media_Room/Documents/Speeches/Speech%20Mining%20Indaba%20Online%20Apps.docx).

148 South Africa, Department of Mineral Resources, “Address by the Minister of Mineral Resources, Ms Susan Shabangu, MP,” Nov. 2, 2010, [http://www.dmr.gov.za/Media\\_Room/MINISTRY%20OF%20MINERAL%20RESOURCES.docx%20Website%20speech.docx](http://www.dmr.gov.za/Media_Room/MINISTRY%20OF%20MINERAL%20RESOURCES.docx%20Website%20speech.docx).

149 South Africa, Department of Mineral Resources, “Address by the Minister of Mineral Resources, Ms Susan Shabangu, MP.”

150 South Africa, Department of Mineral Resources, “Address by the Minister of Mineral Resources, Ms Susan Shabangu, MP.”

151 André Janse van Vuuren, “Shabangu responds to Fraser findings,” *Miningmx*, March 8, 2011, <http://www.miningmx.com/news/markets/Shabangu-responds-to-Fraser-findings.htm>.

152 Philippines Department of Environment and Natural Resources, “DENR Suspends Issuance of New Mining Permits” (press release), Feb. 28, 2011, <http://www.gov.ph/2011/02/18/denr-suspends-issuance-of-new-mining-permits-2/>.

Box 11, continued from previous page

were reviewed, and more than 900 were rejected or disapproved. Around 250 were approved.<sup>153</sup>In addition to pending mining applications, Secretary Paje also said the Mines and Geosciences Bureau would be looking at exploration contracts that expired more than five years ago, mining contracts whose three-year work programs have not been implemented for two consecutive years, as well as mineral production sharing agreements, industrial sand and gravel permits, and financial and technical assistance projects.<sup>154</sup>

In March 2011 the Department of Environment and Natural Resources (DENR) announced that an applicant for a small-scale mining agreement could face criminal and administrative charges for conducting mining operations while his or her permit application was still pending.<sup>155</sup>

These measures constitute part of the government's new "use it or lose it" policy—which in turn is a part of general reforms that the DENR started using in earnest in 2010.<sup>156</sup> The second impetus behind these measures is that the government has also become increasingly concerned about cleaning up its image, which is perceived as corrupt and bureaucratic.<sup>157</sup> Under the policy, the department seeks to cancel mining applications that do not comply with government requirements, including projects that have remained inactive and unproductive or that do not acquire free, prior and informed consent (FPIC) from indigenous groups. Another measure includes designating a senior official to head the Internal Audit and Anti-Corruption Office, to strengthen the DENR's anti-corruption program.<sup>158</sup>

### Fines

Fines serve as sanctions against companies that do not comply with their obligations. Fines also have a deterrent effect—companies are more likely to comply if they risk being fined for noncompliance. The U.S. EPA recommends that fines should be fair and proportionate to the offense and should, at a minimum, recover "the economic benefit of noncompliance plus some appreciable portion reflecting the gravity of the violation."<sup>159</sup>

In the 2011 revisions to Zambia's Environmental Management Act, the country's ECZ revised the scale of fines for exceeding permissible emissions. Under the old system, a company would pay a single flat fine for exceeding permissible emissions, regardless of whether it exceeded the limit by a very small or very large amount. Under the new system, fines will be based on the amount of overage.

Enforcing tax laws relies heavily on the extent to which penalties are levied for evasion or fraud. For failure to file returns or pay taxes on time, the most common penalty is a fine. Failure to correctly report tax liabilities incurs penalties that vary according to the seriousness of the infraction. The United Kingdom, for example, has a range of penalties: "careless" errors range from 0 to 30 percent of the amount evaded; "deliberate and concealed" mis-reporting ranges from 30 to 100 percent. Some countries have criminal penalties as well.<sup>160</sup>

153 Philippines Department of Environment and Natural Resources, "Paje Reports Initial Success in Cleaning Pending Mining Applications" (press release), March 28, 2011, <http://www.denr.gov.ph/index.php/news-and-features/latest-news/113-paje-reports-initial-success-in-cleansing-pending-mining-applications-.html>.

154 Philippines Department of Environment and Natural Resources, "DENR suspends issuance of new mining permits"; Kristine L. Alave, "DENR starts purge of mine applications," *Philippine Daily Inquirer*, Feb. 19, 2011, <http://newsinfo.inquirer.net/breakingnews/regions/view/20110219-321117/DENR-starts-purge-of-mine-applications>.

155 U.S. News Agency/Asian, "Small-scale mining applicant under fire in Ilocos Norte," *U.S. News Las Vegas*, March 22, 2011, <http://www.usnews.com/provincial/%EF%BB%BFsmall-scale-mining-applicant-under-fire-in-ilocos-norte/>.

156 Some of the other measures are protecting investments, industrializing industry, streamlining the permitting system, engaging in proactive information campaigns, promoting transparency in government transactions and establishing a proactive public-private partnership. Ricardo Fian, "Mining Reforms in the Philippines," Philippines Department of Energy and Natural Resources, 2010, <http://www.denr.gov.ph/index.php/news-and-features/features/15-mining-reforms-in-the-philippines.html>.

157 Alave; Michael Punongbayan, "DENR: 903 mining applications junked," *Philippine Star*, March 28, 2011, <http://www.philstar.com/Article.aspx?articleId=670481&publicationSubCategoryId=63>.

158 Philippines Department of Environment and Natural Resources, "Paje Fortifies Anti-Corruption Program in DENR" (press release), March 31, 2011, <http://www.denr.gov.ph/index.php/news-and-features/latest-news/121-paje-fortifies-anti-corruption-program-in-denr.html>.

159 Herman, 3.

160 Forum on Tax Administration, 2009, 128-29, 143, 145.

In enforcing revenue laws, many countries allow some flexibility to take the unique challenges of the mining industry into account, particularly in the payment of royalties. Many mining projects have a negative cash flow during the early phases because mining requires large upfront investments well before mineral production begins. It takes time for the revenues from mining to repay those initial costs. Because royalties are typically assessed based on mineral production, rather than a company's profits, companies may owe royalties even before they earn a profit. Paying royalties can thus be a challenge and may lead to insolvency. To combat this challenge, tax regimes in some African countries, and also developed countries like Australia, allow companies to defer royalties. Some nations, like Ghana, even allow for special royalty regimes for extraordinary investments.<sup>161</sup>

### **Mine Shutdowns**

Countries are increasingly introducing or strengthening enforcement sanctions that allow them to close mines that present an unacceptable level of risk, particularly for workers.

A new mining law in Queensland, Australia, allows enforcement officials to seek injunctions from the district court in cases of actual or attempted violations of worker safety laws. The injunctions allow the government to shut down mining operations until the risks have been addressed.<sup>162</sup>

South Africa's inspectors have also used work stoppages to address worker safety issues. In 2009, they ordered AngloGold Ashanti to suspend sections of their operations 44 times and Anglo-Platinum 61 times.<sup>163</sup>

In the United States, the Mine Improvement and New Emergency Response Act (MINER Act) of 2006 reintroduced a long dormant enforcement practice—use of “pattern of violations”—whereby the Mine Safety and Health Administration evaluates mines twice a year to determine if a mine should be placed on a pattern review process. If a mine has a pattern of violations, it enters into a 90-day probation period and must develop a plan to address identified risks and lower its violations. Any violations of mandatory standards within 90 days of the notice result in closing that area of the mine until the violation has abated.<sup>164</sup>

### **Criminal Charges**

In cases of severe legal violations, countries may also seek criminal charges against company officials. These cases tend to arise most often for violations related to the environment or health and safety, and only apply for particularly egregious violations.

Authorities in Honduras filed criminal charges against two senior officials of a mining company, Entremares, for water contamination and environmental damage. A local stream contained high acidity and dangerous levels of metal contamination. The officials could face up to six years in prison if they are found guilty of the charges, which were filed under Article 181 of Honduras's criminal code. Authorities also filed charges against a former senior official in the Honduran Department for the Administration of Mineral Resources for breach of official duties for failing to act on evidence of pollution. These charges were filed under Article 349 of the criminal code and could result in up to three years along with disqualification from public office. The criminal charges reportedly stemmed from information gathered by CAFOD, a Catholic aid agency in England and Wales.<sup>165</sup>

The U.S. Justice Department is conducting a criminal investigation of officials at Massey Energy. The company was found to have kept two sets of books on safety conditions at its mining site. One set reflected the true safety conditions and was used for internal mine management, while the other set was for federal inspectors and had been sanitized to reduce scrutiny of known safety

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<sup>161</sup> Otto et al., 76.

<sup>162</sup> McCullough Robertson, “Queensland Mining Safety Legislation Update—Systems, Penalty and Administration Changes,” *Resources*, Dec. 22, 2010, <http://www.mccullough.com.au/publications/publications.aspx?p=47&itm=3060>.

<sup>163</sup> Jeffrey Sparshott, “Mine safety shutdowns fuel tensions in South Africa,” *Wall Street Journal*, March 11, 2010.

<sup>164</sup> Mark E. Heath and Timothy D. Houston, “Increased Enforcement and Higher Penalties Under the MINER Act: Do They Improve Worker Safety?” *Energy & Mineral Law Foundation* 30 (2009): chap. 10.

<sup>165</sup> Indigenous Peoples Issues & Resources, “Goldcorp Staff Face Criminal Charges Over Mine Pollution After CAFOD Investigation,” Aug. 16, 2010, [http://indigenouspeoplesissues.com/index.php?option=com\\_content&view=article&id=6301:goldcorp-staff-face-criminal-charges-over-mine-pollution-after-cafod-investigation&catid=60:central-american-and-caribbean-indigenous-peoples&Itemid=82](http://indigenouspeoplesissues.com/index.php?option=com_content&view=article&id=6301:goldcorp-staff-face-criminal-charges-over-mine-pollution-after-cafod-investigation&catid=60:central-american-and-caribbean-indigenous-peoples&Itemid=82).

issues.<sup>166</sup> An explosion at the mine in April 2010 killed 29 people, and some of the safety risks that had been removed from the records provided to federal inspectors are believed to have contributed to the explosion.<sup>167</sup>

### ***Revocation of License***

Governments can revoke mining licenses in some instances. When a company holds a prospecting or exploration license but fails to comply with operational and production requirements, the government often reserves the right to revoke that company's license. Provisions granting the government the right to revoke in such instances are sometimes referred to as "use it or lose it" provisions. In the examples from South Africa and Philippines discussed in Box 11, the governments revoked licenses after audits identified companies that had not complied with their legal requirements.

### **Civil Society Advocacy Mechanisms**

Although civil society groups are unable to revoke mining rights or assess fines like government agencies can, they have several paths available to pursue accountability. Civil society advocacy mechanisms can be broadly divided into the following categories:

- Working through government mechanisms to improve enforcement of laws, regulations and contracts
- Leveraging public opinion and company reputational concerns to improve compliance

### ***Company Grievance Mechanisms***

More and more companies are beginning to provide grievance mechanisms through which communities can raise concerns directly with the company itself. When these mechanisms exist, they are a useful first step for engaging directly with companies to resolve issues. For example, Newmont Mining Co. has established a grievance mechanism for its Ahafo South Project in Ghana. The project involved resettling communities and individuals affected by the mining project, and the grievance mechanism was developed to resolve issues around resettlement and compensation. The mechanism allows for different levels of procedure, depending on the complexity of a complaint.<sup>168</sup>

More information on company grievance mechanisms is available from BASESwiki at [http://baseswiki.org/en/Main\\_Page](http://baseswiki.org/en/Main_Page).

### ***Complaints to Parliament/Government***

When civil society advocates identify areas of noncompliance, sharing that information with the government agencies responsible for enforcing the companies' obligations allows those agencies to conduct independent investigations and to sanction the companies when appropriate. When government officials are not responsive, citizens can also complain to their members of parliament, who may be able to provide a voice for citizens' concerns and/or question the executive branch's management of the sector.

### ***Third-Party Suit***

Taking companies or government agencies to court may be another method of working to improve company and government accountability. Because court cases tend to be adversarial and very expensive, litigation is typically a last effort after other advocacy mechanisms have failed. However, some advocates have successfully used the courts to seek better management of their countries' mining sectors.

A group of Canadian organizations won a case against the federal government in 2011. It had been refusing to conduct comprehensive environmental assessments of some large mining

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<sup>166</sup> Tim Huber and Vicki Smith, "Feds show fake safety records in W.Va. mine blast," *Washington Times*, June 29, 2011, <http://www.washingtontimes.com/news/2011/jun/29/feds-fake-safety-records-west-virginia-mine-blast/>.

<sup>167</sup> Howard Berkes, "Officials: W.Va. mine operator kept two sets of safety records," *National Public Radio*, June 29, 2011, <http://www.npr.org/blogs/thetwo-way/2011/06/29/137493009/w-va-mine-operator-kept-two-sets-of-safety-records-investigators-say>.

<sup>168</sup> Business and Society Exploring Solutions (BASES) wiki, "Ahafo South Project, Newmont Mining Corporation, Ghana," [http://baseswiki.org/en/Ahafo\\_South\\_Project\\_Newmont\\_Mining\\_Corporation\\_Ghana](http://baseswiki.org/en/Ahafo_South_Project_Newmont_Mining_Corporation_Ghana).

projects. The Supreme Court of Canada found that the government's actions violated the Canadian Environmental Assessment Act.<sup>169</sup>

In Papua New Guinea, a 2011 court decision ordered a Malaysian logging company to pay 225.5 million kina (\$97 million) to four tribes for massive environmental damage caused by illegal logging. An environmental group, Centre for Environmental Law and Community Rights, represented the tribes in court. The decision was based on statements from tribe members and expert evidence presented by three environmental scientists who conducted audits in the affected areas. The judgment reportedly compensated the tribes for trespass, loss of trees and breach of constitutional rights.<sup>170</sup>

Other recent cases have yet to be decided but demonstrate how some groups have chosen to use the courts to enforce their country's laws. A group of Armenian ecologists recently sued their government for failing to prevent a mining company from dumping polluted waste into a river.<sup>171</sup> In Chile, 31 of the 33 miners who spent 69 days trapped underground after a mine collapse have sued Chile's National Geology and Mines Bureau for negligence, alleging that the government agency did not conduct proper safety inspections of the mine.<sup>172</sup>

### **Media Coverage**

Civil society groups have long used the media to educate the public about the extractive industries and related governance concerns, and to encourage better compliance and accountability. Most large multinational mining companies are conscious of their reputations, and continuing media coverage of mining projects can be an effective tool in encouraging compliance. The coverage also helps educate other citizens about mining sector management within the country, which allows citizens to better hold their governments accountable for good governance. Civil society advocates can develop their own reports to share information obtained through monitoring efforts, and they can develop press releases and work with journalists to help publicize the information.

### **Complaints to Home Governments—Anticorruption Laws**

Many countries that are home to a large number of mining companies have laws that can be used to combat corruption. Laws on the books in the United States, Canada, the United Kingdom and Australia may provide additional checks beyond host countries' anticorruption laws.

#### ***The U.S. Foreign Corrupt Practices Act (FCPA)***

The FCPA has two main sets of provisions. The first are the anti-bribery provisions that forbid companies or any intermediaries or subsidiaries from offering anything of value to a "government official" for the purpose of obtaining an "improper advantage." The second are the accounting provisions. Under these, companies must maintain accurate books and records that reflect transactions with government officials. Moreover, they must maintain a sufficient system of internal oversight over these transactions.<sup>173</sup>

The law applies to both foreign and domestic companies. For example, in 2008 Siemens AG settled with the U.S. Department of Justice, the U.S. Securities and Exchange Commission and German authorities, agreeing to pay penalties of \$1.6 billion for bribing government officials to win contracts and for improperly characterizing those payments on its books.<sup>174</sup> Half of the total amount, \$800 million, was attributable to violations of the FCPA.

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169 Ecojustice, MiningWatch Canada and Canadian Environmental Law Association, "Supreme Court of Canada gives public a voice on major industrial projects—Court ensures meaningful environmental assessments across country," Jan. 21, 2010, <http://www.miningwatch.ca/en/supreme-court-canada-gives-public-voice-major-industrial-projects-court-ensures-meaningful-environme>.

170 Harlyne Joku, "Asian logging firm fined K225.5m," *Papua New Guinea Post-Courier Online*, June 23, 2011, <http://www.postcourier.com.pg/20110623/news.htm>.

171 Ararat Davtyan, "Ecologists take ministry to court over polluted river," *Armtown.com*, Feb. 24, 2011, <http://www.armtown.com/news/en/htq/20110224/2011022411/>.

172 Kosich.

173 PricewaterhouseCoopers, "The US Foreign Corrupt Practices Act—What Canadian Directors Need to Know," 2011, <http://www.pwc.com/ca/en/directorconnect/foreign-corrupt-practices-act.jhtml>.

174 "Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations and Agree to Pay \$450 Million in Combined Criminal Fines" (press release), U.S. Department of Justice, Dec. 15, 2008, <http://www.justice.gov/opa/pr/2008/December/08-crm-1105.html>.

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Enforcement of the statute has increased in recent years. In 2009, Mark Mendelsohn, the U.S. Department of Justice's deputy chief prosecutor responsible for FCPA cases, said that the all-time high level of enforcement would remain in place.<sup>175</sup>

#### ***Canada's Corruption of Foreign Public Officials Act (CFPOA)***

The CFPOA forbids bribing foreign public officials. Although it was infrequently used in its first decade, enforcement has picked up; there are now 23 ongoing investigations of violations of the CFPOA.<sup>176</sup> In one case, a number of NGOs have submitted a complaint against Blackfire Exploration for acts the mining company and its Mexican subsidiary committed in Mexico.<sup>177</sup>

Penalties for violating the CFPOA are stiff. The act can only be enforced through criminal sanctions, which can be up to five years in prison for an individual.<sup>178</sup> There is also no legal limit on the amount of fines, which are left to the court's discretion. Nor is there a statute of limitations on when actions can be brought. Finally, companies can be ordered to forfeit all profits and proceeds from the transaction.

#### ***The UK Bribery Act***

The Bribery Act took effect in July 2011. The law replaces England's old and often-criticized bribery laws. The law is similar to those in the United States and Canada, and includes liability for corporations that fail to prevent bribery and corruption of foreign officials.<sup>179</sup> The offenses can be prosecuted if they have been conducted by British nationals or corporations, or by those who are ordinarily UK residents, regardless of where the act took place. This includes third-party contractors.<sup>180</sup> Moreover, it applies to any corporation that has a business presence in the country, regardless of where the bribe is paid or where the company is based. Penalties can be quite severe. The act allows judges to impose criminal penalties, with jail time of up to 10 years and an unlimited fine.<sup>181</sup>

#### ***Australia's Bribery of Foreign Public Officials Act***

Australia's version of anti-bribery legislation is a recent amendment to the criminal code, which includes the offense of bribing a foreign public official. Under the statute, a corporation can be held criminally liable for bribery, or even for failing to create and maintain a culture that requires compliance with the law.<sup>182</sup> "Bribery" and "foreign public official" are defined broadly, as in other home countries' anticorruption legislation. The maximum penalty for an individual is up to 10 years in prison and up to \$1 million in fines. A corporation can be liable for \$11 million, or three times the value of the benefit obtained from committing the offense, whichever is greater.<sup>183</sup> The act covers Australian individuals or corporations.<sup>184</sup>

#### ***Human Rights Complaint Mechanisms***

In addition to the legal and contractual obligations discussed throughout this report, companies

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175 PricewaterhouseCoopers.

176 "With 23 RCMP Corruption Investigations Underway, Corporations Will Welcome TI Canada's Anti-Corruption Compliance Checklist" (press release), Transparency International Canada, Jan. 31, 2011, [http://www.transparency.ca/New/Files/TI-Canada\\_Anti-Corruption\\_Compliance\\_Checklist-Press\\_Release.pdf](http://www.transparency.ca/New/Files/TI-Canada_Anti-Corruption_Compliance_Checklist-Press_Release.pdf).

177 MiningWatch Canada, "Corruption and Oppression in Chiapas, Mexico," July 18, 2010, <http://www.miningwatch.ca/en/corruption-and-oppression-chiapas-mexico>.

178 Mark Morrison et al., "Canada's Corruption of Foreign Public Officials Act: What You Need to Know and Why," Blakes, 2009, [http://www.blakes.com/english/view\\_disc.asp?ID=3437](http://www.blakes.com/english/view_disc.asp?ID=3437).

179 Aron Chakrabarti et al., "UK Bribery Act 2010," Allan & Overy, 2011, <http://www.allenoverly.com/AOWEB/Knowledge/Editorial.aspx?contentTypeID=1&itemID=55579&prefLangID=410>.

180 Richard Orange, "Britain's new Bribery Act will encourage firms to avoid the London Stock Exchange," *Telegraph*, Sept. 20, 2010, <http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/8012137/Britains-new-Bribery-Act-will-encourage-firms-to-avoid-London-Stock-Exchange.html>.

181 Chakrabarti et al.

182 Gayle Hill, *Australian Laws Prohibiting Foreign Bribery*, Transparency International Australia, 2000, <http://www.transparency.org.au/documents/Australian%20Laws%20Prohibiting%20Foreign%20Bribery.pdf>.

183 Ernst & Young, *Upping the Ante: Bribery and Corruption Back on the Agenda*, 2010, [http://www.ey.com/Publication/vwLUAssets/Upping\\_the\\_ante/\\$FILE/Upping\\_the\\_ante\\_Bribery\\_corruption.pdf](http://www.ey.com/Publication/vwLUAssets/Upping_the_ante/$FILE/Upping_the_ante_Bribery_corruption.pdf).

184 Brett Cowell, "Bribery of Foreign Officials," CowellClarke, 2010, <http://www.cowellclarke.com.au/docfiles/Bribery%20of%20Foreign%20Officials%20April%202010.pdf>.

and governments also have obligations with regard to international human rights. Mining operations often raise serious human rights concerns, particularly related to community consultation, forced relocation and the use of private security forces. While this report generally does not focus on human rights obligations of mining companies and is not intended as a comprehensive guide to human rights complaint mechanisms, the following pages present some of the international mechanisms most relevant to communities affected by mining: the OECD's Guidelines for Multinational Enterprises, the Voluntary Principles on Security and Human Rights, and International Labour Organization (ILO) Convention 169, the Indigenous and Tribal Peoples Convention.

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**Additional Resource:**

More information on human rights recourse mechanisms is available in a recent guidebook from the International Federation for Human Rights (FIDH).<sup>185</sup>

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**OECD**

The OECD is an international forum for governments to work together to promote global economic and social well-being. It has created a set of Guidelines for Multinational Enterprises covering areas such as the environment, bribery, employment and human rights, and has helped establish a set of National Contact Points (NCPs) to hear complaints related to the implementation of the guidelines in specific cases.<sup>186</sup> OECD Watch is a network of civil society organizations that may be able to provide support to communities or civil society activists interested in using the OECD guidelines in their work.<sup>187</sup> Groups have used them to address concerns related to community relocation and tax evasion at MCM in Zambia, and groups in Argentina recently filed a case regarding environmental pollution at a mine operated by the Canadian company Barrick Gold Corp.<sup>188</sup>

**Community Relocation**

In 2001, Oxfam Canada and the Zambian NGO DECOP filed a complaint with Canada's NCP against MCM regarding the company's eviction of squatter communities that had been using land on the mining concession for small-scale farming. Zambia's mines had historically been owned by the state through Zambia Consolidated Copper Mines Ltd., and the state company had been allowing former workers to farm the land. However, the country's mines were privatized in the late 1990s and early 2000s, and the Mopani mine became jointly owned by First Quantum Minerals, a Canadian company, and Glencore International, a Swiss company. When they took over, they began evicting the farmers.<sup>189</sup>

Canada's NCP organized in-person meetings among Oxfam, local Zambian NGOs and First Quantum to discuss the complaint. The mining company promised to stop the evictions, to continue working with DECOP and the local council to identify a long-term solution, and to continue working with civil society.<sup>190</sup>

**Tax Evasion**

A government-commissioned private audit in 2010 found that MCM was evading its tax obligations in Zambia.<sup>191</sup> The audit, which was leaked to the public, sparked outrage among civil society groups.<sup>192</sup> In 2011, a group of five NGOs filed a complaint with the Canadian and Swiss NCPs against

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185 FIDH, *Corporate Accountability for Human Rights Abuses: A Guide for Victims and NGOs on Recourse Mechanisms*, 2010, <http://www.fidh.org/Corporate-Accountability-for-Human-Rights-Abuses>.

186 For more information on the OECD guidelines and the available complaint mechanisms, see FIDH, sec. III.

187 OECD Watch, <http://oecdwatch.org/>.

188 OECD Watch, "Environmental Pollution at Barrick's Gold Mines in Argentina," [http://oecdwatch.org/cases/Case\\_221/@@casesearchview?type=Issue&search=en\\_Environmental%20pollution%20at%20Barrick%E2%80%99s%20gold%20mines%20in%20Argentina](http://oecdwatch.org/cases/Case_221/@@casesearchview?type=Issue&search=en_Environmental%20pollution%20at%20Barrick%E2%80%99s%20gold%20mines%20in%20Argentina). The complaint was filed June 9, 2011.

189 OECD Watch, "Oxfam Canada vs. First Quantum Mining," [http://oecdwatch.org/cases/Case\\_19](http://oecdwatch.org/cases/Case_19).

190 OECD Watch, "Oxfam Canada vs. First Quantum Mining."

191 Grant Thornton and Econ Pöyry. The audit is discussed in more detail in Section 3.4 of this report.

192 OECD Watch, "Sherpa et al vs. Glencore International AG," [http://oecdwatch.org/cases/Case\\_208](http://oecdwatch.org/cases/Case_208).

Glencore and First Quantum. The complaint alleged tax evasion at MCM and used the private audit to support its claims. The complainants are awaiting the NCPs' initial assessment.

### ***Security Forces and Human Rights***

The use of security forces at mining sites has raised concerns regarding violence and human rights violations. For example, a recent Human Rights Watch (HRW) report details staggering human rights abuses in the Porgera gold mine in Papua New Guinea, owned by Barrick Gold Corp. The private security forces that Barrick hired were responsible for grave abuses, including gang rape, murder and violent abuse of artisanal miners.<sup>193</sup>

Civil society in the country had not been able to draw attention to the human rights abuses at Porgera, nor were they able to get the mining company and the government to act. When HRW began conducting field research for its report, however, Barrick was open and receptive to the researchers, with whom they "carried on a sustained dialogue."<sup>194</sup> Pressured by the pending HRW report and concerned about its international image, Barrick aligned itself with international norms like the Voluntary Principles on Security and Human Rights (VPs) in 2010. It also dismissed the employees linked to the human rights abuses.

The VPs give the extractive industry guidance on using security forces properly and outline general human rights obligations. Companies and governments can sign on the VPs, which means that they agree to support the principles and report annually to the international steering committee on their efforts to implement them. So far 18 extractive companies have done so, including Barrick, Rio Tinto Group, Newmont and AngloGold Ashanti. By signing on to the principles, a company:

- recognizes its international human rights obligations, including the Universal Declaration of Human Rights
- commits to abide by domestic laws
- commits to meaningful engagement with civil society

The VPs address both public and private security forces and recommend that mining companies incorporate the VPs directly into contracts with private ones. The obligations contained in the VPs fall into three main categories: risk assessment, relations with public security and relations with private security. Some of the relevant VP obligations include:

- committing to ensuring that private security forces will abide by international laws and obligations
- instituting monitoring mechanisms for private security forces or hiring a third party to do so
- creating mechanisms for investigating human rights complaints and recording all human rights abuses

When companies and/or governments that have signed on to the VPs appear to be violating them, the steering committee can revoke membership. This is likely to generate national and international attention. When companies and/or governments have not yet signed on, civil society advocacy encouraging them to join may be productive.

### ***Community Consultation and Consent Requirements***

Because community consultation and consent are complex and developing areas of international practice, activists interested in pursuing claims regarding lack of proper consultation or consent should research the relevant laws and precedents within their countries. This section provides general information on how FPIC can be and has been defended in courts, with a focus on Latin America.<sup>195</sup>

<sup>193</sup> Human Rights Watch, *Gold's Costly Dividend: Human Rights Impacts of Papua New Guinea's Porgera Gold Mine*, 2011, <http://www.hrw.org/en/reports/2011/02/01/gold-s-costly-dividend-0>.

<sup>194</sup> Human Rights Watch, 10.

<sup>195</sup> Jurisprudence from this region represents the most extensive enforcement of these rights by domestic courts and regional human rights bodies. The ILO has compiled a comprehensive casebook on the region's jurisprudence in *Application of Convention No. 169 by Domestic and International Courts in Latin America*, 2009, [http://www.ilo.org/wcmsp5/groups/public/---ed\\_norm/---normes/documents/publication/wcms\\_123946.pdf](http://www.ilo.org/wcmsp5/groups/public/---ed_norm/---normes/documents/publication/wcms_123946.pdf).

FPIC is a widely recognized principle that gives some communities the right to consent before certain types of activity can take place on their land. It is recognized in national and international law, and FPIC violations are actionable in domestic and international forums through a wide range of actions, including actions for the protection of constitutional rights, claims of unconstitutionality and actions in administrative, civil and criminal proceedings. Such suits can be brought by the affected indigenous or tribal community, its members or representatives, as well as by ombudsmen and domestic human rights institutions. They can also be brought before regional human rights bodies.

The following cases provide examples of how communities have successfully challenged their right to prior consultation and FPIC:

- *Colombia—consultation required prior to grant of environmental license:* In 2009 communities filed suit against several government ministries for violation of their collective right to consultation prior to mining exploration activities. The Constitutional Court found that the Muriel Mining Corporation had not conducted appropriate consultation on the environmental and cultural impact of the mines. It ordered the company to suspend all activity until it could hold new consultations after conducting environmental impact studies.<sup>196</sup>
- *Ecuador—constitutional right to prior consultation upheld despite absence of implementing regulations:* The ombudsman brought a lawsuit in 2002 regarding the protection of communities' constitutional rights to consultation prior to the grant of a mining concession. The Constitutional Court suspended the challenged concession, holding that the state as signatory to ILO Convention No. 169 must establish consultation procedures to assess the effects of the exploitation of resources on the lands of these communities.<sup>197</sup> It also upheld the constitutional right to consultation even in the absence of implementing regulations.<sup>198</sup>
- *Ecuador—requirement for consultation with authorized community representatives:* In 2000 an organization representing the Shuar people in Ecuador successfully brought an action against a privately owned oil company for violation of constitutional rights and ILO Convention No. 169. The Constitutional Court held that the company disrupted the community's collective rights and interests when it attempted to enter the community's territory without the permission of its authorities and sign agreements with unauthorized members of the community.<sup>199</sup>
- *Costa Rica—requirement to undertake prescribed consultation procedures:* In 2000 indigenous community development associations in Costa Rica successfully filed a claim for protection against the Ministry of Environment and Energy's grant of a hydrocarbon exploration and operation concession because it failed to meet the procedural requirements for prior consultation. The Constitutional Chamber of the Supreme Court held that the ministry did not follow the mandatory procedure of a consultation summons and that the announcement of a bidding process in the national media did not fulfill the requirements of an appropriate consultation process under ILO Convention No. 169.<sup>200</sup>

### Box-Ticking

The focus of this report has been on ensuring compliance with companies' legal obligations, but even full compliance with obligations may not always be enough. Although a good legal framework is meaningless if it is not enforced, blind enforcement of a bad legal framework is also problematic.

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196 *DOMINICO y otros contra el Ministerio del Interior y de Justicia y otros (DOMINICO and others v. the Ministries of the Interior and Justice and others)*, Expediente T-2315944, Colombian Supreme Court, Sentence T-769 (2009); Amazon Watch, "The Right to Decide: The Importance of Respecting Free, Prior and Informed Consent," 2011, <http://amazonwatch.org/assets/files/fpic-the-right-to-decide.pdf>; Bar Human Rights Committee of England and Wales, Letter to the Constitutional Court of Colombia, Jun. 29, 2009, [http://justiciapazcolombia.com/IMG/pdf/Carta\\_de\\_bar\\_human\\_rights\\_committee.pdf](http://justiciapazcolombia.com/IMG/pdf/Carta_de_bar_human_rights_committee.pdf); Interamerican Association for Environmental Defense, "EcoAméricas Interview: AIDA Co-Director Sees Climate Urgency in Mining Issues," 2011, [http://www.aida-americas.org/en/ecoamericas\\_interview](http://www.aida-americas.org/en/ecoamericas_interview).

197 ILO Convention No. 169 recognizes the principle of FPIC and protects the fundamental rights of indigenous and tribal people to their land and resources. It is discussed in more detail in Appendix 2.

198 ILO, *Application of Convention No. 169 by Domestic and International Courts in Latin America*, 148.

199 ILO, *Application of Convention No. 169 by Domestic and International Courts in Latin America*, 144.

200 ILO, *Application of Convention No. 169 by Domestic and International Courts in Latin America*, 134.

The ultimate goal is a good legal framework that is well enforced. To that end, ongoing management of the natural resource sector should include some flexibility to review contracts, laws and regulations to ensure that their continued enforcement is contributing to the country's overall long-term goals for the sector.

Several recent legal reform and contract renegotiation efforts indicate that governments and civil society are conducting this kind of ongoing periodic review. South Africa's experience with its Mining Charter and SLPs highlights some of the challenges.

After the end of apartheid, the new South African government set out to make the country's economy more inclusive. In 2002, the DMR (then known as the DME) and several mining industry stakeholders, including the Chamber of Mines, South African Mining Development Association and the National Union of Mine Workers, signed the Mining Charter. It included several provisions designed to improve the economic participation of historically disadvantaged South Africans (HDSAs) in the mining industry, including specific targets for the year 2009. The participants in the Charter's development agreed to conduct a review in 2009 to determine whether the industry was meeting those targets. One such target was to fill 40 percent of management positions with HDSAs, but the review identified challenges with the implementation. If 50 percent of a company's lower management positions were filled by HDSAs but upper management had just 20 percent, the company would meet the Charter's technical requirement but not the true objective of equality throughout all levels of the company. Following the review, the revised Mining Charter requires 40 percent participation at all levels of management. The review is an example of how stakeholders can work together to ensure better achievement of a policy objective, rather than mere technical compliance with an obligation.

South Africa's experience with SLPs, on the other hand, appears to be less successful. Companies are required to submit SLPs as a part of their applications for mining rights and to submit new five-year SLPs every five years. The DMR defines what subjects must be covered in the SLPs, including infrastructure and poverty eradication programs. However, some companies report that the SLP requirement has become a mere technicality, in which companies seek to check off the boxes required by an SLP without really working closely with a particular community to identify and meet their highest priority needs. In this situation, even when a company complies with all of its legal obligations, the ultimate goal of the SLP process—ensuring a more equitable allocation of the risks and benefits of mining—may not be met.

Two factors contribute to this problem. First, SLPs are private plans the companies submit to the government; they are not typically shared with the communities affected. Second, because the DMR defines particular categories companies must address in their SLPs, companies have less flexibility and incentive to identify and prioritize the needs of a particular community in which they work. In summary, even though community consultation is required during the process of developing an SLP, the lack of transparency of the ultimate outcome reduces the company's accountability to the community, and the lack of flexibility reduces their ability to meet the community's particular needs.

This experience can be contrasted with Canada's IBAs, which are private agreements signed between companies and communities. IBAs have reportedly been quite innovative in terms of the types of obligations they include, ranging from types of local foods provided to local workers to education and local employment targets. There are at least two key differences between SLPs and IBAs. First, IBAs are directly negotiated with and signed by the affected communities, and the resulting agreement is public within the community. Second, the contents of IBAs are not mandated by law but can be determined instead by companies and communities collaboratively during the consultation and negotiation process.

The ultimate test of whether any legal framework is successful is whether it is meeting its original goals, be they protecting the environment, ensuring community participation in monitoring, protecting workers' health and safety, or collecting a fair rate of return. Periodic reviews of laws and/or contracts can help ensure that they are on track to do so.

Low- and middle-income countries have a huge stake—and face a greater challenge—in ensuring effective monitoring to collect much-needed revenues and to avoid harm. Because institutional and individual capacity is often lacking, innovative partnerships are critical. They help counter problems of capacity, imbalanced incentives and deficient access, but not without careful attention to checks and balances.

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## 4.

# Conclusion and Recommendations

While no country has gotten its monitoring efforts entirely right, the problem is particularly acute for low- and middle-income countries. These countries have a huge stake—and face a greater challenge—in ensuring effective monitoring to collect much-needed revenues and to avoid harm. As mining investments have flowed into many of these countries, a similar surge in monitoring efforts has not taken place. Laws and institutions still tend to emphasize promoting investment at the expense of tracking compliance. Because institutional and individual capacity for monitoring is often lacking, innovative partnerships are critical. They can help counter problems of capacity, imbalanced incentives and deficient access, but not without careful attention to checks and balances in the partnership process. Civil society, governments and companies must work together to improve sector governance. At the international level, governments and intergovernmental institutions should work together to create an environment for better monitoring. Some policy options for improving monitoring are presented below.

As new production comes on line throughout the developing world, it is increasingly important to address gaps in monitoring implementation. For government, this requires attention both to the administrative architecture—the structure of laws and agreements—as well as actual mechanisms for monitoring. For domestic and international civil society, this demands skills and practices that are not typically filled by a single organization or group of NGOs. While some organizations may monitor a particular sector, others will be more expert at responding to crises or reporting on egregious violations. Systematic monitoring will require collaborations to identify and fill gaps. Donors, banks, companies and their home countries all have roles to play in filling those gaps, building the necessary capacity and ensuring that effective, credible monitoring is carried out over the life of a project.

### **Governments of Natural Resource States (Host States)**

- Governments should develop legal frameworks that enable effective government and civil society monitoring efforts and should push toward more uniformity in companies' obligations. Good practices include: defining more obligations in laws and regulations rather than contracts; developing model agreements with limited variability in terms; establishing clear governmental monitoring authority and accountability; and using clearly defined rules instead of vague standards to establish companies' commitments.
- Governments should promote transparency as a necessary condition for monitoring and as a way to incentivize compliance by all parties. This includes disclosing all of the following: contracts; social and environmental agreements; production, cost and revenue figures; statistics on government monitoring; reports and results of government monitoring efforts; and other ongoing project information.
- Governments should establish and maintain accountable structures for monitoring with sufficient staff and resources to achieve their goals. Monitoring agencies should be

independent from the promotional function of other government agencies or state companies with potentially conflicting purposes. These agencies should provide dedicated monitoring staff to ensure that monitoring activities are prioritized. And governments should explore opportunities to develop specialized monitoring agencies, such as large taxpayer units, where agencies can develop and concentrate expertise around the unique challenges of monitoring large mining companies.

- Governments should be continually attentive to risks of corruption and institutional obstacles to change. Oversight mechanisms should limit unnecessary discretion and include checks and balances to avoid agency capture.
- Governments should actively work to identify and correct areas of noncompliance, including through partnering with companies and communities to improve compliance, and by establishing and leveraging sanctions when appropriate.
- Governments should identify strategic partners to enable better monitoring, including through participative community monitoring structures, and through supplementing public capacity with private capacity to conduct required monitoring activities and to build long-term public sector capacity.

### **International and Domestic Civil Society and Their Donor Organizations**

- Civil society should maximize the use of information that is already available on mining projects to conduct monitoring.
- Civil society should continue to seek access to contracts, licenses and permits that define project obligations, as well as information about ongoing projects. They should promote laws and practices that institutionalize transparency. Donors should support this effort.
- Civil society and donors should map out and identify existing capacity for monitoring extractive projects with a view toward appropriate strengthening of the capacity and technical skills necessary to analyze and monitor project obligations.
- Civil society should explore the feasibility of credible monitoring partnerships with companies and government agencies.
- Civil society should develop evidence-based advocacy campaigns and should systematically report noncompliance using the media, parliament and the judiciary when appropriate.
- Donor organizations should recognize the range of company obligations and should seek to identify appropriately placed civil society organizations to monitor companies' activities across this range of issues. They should provide the necessary capacity-building and investment support to sustain effective monitoring consistently throughout the life of the mining project.

### **Extractive Companies**

- Companies should disclose contracts, permits, licenses, community development agreements, and environmental and other plans that delineate their legal obligations. They should also disclose ongoing monitoring information to demonstrate their legal compliance and to enable civil society and government to meaningfully follow mining operations.
- Companies should develop partnerships and participative monitoring structures that enable communities to monitor mining operations in areas of particular concern to the communities.
- Industry associations like the International Council on Mining and Metals and local mining chambers should encourage their members to disclose information and to enter into participative monitoring structures with communities.

### **Home States of Extractive Companies**

- States should cooperate to facilitate monitoring of fiscal terms, particularly transfer pricing issues, through disclosure and information-sharing agreements.

- Home states should enshrine disclosure requirements in regulations, such as through listing requirements like Section 1504 of the U.S. Dodd-Frank Wall Street Reform Act or accounting rules.
- Home states should pass and enforce anticorruption laws.

#### **The World Bank Group and Other Funding Agencies**

- The World Bank Group should require the level of disclosure by mining companies outlined above for all mining investments and resource-rich countries to which it provides loans.
- The IFC should publicize the results of its ongoing monitoring and evaluation of IFC-funded projects, including reports of IFC site visits and companies' annual reports on their compliance with social and environmental terms.
- Government export credit and guarantee agencies should apply the highest disclosure and performance standards for all mining projects they finance. Export credit agencies should seek to develop common, high standards.

# Appendix 1

## Civil Society Monitoring Toolkit

Civil society monitoring of mining projects can help improve project outcomes and increase government and company accountability. This appendix provides more concrete ideas on how advocates can analyze the legal obligations applicable to a particular mining project and where they can get information on whether the various obligations have been fulfilled.

The appendix is organized according to the following five categories of company obligations: financial, social, environmental, occupational health and safety, and operational. Appendix 2 provides additional background on each category.

The availability of information varies depending on many factors, including the size of the project, the size of the company involved, whether the company is publicly listed, the country in which the mining project is located, and the country in which the company is based.

Throughout this section, we refer to specific examples from Liberia's China Union mineral development agreement. This analysis was made possible by Liberia's EITI commitment, which made the contract public. The country's EITI reconciliation reports provide useful monitoring information on the tax, royalty and bonus payments of the mining companies operating there. Please note, however, that since the operation phase of this mining project has not yet begun, many of the tax payments are zero since there is not yet any profit to be taxed. This appendix builds on prior contract analysis work by Green Advocates Liberia and by Susan Maples through Columbia Law School's Human Rights Institute.

### Financial Obligations

A company's financial obligations usually include requirements to pay taxes and royalties to the government. In some cases, companies may also commit to paying an upfront bonus. These financial obligations represent an important source of government revenue in resource-rich countries.

Information on a company's payments can be obtained from the following sources:

- Financial disclosures via company websites or stock exchange disclosures
- Reports and figures published by government ministries, including the finance and mining ministries
- EITI reports and country EITI websites

In seeking to understand whether a company has fulfilled its financial obligations, civil society should ask:

- What taxes and royalties must the company pay?
- How much did the company pay in taxes, and how does their total tax payment break out into the different types of taxes (corporate income tax, withholding tax, VAT, etc.)?
- How much did the company pay in royalties?
- What were the company's mineral production figures?

- What were the company's profits?
- Do the company's tax and royalty payments match their legal obligations, given the information collected on their profit and production figures?
- Did the company commit to paying a bonus? If so, has the bonus been paid?

TABLE A1 | CHINA UNION IN LIBERIA—MONITORING SELECTED FINANCIAL PROVISIONS

	Description of Obligation	Monitoring Information
Bonus	<p>China Union committed to paying a bonus of \$40 million. The bonus was to be paid in cash in two installments: one directly following the contract's effective date and the second 120 days later.</p> <p>Source: MDA, Section 16.6.</p>	<p><b>EITI:</b> Liberia's EITI reports include tables summarizing government revenues by category, including a category for "Signature fees/signing bonus." The figures are not broken down by company or project. Liberia's second EITI report, which covers the period from July 1, 2008, through June 30, 2009, reports no payments for signature fees and bonuses.</p> <p><b>Ministry of Finance:</b> Liberia's Ministry of Finance produces reports, which it posts to its website.<sup>201</sup> One such report noted that China Union's bonus payment had not been received as expected: "During quarter one, a total of US\$23.7 million was projected to have come from . . . China Union [including] a Signature Bonus of US\$20 million . . . in keeping with the concession agreement . . . This payment did not materialize; so there is a growing concern about this revenue stream and the commencement of operations of the company."<sup>202</sup></p> <p>Shortly afterward, another report said China Union had paid \$20 million; the shortfall from the expected \$40 million was "due to the negative impact of the financial crisis."<sup>203</sup></p>
Royalty	<p>China Union's royalty rates are variable, increasing as the value of iron ore increases.</p> <p><i>Rates:</i> The royalty rate ranges from 3.25 percent when the price of iron is less than \$100 per metric ton to 4.5 percent when the price of iron is more than \$150 per metric ton.</p> <p><i>Base:</i> The base for the royalty calculations is the index price, which is defined in the contract.</p> <p>Source: MDA, Section 15.1.</p>	<p><b>EITI:</b> Liberia's second EITI report lists amounts China Union paid for taxes and fees, other payments and withholdings. It includes a category for royalties. It reports that China Union paid no royalties between July 1, 2008, and June 30, 2009.<sup>204</sup></p> <p>In order to monitor whether royalties were paid correctly, we must also know the company's production figures. Royalties are paid based on minerals produced, so a company that has not produced any minerals in a particular time period will not owe royalties. Production figures may be available through a company's financial disclosures if they are listed on a stock exchange, through the company's website, or through the government's mining ministry. In this case, production figures were unavailable. However, because the mine has not yet entered its operational phase, there should be no production.</p>

Table A1, continued on next page

201 Liberia Ministry of Finance, "Fiscal Reports," <http://www.mof.gov.lr/content.php?sub=70&related=22&res=70&third=70>.

202 Liberia Ministry of Finance, *Quarter One Fiscal Outturn: Fiscal Year 2009/10*, 2009, 6-7, <http://www.mof.gov.lr/doc/PUBLISHED%20FISCAL%20OUTTURNS%20FOR%20QUARTER%20ONE-FY200910-FINAL.pdf>.

203 Liberia Ministry of Finance, *Annual Fiscal Outturn: FY2009/10*, 2010, 8, <http://www.mof.gov.lr/doc/FISCAL%20OUTTURN.pdf>.

204 Liberian Extractive Industries Transparency Initiative Secretariat, *Final Report of the Administrators of the Second LEITI Reconciliation*, 2010, Annex 2, <http://www.leiti.org.lr/doc/LEITI2ndReconciliationFinalReport.pdf>.

Table A1, continued from previous page

	Description of Obligation	Monitoring Information
Profit Tax	<p>China Union owes profit taxes at a rate of 25 percent.</p> <p>Source: MDA, Section 14.3.</p>	<p><b>EITI:</b> According to Liberia's second EITI report, China Union paid no profit taxes between July 1, 2008, and June 30, 2009.<sup>205</sup></p> <p>We must determine what a company's profits were in order to determine how much they should have paid in profit taxes. However, since China Union is a private company and does not disclose financial information through a company website, profit data is unavailable. Because the mine has not yet entered its operational phase, there should be no profits.</p>
Surface Rent	<p>China Union must pay \$100,000 a year in surface rents for the first 10 years of its project. After that period, it must pay \$250,000 a year for the next 15 years.</p> <p>Source: MDA, Section 15.4.</p>	<p><b>EITI:</b> Liberia's second EITI report includes a category for surface rental fees. China Union paid \$98,842 in surface rents between July 1, 2008, and June 30, 2009.<sup>206</sup></p>

## Social Obligations

Companies may have a variety of social obligations arising from the country's laws and regulations and/or the company's contract with the government. These obligations can be divided into three categories:

- Local content provisions
- Community consultation requirements
- Infrastructure requirements

### Local Content Provisions

Companies often have obligations to hire local workers or contracting companies. These provisions are intended to ensure that more of a country's citizens see an economic benefit from mining.

As an example, China Union's contract in Liberia provided the following local content obligations (MDA, Section 11):

- China Union may not hire non-Liberian workers for unskilled positions.
- China Union must develop a progressive employment schedule that builds up to Liberians holding 70 percent of management positions and 70 percent of the 10 most senior positions within 10 years of the contract's effective date.

When a company has obligations related to local content, activists can try the following sources of information to determine whether those obligations have been fulfilled:

- Labor unions: Where labor unions are active, they are likely to have information and statistics related to mine employment.
- Workers and the local community: Members of a community close to a mine site may work in the mine or may have sought employment there. As a result, they may have information about who works at the mine.

<sup>205</sup> Liberian Extractive Industries Transparency Initiative Secretariat, Annex 2.

<sup>206</sup> Liberian Extractive Industries Transparency Initiative Secretariat, Annex 2.

- Company reporting: Some mining companies produce corporate social responsibility (CSR) reports, which often include information on labor. If they do not include this information, civil society organizations could determine whether the company has a CSR representative and could contact that person to request information.
- Ministry of labor: The country's labor ministry may collect statistics on mine employment.

In seeking to understand whether the company has fulfilled its local content obligations, civil society should ask:

- What local content commitments did the company make?
- What percentage of the mine's employees are from abroad?
- What percentage of the mine's management positions are filled from abroad?
- What contracting companies is the mine using? Where are those contracting companies based?
- From what companies is the mine sourcing its goods? Where are those companies based?
- Has the company faced any challenges in fulfilling its local content requirements? If so, how is the company working to address those challenges for the future?

### Community Consultation Requirements

Companies may be required to consult with local communities about their mining operations. These obligations can arise from treaties, laws, contracts or conditions imposed by financial institutions. Coming out of these consultations, companies may also need to submit plans or reports on the social impacts of their projects.

For example, China Union's contract in Liberia required the company to conduct a social impact assessment and to submit a social action plan. It was required to hold public hearings on both of these documents (MDA, Section 5.4).

To determine whether a company has fulfilled its obligations with respect to community consultation, civil society can:

- Speak with local community members.
- Request copies of any documentation the company was required to submit to the government and/or any documentation the company was required to make publicly available. The company or the mining ministry may be able to provide these documents.

Civil society should ask the following questions:

- Was the company required to conduct consultations with affected communities? And, if so:
  - Did the required consultations take place?
  - Who participated in the consultations? Did the participants adequately represent the affected communities?
  - Did the company make efforts to publicize the consultations?
- Did the company make any specific commitments to the community coming out of these consultations? If so, have those commitments been fulfilled?

### Infrastructure Requirements

Companies may be required to build and/or operate infrastructure, such as hospitals, clinics, schools or roads, in the area around their mine operations. They may also be asked to contribute funds specifically to social infrastructure projects.

For example, China Union's contract in Liberia included several social infrastructure obligations. The company was required to:

- Provide \$200,000 annually in educational scholarships. It was also required to provide \$50,000 annually for the government's general revenue account to be earmarked for a mining and geology institute at the University of Liberia (MDA, Section 11.3).

- Contribute \$3.5 million annually to a community development fund, managed by the government (MDA, Section 8.2).
- Renovate and extend portions of a railroad and port facility, and renovate roads in the area of the mine and make them available to third parties (MDA, Sections 6.6 to 6.7).
- Provide clean housing, water and health care to all employees (MDA, Sections 9.2 to 9.5, and 10).

The following sources may provide information on a company's infrastructure obligations and whether they have been fulfilled:

- Government ministries, including the ministries of finance, mining, central planning, labor, health and education: Government reports may detail the status of infrastructure projects. Citizens can also contact ministries to request information about the status of particular projects.
- Company CSR reports: Company reports may include information on social investments, including infrastructure construction projects, contributions to social and community development funds, and operation of social infrastructure.
- Local community members: Community members living near a mining site can observe whether infrastructure projects are progressing and whether the company is providing social services.
- Independent observation of the area: Citizens can visit mining sites to determine the status of construction projects and to observe whether the company is providing social services.

Civil society should ask the following questions:

- Does the company have any obligations to build infrastructure or to provide social services?
- Has the infrastructure been constructed?
- What is the quality of the infrastructure or the services provided?
- Under what conditions will the infrastructure be available for general use, as opposed to being available only for the mining project?
- Which government ministries provided oversight for the construction project or the provision of services? How much oversight did they provide?
- Does the company have any obligations to give money to the government for social infrastructure projects?
- Has the company paid the required money?
- How has the government used the money the company gave?

## Environmental Obligations

Company environmental obligations will most often include developing an EIA and/or an EMP. Once these documents are developed, they will lay out the company's environmental plans for the project in more detail. Therefore, civil society will need to determine what project-specific documents the company was required to submit, get access to them, and analyze them to determine the company's obligations with respect to a specific project.

China Union's contract in Liberia included the following environmental obligations:

- China Union had to submit an EIA and an EMP (MDA, Section 5.3).
  - Both must be updated every four years and submitted to the Environmental Protection Agency (MDA, Section 13.4).
  - More detail on the EIA requirement is available in sections 37 through 39 of Liberia's Environmental Protection Act.<sup>207</sup>

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<sup>207</sup> Liberia, An Act Creating the Environmental Protection Agency of the Republic of Liberia, 2002, [www.moa.gov.lr/doc/epa\\_act.pdf](http://www.moa.gov.lr/doc/epa_act.pdf).

- China Union must provide the government with an annual environmental audit and assessment to determine whether the mine's operations are being conducted in conformity with environmental laws, the contract and the EMP. An independent environmental consultant must conduct the audit (MDA, Section 13.2).

Civil society can go to the following sources for information:

- EIA and EMP: Request copies of these documents from the company and from the government's mining and environmental ministries.
- Civil society and community observation: Civil society and community members can seek to gain access to the mine site to check for potential environmental issues and/or can measure water and soil samples from the surrounding area to check for metals contamination and acidity. Community members can identify and report any unusual changes in the environment.
- Government monitoring: Civil society can ask for information about what monitoring efforts the government has conducted on the mine's environmental performance and, if so, whether any reports are available from the efforts.
- Company reporting: If the company is required to submit environmental audits to the government, as in the China Union example, civil society can request copies of those audits from the company and from the government's environmental and mining ministries. Company CSR reports may contain information on environmental management.
- Third-party monitoring: If external financing institutions—like the World Bank—are involved in a project, they may have conducted some independent environmental monitoring. Civil society can check these institutions' websites for environmental assessments.

In monitoring a company's environmental obligations, civil society should ask:

- Was the company required to submit an EIA and/or an EMP?
- Did the company submit the required documents?
- What commitments did the company make in the EIA and/or EMP?
- Is the company complying with those commitments?
- Do the water and soil around the mine site indicate high levels of pollution from the mine?
- What impacts has the mining project had on the ecosystem?

## Occupational Health and Safety Obligations

Occupational health and safety is a serious concern for mining companies. Workers' injuries and illnesses have plagued the industry and its workforce for years. Governments usually require companies to provide protective gear to their workers, to ensure a safe working environment, and to report accident statistics. Historically traditional civil society has not been very active in understanding and monitoring health and safety concerns, perhaps because unions and other worker organizations have been quite active in this area.

China Union's contract in Liberia included the following health and safety requirements:

- China Union must install and use health and safety devices and worker gear and equipment that comply with applicable law and international standards (MDA, Section 9.1).
- China Union must notify the government promptly of any death or serious injury (defined as one resulting in missing more than three days of work) of an employee or contractor that happens as a result of operations (MDA, Section 9.1).

Civil society can go to the following sources for information:

- Local unions and workers: Citizens can contact workers and their union representatives for information on health and safety risks, measures the company has taken to address them, and statistics on accidents.

- Company CSR reports: These often include information on accident statistics and safety measures.
- Government agencies: Government agencies, including the mining and labor ministries, may provide their own reporting on mine accident statistics. Citizens may also contact them for information on the frequency of government inspections.

In monitoring a company's health and safety obligations, civil society should ask:

- Have there been any accidents or injuries at the mining site? What caused the accidents or injuries? Have the causes of accidents been addressed?
- What are the biggest risks to workers' health and safety at the mine site? How are those risks being addressed?
- Have workers been provided with appropriate protective gear?
- How frequently has the government inspected the mine for health and safety concerns?
- Has the company been complying with requirements to report on accidents at the mine site?

## **Operational and Production Obligations**

Governments often impose operational and production requirements to help ensure that mining exploration and production are taking place at the appropriate pace, using appropriate techniques and within an appropriate budget. Company obligations may include submitting work plans and budgets detailing how the exploration or construction phase of a mining project will proceed, meeting minimum expenditure requirements, and relinquishing a portion of their exploration concession each year or before they can request a renewal.

China Union's contract in Liberia included the following operational and production requirements:

- China Union must submit quarterly statistical reports on the amount of iron ore mined, processed and shipped (MDA, Section 6.8).
- In case China Union cannot improve production, the government may convene a third-party study to determine a fair average recovery rate. If China Union fails to achieve this rate, the government may increase its royalty take (MDA, Sections 6.4c and 6.8).
- China Union must submit a feasibility study, which must be completed by an independent expert (MDA, Section 5.2).

Civil society can go to the following sources for information:

- Government disclosures on mining production figures
- Company financial reports
- Company technical reports disclosed through stock exchanges

In monitoring a company's operational and production obligations, civil society should ask:

- Was the company required to submit a work plan or budget? Were the required documents submitted?
- During the exploration phase, has the company conducted the exploration activities it was required to conduct? How much drilling did the company conduct? What were the results of those exploration activities?
- During the exploitation phase, has the company conducted its operations in accordance with its work plan and budget?
- In times of economic downturn, has the company ceased operations? Is the company permitted to cease operations in such conditions?

Appendix 1, along with Appendices 2, 3 and the bibliography, can be found at [www.renewwatch.org/enforcingtherules](http://www.renewwatch.org/enforcingtherules).





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