

This paper reflects the views of the author and does not represent the views of the Panel.

It is provided as background research for the HLP Report, one of many inputs to the process.

Regulating Extraction in the Global South: Towards a Framework for Accountability

BACKGROUND RESEARCH PAPER

Franklyn Lisk
Hany Besada
Philip Martin

**Submitted to the
High Level Panel on the Post-2015
Development Agenda**

This paper reflects the views of the author and does not represent the views of the Panel.

It is provided as background research for the HLP Report, one of many inputs to the process.

May 2013

**Regulating Extraction in the Global South: Towards a Framework for
Accountability**

Franklyn Lisk, Professorial Research Fellow, University of Warwick

Hany Besada, Research Specialist, HLP Secretariat

Philip Martin, Support Officer, Norwegian People's Aid (Tajikistan)

1.0 Introduction

The Global South - the developing regions of Africa, Asia and Latin America – is richly endowed with mineral assets that are essential for modern production and consumption worldwide. Africa, for example, hosts over two-thirds of the world's reserves of platinum which are essential in the electronic industry; Latin America accounts for over half of global production of copper; Asia accounts for over half of the world's coal and more than a third of global iron-ore deposits used for energy and steel production. Moreover, Africa currently accounts for about 12 per cent of the world's oil reserves, 40 per cent of its gold, 80 to 90 per cent of chromium and platinum group of metals, 85 per cent of phosphate reserves, more than half of cobalt and one-third of bauxite (UN ECA and AU Commission 2012, 7; African Development Bank, 2013). US Geological Survey estimates also show Africa expanding its metal and minerals extraction by 78 per cent between 2010 and 2017 (US Geological Survey, 2010).

As a result, the mining and extractive sector constitutes a major share of exports and tax revenues for countries in the Global South, and holds enormous potential to finance rapid economic development and poverty reduction. From 2000 to 2011, for instance, natural resource extraction constituted a major component of real GDP growth in over fifteen African states, including over half of all growth in Equatorial Guinea, Ghana, and the Democratic Republic of Congo (IMF 2012, 65). With high commodity prices and the rise of emerging economies driving more ambitious investment strategies among international mining companies, there are now unprecedented opportunities for leveraging natural resource wealth in pursuit of human development and economic prosperity.

However, harnessing these benefits remains problematic; many countries do not reap the full benefits of their extractive resource endowments. Rather than provide for broad-based and sustainable economic growth, resource revenues often end up benefiting only a small number of local elites and foreign investors due to corruption, undervaluation of mineral assets, revenue mismanagement, and various forms of taxation manipulation and evasion. The disparity between the quality of resource extraction regimes in the Global North and Global South is a critical factor in this, preventing many developing nations from achieving positive development outcomes. The regulatory and legal frameworks for resource extraction in the Global South are often designed to maximize benefits for privately owned foreign companies and a small subsection of elites rather than provide broad-based benefits – in the form of employment, local investment, or monetary compensation – to local populations (Campbell 2009). Natural resource dependence also insulates national leaders from public pressure and accountability – one manifestation of the “resource curse” – with an observable correlation between resource abundance and political corruption (Tsui 2011; Ross 2012). Moreover, the capacity of local administrators to monitor and enforce existing regulations is often low, resulting in the manipulation or obfuscation of revenue-tracking and lower financial yields for host governments and communities.

At the same time, discussions of transparency in the Global South are increasingly shaped by extractive industry efforts at self-regulation, or corporate social responsibility (CSR). These protocols are applied voluntarily, with corporate interest stemming from the “business case” for CSR – protecting corporate reputations and maintaining access to markets (Hamann & Kapelus 2004). A lack of national and international constraints placed on corporate action, mirrored by a failure to institute robust checks and balances, has left a contentious debate on the usefulness of

CSR protocols (Newell 2005). Nevertheless, working with the private sector is both inevitable and an opportunity, in particular with large foreign extractive companies which have extensive geological knowledge, capital and technological expertise to invest in extractive industries in the Global South.

.In short, wealth from extractive resources has not been sufficiently transformative and there has been little progress in overall development and welfare in these countries. Available evidence suggests that this unsatisfactory state of affairs is largely due to exploitative practices of foreign investors coupled with weak governance, mismanagement and poor politics of local administrations (Africa Progress Panel, 2013). In the context of a post-2015 development agenda, revenue flows from natural resources represent an unprecedented opportunity to make a breakthrough in development – a breakthrough that could underpin transformative investments in transport and energy infrastructure, decent education and health systems, job creation, smallholder agriculture, as well as finance social programmes to reduce poverty, vulnerability and insecurity that blight so many lives in the Global South.

This briefing paper illustrates these challenges in the context of the post-2015 MDGs development agenda, and highlights policy recommendations on how developing countries can implement more effective regulations in the extractive sector to improve sustainable development outcomes. It also points to strategies for improving monitoring and compliance mechanisms for CSR protocols. Drawing on illustrative cases and number of recent studies, a balanced approach between government (regulations) and industry (CSR) is recommended to improve accountability and development outcomes in the extractive sector.

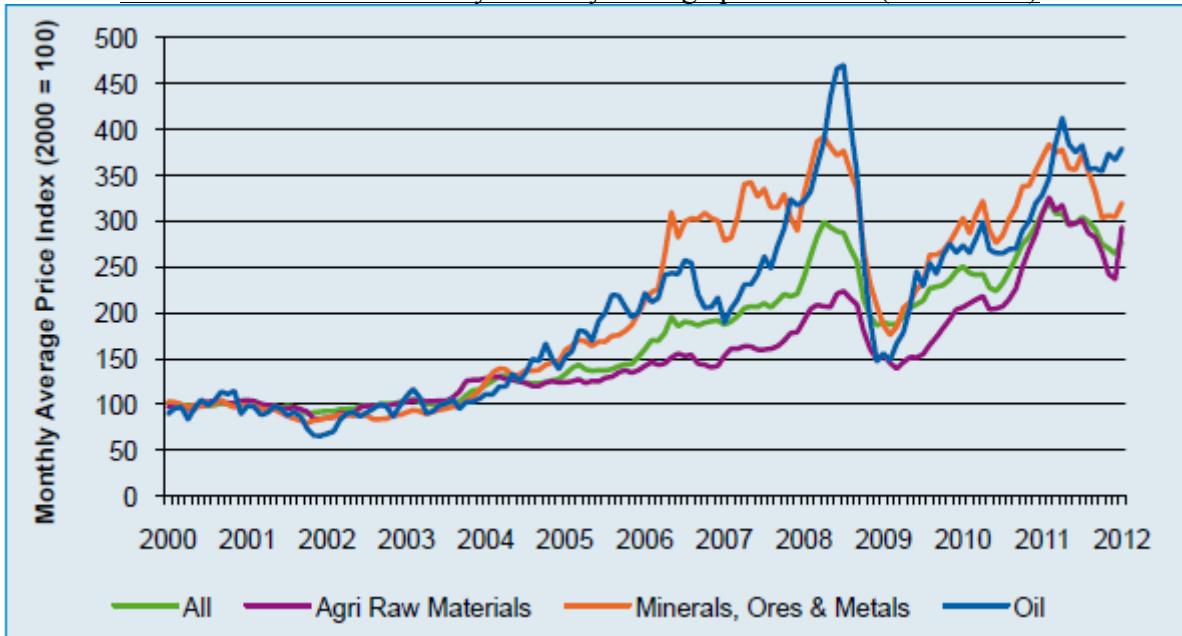
2.0 Sustainable Development and Economic Growth through Resource Extraction: Effective Policy Frameworks and Corporate Social Responsibility

Harnessing the benefits of resource wealth for structural transformation of the broader economy has remained difficult for many resource-endowed developing countries. In Africa particularly, the failure to manage natural resources properly has given rise to the troubling question: How can a continent be so rich in natural resources, yet so poor in human and physical development? Despite the high growth rates of recent years, many countries in the region have failed to turn resource wealth into inclusive economic development. Rather, resource rents appear to have gone mostly toward fuelling domestic consumption instead of productive investment needed for long-term growth and development. If anything, resource wealth has in many cases resulted in increased income inequality and economic distortion, and even triggered social and political instability – a situation that has been widely described as the “resource curse.”

In this paper, we focus on extractive resources - minerals and energy commodities - which commonly comprise the largest proportion of resource rents accrued by governments, and which are most commonly identified with the resource curse. As Table 1 illustrates below, global commodity prices have enjoyed a sustained boom beginning around 2002, mostly driven by increased demand from emerging economies such as China and India. One consequence of this price surge has been a sharp increase in resource rents, both for the public and private sector. For the world’s 40 largest private sector companies in the hard commodities sector, for instance, revenues increased by 357 percent between 2002 and 2008 (UNIDO 2012, 15). In the energy sector, revenues for the 100 largest extractive firms grew by nearly 80 percent between 2006 and 2008 (*ibid*). Many governments increased their revenues as well. Corporate taxes paid by oil companies to governments between 2005 and 2008, for instance, grew by 55 percent. Royalties

on production and exports in the mining sector also contributed to higher state revenues in many countries, in some cases comprising an overwhelming share of national GDP.

Table 1 – Global commodity monthly average price index (2000-2012)



Source: United Nations Conference on Trade and Development (UNCTAD).

<http://unctadstat.unctad.org>

However, many countries endowed with extractive resources have had only limited success in translating this wealth into sustainable economic development and reducing poverty levels among the broader population. Two thirds of the world's poor currently live in resource-rich countries, and many of these well-endowed states are struggling to keep pace economically with their resource-poor counterparts. One observer at the Brookings Institute described the problem in stark terms:

"In 1990, almost 600 million people lived on less than \$5 a day in resource-rich countries. Today, it is estimated that poverty has increased to about 700 million people. Among this population, close to 300 million live in dire poverty, surviving

on \$2 a day or less. The majority of the poor in resource-rich countries live in Africa, where 80 percent of citizens in extractive-intensive countries live on under \$5 a day, and over 50 percent live on under \$2 a day” (Kaufmann 2012).

Many studies have analyzed this problem, contributing to a large body of research on the so-called resource curse, which this paper will not attempt to comprehensively catalogue here. However, over a decade of research on natural resource governance in developing economies has made one finding abundantly clear: the extent to which the positive benefits of resource extraction are attained – and corruption, environmental destruction, and civil conflict avoided – is shaped by the ***quality of governance*** over the activities of the key actors involved, particularly extractive companies and host governments. International perceptions of good governance include a complex web of issues, ranging from transparency, efficient and effective management, checks and balance to absence of corruption and accountability of governments to their citizens. Good enough governance has been associated with the experience of a few resource-endowed countries in Africa (e.g. Botswana, Namibia, Ghana and Mozambique) that have been using their resource-wealth to stimulate high growth, create strong private sectors with additional jobs, and transform their development path towards sustainable and inclusive outcomes.

By contrast, poor transparency and lack of accountability in the extractive sector have allowed for vast imbalances between the wealth created by resource exploitation and poor human and economic development among local populations. This lack of transparency and accountability applies to the negotiation and tendering of contracts, the various payments and royalties made by multinational corporations (MNCs) to governments, and the public management of these revenues. In the worst cases, resource wealth has led to widespread corruption and a culture of rent seeking and self-accumulation by a small elite and increasing

income inequality; economic destabilization and distortions caused by the perverse effects of the “Dutch disease,” and in the worst case has produced armed conflict and war.

The policy framework of the extractive industry in which these actors operate is defined by both national legal frameworks as well as corporate practices which establish norms pertaining to accountability measures, revenue-sharing, local employment and investment requirements, and social and environmental safeguards. “Governance” of natural resources must therefore be considered as a shared and interconnected responsibility between host governments in developing countries and foreign investors from developed and emerging economies, with complimentary regulatory roles and accountability standards. Therefore, in terms of analyzing the policy challenges of natural resource extraction, the national regulatory frameworks of governments as well as extractive industry self-regulation (CSR) are key determinants of how natural resources and revenues are managed. In addition, it is also important from a policy standpoint to consider the specific political economy context in which regulatory policies are formulated and implemented.

2.1 National Regulatory Frameworks

A successful regulatory framework for natural resource extraction – that is, one which effectively translates natural resource wealth into broad-based economic development – requires three essential components. First, the institutional environment must be sufficiently secure such that private investors are willing to provide the capital needed to develop the resource. An investment environment in which property rights are weak and the possibility of asset confiscation is high will be unlikely to provide sufficient incentives for private sectors actors to prospect for and develop resource discoveries (Collier & Venables 2011). Second, the

framework must guarantee through an appropriate contractual system that host governments, or local communities directly, receive a substantial portion of the value of the resource through taxation or royalties. Finally, the domestically captured value of the natural resource should be transparently re-invested into assets which diversify the national economy and offset the depletion of the extractable resource. As a recent report by the African Development Bank noted, “[p]romoting inclusive growth means... broadening the economic base beyond the extractive industries and a handful of primary commodities” (ADB 2012, 21). While the first requirement is usually a long-term institutional goal, of immediate concern for policy-makers are the second and third requirements, namely the need for transparent revenue capture and re-investment.

The design of revenue-sharing and taxation systems for resource extraction is politically sensitive and context-specific. Broadly speaking, taxation regimes can be problematic because rates are insufficiently high, because companies are able to evade payment to governments through loopholes in the tax code or inconsistencies in mineral valuation, or because the taxation regime is not adequately enforced (Collier & Venables 2011). Over the last number of decades, the general trend in the Global South has been towards reduced taxation and royalties applied to the extractive sector, as countries compete to attract and retain foreign investment (Campbell 2009). As indicated in the 2013 Africa Progress Report, ‘Equity in Extractives,’ many foreign companies operating in the extractives sector in Africa have been provided with extremely favourable tax concessions and incentives, such as very low rates of royalty and exemption from custom duties, VAT, export and corporation taxes (Africa Progress Panel, 2013). Many mining companies are also increasing operations in countries which little experience negotiating revenue-sharing contracts or legislating proper taxation regimes. Hence, foreign firms tend to use their power to extract excessive economic rents beyond reasonable returns, and sometimes

operate within multinational cartels which give them monopoly power in negotiations. The combined effects of these practices are reductions in the tax revenues of host governments even when foreign investors are enjoying very high profits. Section 2.1.1 highlights some of these challenges in the case of Ghana's gold extractive sector.

2.1.1 Gold Extraction in Ghana

Known as the “Gold Coast” for its generous mineral endowments, Ghana is Africa’s second-largest gold producer. The production of gold grew from 63 tons in 2004 to 80.5 tons in 2008, and now accounts for approximately 40 percent of total export earnings, 14 percent of total tax revenues, and 5.5 percent of the national GDP (Ayee et al., 2011). Despite this, the net impact of Ghana’s mining sector on its economic development and poverty reduction have been modest, and contractual arrangements between the government and multinational corporations have given only a limited share of revenue to the host country. For instance, even though mineral exports increased 50 percent between 2004 and 2008, the overall share of tax revenues derived from the mining sector decreased over the same period (*ibid*).

The regulatory framework in the mining sector underwent substantial reform with the Minerals and Mining Law of 1986, part of the broader structural adjustment policies in the country supported by the IMF and World Bank. Liberalisation of ownership and taxation regulations resulted in an inflow of international investment from multinational corporations, which rapidly took over underperforming state-owned mining operations and opened new projects (Opoku-Dapaah and Boko 2010). Foreign investors were granted a number of incentives for doing business in Ghana, including the right to repatriate their profits, exemption from paying duties on imported equipment, and total ownership of business ventures in the country.

Currently, the Minerals and Mining Act of 2006 (revised in 2010) formally governs all aspects of mining regulations in Ghana, and is considered by the World Bank to be “in line with international best practices in the industry” (World Bank 2008, 32). Under the new legislation, private holders of mineral extraction licenses in Ghana must pay a royalty of 5 percent of their gross revenues (Ayee et al. 2011, 23).

The windfall of private investment in Ghana’s gold extraction sector brought a number of undeniable economic benefits. Approximately 220,000 new mining jobs were created for Ghanaians between 1987 and 2002, and the mining sector spent millions each year on goods and services from local businesses around areas of operations (Opoku-Dapaah and Boko 2010). Prompted by these pro-investment policies, the recovery in global demand for primary commodities, and direct efforts by the Ghanaian government to attract and support joint ventures with foreign firms (for example, by creating the Ministry for Private Sector Development to play a facilitating role between the government and private companies), since the late 1980s the three largest mining companies in the country – Newmont, Golden Star and AngloGold – invested over \$3 billion in mining operations (*ibid*). Foreign investment also created economic “linkages” with broader sectors of the economy. In 2006 the Ghanaian gold mining industry saw \$465 million (20 percent of total expenditures) spent on locally acquired inputs. These suppliers often sourced their materials from other local enterprises, and so on down the chain, creating a “multiplier” effect as incomes generated from the extractive industry fed back into the domestic economy (UNIDO 2011, 37). Moreover, \$175 million was paid in wages and salaries to mining employees, bolstering local consumption and creating more employment in retail and service sectors.

Despite these benefits, however, natural resource wealth created by Ghana's extractive sector has not been fully leveraged to create broad-based growth and poverty reduction. A number of important regulatory challenges persist, including:

- *Transparency.* The process of awarding mining rights, licenses, and contracts in Ghana remains insufficiently transparent and accountable. One major problem is the absence of an open tendering or bidding process to acquire prospecting or exploration rights. Instead, individuals and companies are awarded licenses through an opaque administrative process, providing openings for corruption, bribery, and tax evasion (Ayee et al, 24). Mining contracts are also awarded with non-disclosure clauses, creating a barrier to accountability and transparency. Moreover, the President maintains wide-ranging authority over many matters of mining sector governance, since all public lands and minerals are technically vested by the Constitution to the president on behalf of the people.

- *Low Taxation Rates and Exemptions.* In addition to royalties, a profit tax of 25 percent is applied to mining sector operators. Unlike other sectors, however, the mining industry maintains special concessions. Staff of mining companies are exempted from paying any income tax on furnished accommodations, remittances by expatriate personnel are also exempted from taxation, overtime payment to labour is taxed at reduced rates, and exemptions are made from payment of customs duties for imported mining equipment, machinery, and accessories. Thus, private sector investment in Ghana's mining sector results in proportionately less public revenue than investment in other sectors.

➤ *Tax Evasion and Manipulation.* The 2006 Act allows for mining companies to merge part or all of its mineral rights through the creation of new companies under different names, which often enjoy tax holidays and pay few or no corporate taxes (Ayee et al. 2011, 25). The calculation system for royalty payments – based on the difference between expected revenues and operational costs for the lease holder – also allows private companies to reduce their overall royalty payments, since operational costs are defined to include capital allowances and interest payments for the period. Thus, companies are able to carry forward excessive operating costs into future years, lowering the overall royalty payment even during years of high commodity prices and windfall profits (*ibid*). Indeed, before the 2010 Budget Law introduced a flat rate of five percent in the gold extraction sector, no company in Ghana ever paid more than the three percent royalty.

In fact, corporate and individual taxes and royalties from mining firms amounted to only 3% of total tax revenues from 2000 to 2005 (IMF 2005). While this is partly attributable to low taxation rates, there are also accusations that mining companies manipulate the existence of exemptions and capital allowances, with local tax administrators having limited ability to effectively monitor these claims (Prichard 2009, 262). In the 2004 fiscal year, for instance, a report by the Extractive Industry Transparency Initiative (EITI) revealed that only two companies actually paid corporate income taxes, and that no mining companies paid capital gains, profit, or withholding taxes (Akabzaa 2009, 46). Moreover, inconsistencies in the valuation of minerals render the process of revenue-tracking more difficult, and the application of different exchange rate regimes by mining

companies for the payment of royalties has produced distortions in the amounts of revenues actually paid to the government (*ibid*).

- *Limited local employment.* In Ghana, between 2000 and 2007 the minerals sector employed approximately 0.2% of the non-agricultural labor force, despite contributing 5.5% of Ghana's GDP and 40% of its exports (ADB 2012). This imbalance is exacerbated by the growing use of surface mining technologies, which has constrained employment opportunities in the sector, as well as increased expatriate staff quotas (Akabzaa 2009).

2.2 CSR, Accountability and Sustainable Development in the Extractive Industry

Governments are only one actor in the “policy chain,” and not necessarily the most important actor in the development of economic linkages in the extractive sector which will facilitate growth and poverty alleviation. The emergence of industry efforts in the extractive sector to improve corporate practices originated in the debates over corporate social responsibility in Latin America, where civil society organizations successfully drew attention to human rights and environmental abuses committed by multinational mining corporations (Sagebien and Lindsay 2011). While public concern about CSR in the extractive sector has traditionally been linked to such environmental and human rights incidents (Warhurst 1999), there has also been increased scrutiny over private companies’ collusion with host governments in opaque mineral contracts, as well as the failure to domestically re-invest profits from extractive asset depletion. In 1999, these problems were put in the public spotlight by a Global Witness study – *A Crude Awakening* – which documented the complicity of major multinational oil companies in the embezzlement and mismanagement of Angola’s oil revenues during decades

of civil war and impoverishment in that country (Global Witness 1999). It became widely acknowledged that imbalances between national processes for regulation natural resource wealth and international corporate practices were a serious impediment to development, economic growth, and human rights in resource-rich developing countries.

By 2000, a growing number of companies and civil society groups began considering ways that private sector corporations could play a more constructive role in sustainable development and conflict prevention in resource-rich countries. The Council on Economic Priorities, the Prince of Wales Business Leaders Forum, and International Alert, for example, co-produced the report, *The Business of Peace*, making an economic case for why business should view responsible corporate practices such as transparency, good governance, and environmental protection as being in their own self-interest. The World Bank also launched a high-profile effort to fight corruption and promote “good governance,” supporting the idea that governments and the private sector must provide greater public accountability and transparency in commercial transactions, especially regarding extractive resources (Haufler 2010, 62).

Extractive multinational companies have since become much more active in the implementation of community development schemes over the last decade. CSR initiatives help construct schools and hospitals, finance youth employment programs, and micro-credit schemes. Particularly in post-conflict or fragile environments, the CSR’s role is seen as helping with reconstruction activities (for example, in infrastructure) and investments, by engaging in business activities that will have positive spinoffs and multiplier effects for the host economies, and by social investments and partnerships that help address the main drivers of poverty and conflict, particularly corruption and social inequality (Kolk & Lenfant 2010). Increasingly, these initiatives are undertaken in partnership with established development agencies and NGOs. For

example, the mining companies Rio Tinto Alcan, IAMGOLD and Barrick Gold have co-financed a number of recent CSR projects with the Canadian Government and NGOs in Ghana, Burkina Faso, and Peru aimed at promoting good governance and pro-poor economic programs, and local youth job training (Government of Canada 2011). Indeed, the growing collaboration of governments and civil society organizations with private sector actors seeking to implement CSR projects has led some to view CSR as a potentially long-term solution for delivering development programming (Frynas 2005).

Voluntary CSR initiatives have also become important tools for encouraging improved accountability and transparency in the mining industry (Yakovleva 2005). In addition to individual CSR codes of individual companies, many corporations have begun to sign on to broader transnational extractive transparency initiatives along with governments and civil society organizations. The International Council on Mining and Metals' Mining, Minerals and Sustainable Development Project, for example, represents an effort by the industry to introduce guidelines and codes of practice which are voluntarily adopted by their members. The Extractive Industries Transparency Initiative (EITI), Publish What You Pay (PWYP) campaign, The Kimberly Process for the Certification of Diamonds, and other initiatives pursue similar objectives, encouraging the full publication and verification of company payments made to governments and the revenues accrued from oil, gas and mining activities. At a more general level, initiatives like the UN Global Compact, OECD Guidelines for Multinational Enterprises, and IFC Performance Standards are structured around improved disclosure of payments, transparency in contractual agreements, and adoption of social and environmental impact assessments. These initiatives and institutions are gaining growing adherence by companies in the extractive sector. Among other things, this proliferation of transnational and voluntary

transparency initiatives points to the growing responsiveness of private industry to the influence of global public opinion and the pressure of civil society groups (Ushie 2013).

At the same time, mandatory legal requirements to improve accountability among MNCs operating in the extractive sector in developing countries have also been introduced in various countries. In 2010, the U.S. Congress passed into law the Dodd-Frank Act, placing statutory disclosure requirements on companies to publicize all taxes, royalties and fees made to U.S. or foreign governments for the commercial development of oil, natural gas, and minerals, including exploration, processing, export and granting of licenses (Ushie 2013). The extensive scope of the legislation is expected to affect many of the world's leading oil, gas and mining multinational companies, representing a major advancement in the civil society campaign for greater scrutiny of extractive sector governance. Similarly, the European Commission has issued a Directive on transparency requirements by which companies are obliged to disclose information on all payments made for mining and logging rights. In the U.K., France, Hong Kong, and elsewhere, similar anti-corruption legislation has recently been adopted. Once seen as a fringe policy issue of concern only to civil society groups, extractive sector transparency has become a mainstream issue among governments and multinational corporations alike (Ushie 2013).

However, critics note that CSR protocols in the extractive sector as presently practiced have serious shortcomings in terms of measurably improving accountability outcomes and sustainable development (Frynas 2005). Firstly, most CSR programming (and in the oil industry in particular) has tended to focus on micro-level issues such as compensation to specific communities, rather than macro-level effects like political corruption and distortions to the national economy induced by reliance on extractive resource revenues. There are isolated exemptions to this; Statoil, for instance, has been active in funding human rights and professional

training to the judiciary in Venezuela and Nigeria. Generally, however, for most extractive companies, the fact is that “key development issues are entirely ignored … CSR does not even attempt to address any negative development effects related to the resource curse” (Frynas 2005, 596). Thus, CSR activities undertaken by MNCs in developing countries have been criticized for not addressing the root causes of underdevelopment, and for failing to improve relationships with local communities (Hamman & Kapelus 2004).

Second, the vagueness and non-binding nature of many CSR codes and voluntary transparency initiatives leads many to question their effectiveness. Many companies have been accused of “blue washing” their operations – signing on to non-binding international compacts in order to give a positive public image to unsound practices (Nwete 2007, 313). This is linked to the problem of a lack of broadly accepted measures for evaluating CSR programming outcomes in the extractive sector, allowing companies to claim adherence to social responsibility without satisfying the demands of other stakeholders. A number of global CSR standards incorporating accountability and transparency measures do exist, although none have gained universal application. The Dow Jones Sustainability Index (DJSI), for example, assesses criteria including economic, environmental and social aspects of sustainable development. The FTSE4Good Index, meanwhile, assesses CSR performance of companies in five areas, including “countering bribery.” However, evidence to date has not shown that corporate performance on such indicators significantly affects firm behaviour (Curran & Moran 2007). Moreover, external auditing of CSR and sustainability reports are rare, and are often conducted by consultants paid by the company in other capacities (Jenkins & Obara 2006, 18). Part of the difficulty also relates to the context-specific nature of CSR, putting private corporations in a dilemma of prioritizing their overall social responsibilities in line with local needs (Kolk & Lenfant 2010, 6). These

challenges have led to various attempts to re-conceptualize the proper definition of CSR, such as the idea of incorporating “social justice” benchmarks into CSR evaluation – the idea that social responsibility can only be attained if the cumulative impact of company operations benefits the most vulnerable in society (Hamann & Kapelus 2004, 87).

Finally, the type of financial flows covered by EITI and other reporting schemes remains limited; for instance, these rules usually do not affect bilateral loans, permitting donor countries to lend money to companies which may collude with officials in resource-rich countries without public scrutiny. A 2010 study by Revenue Watch, for instance, found that several of the 41 countries signed up to the EITI were among the least transparent regarding the activities of extractive industries operating on their soil (Revenue Watch 2010). Without sufficient state capacity and political will to enforce good governance norms and corporate behaviour, CSR programming has tended to arrive on an ad-hoc basis, often without adequate long-term planning or concern for sustainability.

2.2.1 – CSR in Nigeria’s Oil Sector

In Nigeria – a country which derives approximately 85 percent of its public revenue from petroleum and gas extraction – the experience with CSR programming by multinational oil companies is illustrative of many of these problems. Over the past two decades CSR projects have provided for the construction of roads, schools and health facilities, the provision of water and electricity, support to professional skills-training, and capacity building initiatives. A recent study of Exxon Mobil’s capacity-building initiatives in the state of Akwa Ibom, for instance, identified 295 graduates of an economic empowerment training course, 100 beneficiaries of a garment design and production training program, and over 1,600 people granted small loans through a company-sponsored micro-credit scheme (Mbat et al. 2013).

Despite the adoption of various CSR initiatives by most major oil companies since the late 1990s, however, local communities have received a proportionately low amount of benefit compared to the high social and environmental costs of extractive activities. For instance, there have been over 5,000 recorded oil spills between 2000 and 2004 alone (Idemudia 2010), as well as a massive spill in November 2012 which polluted ecosystems and impacted the livelihoods of fishing communities along a large stretch of coast of the Niger Delta. For the majority of the population, there have been very few tangible benefits from the oil industry, with more than half the population continuing to live below the poverty line. Moreover, despite the adoption of transparency mechanisms such as NEITI (Nigeria Extractive Industries Transparency Initiative), the extractive industry value chain (including tendering contracts and administration of the tax regime) in Nigeria remains defined by rent-seeking and corruption (Gboyega et. al. 2011).

The key problem is a lack of capacity on the part of either the government or local civil society groups to adequately monitor extractive industry activities and revenue flows. Lacking the technical and institutional resources to effectively monitor oil industry compliance with regulatory statutes, or even to undertake water and soil sample tests, the Department of Petroleum Resources is effectively dependent on self-monitoring by the extractive industry. As one engineer in the Ministry of Natural Resources and Environment in Akwa Ibom State reported, “The entire figures we have are based on what Exxon Mobil chooses to release to us” (Idemudia 2010, 141). Not only does this situation create a conflict of interest for Exxon Mobil, but it impairs the ability of the state to act as an effective arbiter between conflicting corporate-community claims in the event of environmental damage caused by extractive activities.

3.0 A Policy Agenda for Improving Accountability and Sustainable Development

In case after case, the inability to properly and transparently account for resource revenues in developing countries has opened the door to corruption, rent-seeking, and under-investment in the domestic economy. Efforts to increase accountability in the extractive sector are at risk of losing credibility if they are not able to visibly improve resource governance outcomes. It is therefore of primary importance for policy-makers to develop strategies to enable resource rich economies to efficiently utilize these rents for the development of dynamic and sustainable economic growth.

In terms of economic and fiscal reforms, consistent macroeconomic policies are needed to integrate extractive industries into the broader economy with proper policy sequencing. In order to maximise current and future revenues from extractives to serve as a springboard to finance investments in human and physical capital, host governments must design appropriate tax regimes to obtain a fair share of resource wealth and allocate the proceeds equitably for public spending to create opportunities and services needed to achieve inclusive growth and sustainable development. This necessitates an effective management of natural resources and resource rents and finding the right balance to reconcile competing claims for revenues from extractive industries with longer-term objectives of stable growth and sustainable development.

Beyond these regulatory reforms, strengthening capacity-building among governments and local civil society is a critical policy objective for improved natural resource governance outcomes. The 2013 World Economic Forum on Africa in Cape Town, for example, which convened regional and global leaders from business, government and civil society, highlighted the need for capacity-building as one of the top priorities for leveraging natural resource wealth into positive development outcomes (WEF 2013). These include technical and legal capacity-building on the part of government officials, negotiating capacity, auditing and monitoring

capacity, and skills-training at the local level. The African Capacity Building Foundation's 2013 flagship report, *African Capacity Indicators*, also argues for capacity development as a central policy focus for effective natural resource management, focused on four key areas: 1) policy environment; 2) processes for implementation; 3) development results at the country level; and 4) capacity development outcomes (ACBF 2013).

With these considerations in mind, several policy options for fostering accountability, strengthening capacity, and leveraging extractive resource wealth for more sustainable development and poverty reduction are listed below, focusing on a balance between government (regulations) and industry (CSR).

At the level of national governments:

1. The creation of autonomous and independent monitoring agencies within resource-rich states with the legal authority to identify undervaluation of mineral concessions and track extractive resource revenues. Where there is evidence of systematic underpricing of assets and potentially illegal diversion of resource revenues, independent investigations should be instituted to review the evidence through public hearings. This should be accompanied by regular disclosure of detailed and credible information about resource revenues and reserves accumulated in sovereign wealth funds, as well as the spending and assets of state-owned companies. In Chad, for instance, the Petroleum Revenues Oversight and Control Committee (CCSRP) has earned respect for its reporting on government expenditures of oil revenues (Pegg 2009, 317). Such agencies, however, must be independently resourced in order to retain their autonomy. When such institutional checks are not present, or are politically controlled by the ruling regime, extractive revenues will be more likely to fuel rent-seeking behaviour.

2. Institute wherever possible a transparent system of auctions and competitive bidding for natural resource concessions and licences, and require that any company bidding for mining rights fully and publicly disclose its beneficial ownership, with penalty of exclusion for non-compliance.
3. Simplified and streamlined tax schemes, preferably with a progressive rate structure based on a formula which accounts for global commodity prices. The goal of governments should be to promote strong and transparent *fiscal linkages* between the extractive sector and the broader economy, by using taxes and royalties collected from extractive industries to promote economic development in sectors unrelated to commodities (UNIDO 2012). Taxation schemes should be formed through informed and transparent negotiations with foreign investors to foster greater confidence and trust. Host governments should adopt the practices set out in the *IMF's Code of Good Practices on Fiscal Transparency*. Governments should continually reassess tax provisions and request renegotiation of tax arrangements under contracts that are out of line with international practice and market conditions or generate windfall profits as a result of higher than expected export prices.
4. Creation of stabilization and wealth funds for the explicit purpose of saving extractive resource revenues for future investment. This type of fund is a common fiscal instrument for managing hydrocarbon revenues, and could be profitably applied to other resources within the extractive sector. In Kazakhstan, for example, the National Oil Fund (National

Fund of the Republic of Kazakhstan, or NFRK) was created in 2001 and has since saved 78 per cent of total oil revenues (approximately US\$36.8 billion), stabilizing the level of government spending and reducing the impact of volatile oil prices on the economy (Esanov & Kuralbayeva 2011, 168-69). Resource-rich economies can also look to the successful examples of countries such as Botswana and Norway, which have managed large resource rents by storing them in a “heritage fund” or sovereign wealth fund, typically invested in equities and bonds in other countries (UNIDO 2012). Ideally, such funds will be professionally managed, have clear and transparent guidelines for conditions under which they may be accessed, and be directed through standard budget channels.

5. In parallel with the above point, regulatory frameworks should establish spending and investment requirements which direct a minimum portion of resource revenues towards domestic assets which offset resource depletion, diversify the national economy, and explicitly target job creation. This may take the form of direct equity holding by the state (including joint ventures with the private sector), or by directing favourable loans to the private sector to help foster linkages in the commodity value chain. Extractive rents may also be utilized to improve capacities for attractive investment through expanded training, education, and infrastructure development. For instance, extractive resource revenues can be used for the creation of national venture capital funds with the explicit purpose of assisting small and medium-sized local entrepreneurs and for strengthening economic and business partnerships between foreign investors in the extractive industries and local firms.

6. Harmonization of domestic legislature on the disclosure of extractive sector contracts and payments with transnational transparency initiatives such as EITI, as well as legal frameworks such as Dodd-Frank (Section 1504) and comparable EU legislation for the enforcement of project-by-project disclosure. This should include the elimination of confidentiality clauses in contractual agreements for energy and mineral revenues once the bidding process for mineral concessions is concluded. Harmonization of these various disclosure initiatives should serve as the basis for the adoption of a common global standard for extractive transparency.

7. Develop realistic strategies for linkage development (such as local content policy and capacity-building requirements) which move beyond mere ‘guidelines’ and incorporate tangible incentives and sanctions to improve integration with local economies and expand employment opportunities. These policies can help foster the development of a diversified private sector alongside extractive industries and facilitate stronger integration into regional and global markets. “Beneficiation” strategies, for example, which demand value-addition through on-site and local processing of extractives before exporting, have been successfully pursued in countries like Botswana, Brazil, Indonesia, and South Africa. Importantly, local content policies themselves should be developed in a transparent manner, and avoid ambitious but unrealistic requirements which are likely to be ignored and thus undermine the credibility of local content policy (local content mandates in Angola, for example, are compiled on a somewhat arbitrary basis and far exceed the technological competencies of local suppliers) (Teka 2011).

8. Identify best practices on negotiating foreign investment and concessions in the extractive sector. Invest in capacity-building for negotiating fair and better contracts, and utilize neutral third-parties for assistance in the absence of such capacities, especially in the face of intense pressure from investors to conclude a deal. The issue of strengthening negotiating skills for contracts must be accorded a high priority by host governments since these agreements provide the legal framework for mining concessions that will most probably cover a period of 20 years or more.

At the level of industry (CSR):

1. Where not already undertaken, adoption of international codes of transparency such as EITI and PWYP. These transparency requirements must extend beyond basic royalty payments and revenue management. Additionally, they should include: licensing, contracts, physical resource flows and other production factors, as well as integrate stronger tax evasion agendas to reduce illicit financial flows and manipulation of payment requirements (Le Billon 2011).
2. Permitting independent auditing of corporate resources used for community, environmental, and social initiatives, as well as applicable tax regimes. Accurate measurement of the impacts of CSR programming would be improved through the collection of comprehensive baseline data during the auditing process, as well as the maintenance of accurate records during the course of the resource's extraction.

3. Greater CSR funding directed to support capacity-building programmes which educate citizens in auditing and accounting of public revenues and expenditures. Civil society groups must be equipped with the analytical and technical skills to hold officials accountable (Lawson-Remer & Greenstein 2012).
4. Ensure an adequate, inclusive and transparent consultation process with all local stakeholders including possibilities for procurement of products and services locally through transparent contracting and supplier development schemes, beginning before the development of the resource.
5. Greater efforts to implement corporate responsibility at the project level. Companies must develop greater capacities and enhance technical skills among local managers to ensure ground level standards and actions reflect policy level decisions.
6. At the most general level, extractive industry players should set stronger standards for minimum CSR impacts. For example, the application of a “social justice” benchmark for CSR compliance, where the cumulative impact of extractive operations must have a demonstrable positive benefit to the most vulnerable and impoverished members of affected communities. International companies in extractives should strive to raise standards in all areas of CSR, including health and safety, human rights, governance and environmental and social impact management, committing themselves to international best practice standards where local standards are lower than these.

For both governments and multinational companies, simplicity of revenue-management schemes is also an important consideration. Highly complex or large numbers of spending and revenue-sharing stipulations may overwhelm the capacity of domestic institutions and invite corruption and manipulation (Pegg 2007). Ideally in resource-rich economies these policies will be coordinated and supervised at the highest level of government. Currently, these responsibilities often lie with the ministry responsible for the specific resource (such as in Angola's oil sector and Ghana's gold industry), which is frequently inadequate to the task. Effective policy implementation requires national coordination and cross-ministry buy-in to the larger vision. Similarly, private sector corporations require structured, specific policies which apply across all company divisions (i.e. supply chain management, customer development, etc.) which adhere to a vision of accountability, transparency, and linkage development.

Clearly, the efficacy of policies for improving accountability in the extractive sector is not just a matter of economic and fiscal reforms – it also concerns the political will of governments and, as such, the extent to which politics is intertwined with decisions pertaining to the capture of resource rents. Fundamentally, all actors in the extractive industry must recognize transparency and good governance as over-arching principles at all levels, including resource rich countries, foreign investors in extractives and their home countries, as well as the international banking and financial systems.

4.0 Concluding Remarks

The extractive sector can have substantial multiplier effects on the rest of the economy in resource-endowed countries, if properly managed. Many resource rich countries in the Global South, and particularly in Africa, are far from realizing this ideal largely because of unfair global

extractive regimes, weak governance and lack of transparency. Promoting effective and transparent management of natural resources, and the expectations they create regarding economic development and well-being, remains a formidable challenge. The success of long-term economic transformation will depend on action on all fronts – policies, political processes and partnerships. At the policy level, a coordinated and integrated global value chain approach to mineral resource development is necessary. It is important to move away from a narrow perspective which considers the extractive sector as an enclave in the economy, towards a more comprehensive one which focuses on the linkages with local businesses and other productive sectors. At the political level, development-committed leadership and good governance are necessary for decoupling the interest of a few from the pursuit of the broader collective interest in economic transformation.

Beyond good policies at national and industry levels, making extractive resources work for development will also require building constructive partnerships based on trust, mutual interests, and common understanding of challenges and opportunities. They will also require a correction of the current imbalance between international and national regulatory frameworks for natural resource governance. The G20, OECD and the EU for their part have been active in advocating policies and driving actions to promote good governance and revenue transparency in international transactions in the extractive sector. For example, the conclusions of the 4th High Level Forum on Aid Effectiveness, the Busan Partnership for Effective Development Cooperation contained a new framework for cooperation which places a high priority on transparency and accountability. The Australian and Canadian governments are also partnering with the African Union, the UNECA and the African Development Bank in the establishment of the new African Minerals Development Centre to promote the implementation of the African

Mining Vision and Action Plan, which prioritize the development of economic linkages and sustainable development through extractive resource exploitation.

Harnessing the potential of natural resources for sustainable economic growth and poverty reduction is among the foremost priorities for development in the Global South. Maximizing the value of a country's natural resources while minimizing the potential for harmful environmental and social outcomes should be at the highest priority of national development for countries with significant resource endowments. This calls for considerable policy innovation in the areas of rents, taxes and benefits for creating long-term reliable revenue streams and beneficiation modalities. At the same time, extractive industries must increasingly demonstrate social responsibility and transparency in their areas of operation. Building partnerships, based on trust, mutual interest and equality is necessary to support the development aspirations and goals of the Global South and moving the agenda forward.

References

- African Capacity Building Foundation (ACBF), *African Capacity Indicators 2013: Capacity Development for Natural Resource Management*, African Capacity Building Foundation, 2013.
- African Development Bank, *Development Effectiveness Review 2012: Growing African Economies Inclusively*, African Development Bank Group, Tunisia, 2012.
- African Development Bank, *Natural Resource Management and Structural Transformation in Africa* Information Note, Board Seminar, Tunis, 2013.
- Africa Progress Panel, *Equity in Extractives: Stewarding Africa's natural resources for all*, Africa Progress Report, Geneva: APP, 2013.
- Akabzaa, Thomas, "Mining in Ghana: Implications for National Economic Development and Poverty Reduction." In Bonnie Campbell (ed.), *Mining Africa: Regulation and Development*, Pluto Press, New York, 2009.
- Boas and Associates, *Ghana EITI First Aggregated Report: The aggregation/reconciliation of mining benefits in Ghana*, Available at: http://www.geiti.gov.gh/downloads/first_aggregator_report.pdf, 2007.
- Brookings Institute, *Conflict Minerals: An Assessment of the Dodd-Frank Act*. Available at: <http://www.brookings.edu/research/opinions/2011/10/03-conflict-minerals-ayogu>, 2011.
- Campbell, Bonnie, *Mining in Africa: Regulation and Development*, Pluto Press, International Development Research Centre, Ottawa, 2009.
- Collier, P. & A. Venables, *Plundered Nations? Successes and Failures in Natural Resource Extraction*, New York: Palgrave Macmillan, 2011.
- Curran, M. M. & Moran, D., "Impact of the FTSE4Good Index on firm price: An event study," *Journal of Environmental Management* 82 (4): 529-53, 2007.
- Esanov, A. & K. Kuralbayeva,. "Kazakhstan: public saving and private spending," In Collier & Venables (eds.), *Plundered Nations?* 2011.
- Frederick, W.C., Post, J.E. and Davis, K., *Business and Society: Corporate Strategy, Public Policy and Ethics*, 7th ed. McGraw-Hill Inc.: New York, 1992.
- Frynas, J.G., "The false developmental promise of Corporate Social Responsibility: evidence from multinational oil companies," *International Affairs* 81 (3): 581-598, 2005.
- Global Witness, *A Crude Awakening: The Role of the Oil and Banking Industries in Angola's Civil War and the Plunder of State Assets*, Global Witness, London, <http://www.globalwitness.org/sites/default/files/pdfs/A%20Crude%20Awakening.pdf>, 1999.
- Gboyega, Alex, Tina Soriede, Tuan Minh Le & G.P. Shukla, *The Political Economy of the Petroleum Sector in Nigeria*, The World Bank Africa Region Public Sector Reform and Capacity Building Unit, Policy Research Working Paper, 2011.
- Government of Canada, "Minister Oda announces initiatives to increase the benefits of natural resource management for people in Africa and South America." Canadian International Development Agency, Available at: <http://www.acdi-cida.gc.ca/acdi-cida/ACDI-CIDA.nsf/eng/CAR-929105317-KGD>, 2012.

- Hamann, Ralph, and Paul Kapelus, "Corporate Social Responsibility in Mining in Southern Africa: Fair Accountability or Just Greenwash?" *Development* 47 (3): 85-92, 2004.
- Heuty, Antoine, *Can Transparency Transform Mineral Wealth into Wellbeing?* Revenue Watch Institute, Available at: <http://www.revenuewatch.org/sites/default/files/MineralWealthintheMaghreb.pdf>, 2012.
- Idemudia, Uwafio, "Corporate Social Responsibility and the Rentier Nigerian State: Rethinking the Role of Government and the Possibility of Corporate Social Development in the Niger Delta," *Canadian Journal of Development Studies* 30 (1-2): 131-153, 2010.
- International Monetary Fund (IMF), *Regional Economic Outlook: Sub-Saharan Africa: Sustaining Growth amid Global Uncertainty*, World Economic and Financial Surveys. Washington, D.C. <http://www.imf.org/external/pubs/ft/reo/2012/afr/eng/sreo0412.pdf>, 2012.
- Jenkins, H. & Obara, L., *Corporate Social Responsibility (CSR) in the mining industry – the risk of community dependency*, Proceedings of the Corporate Social Responsibility Conference, Available at: <http://www.crrconference.org/downloads/2006jenkinsobara.pdf>, 2006.
- Kaufmann, Daniel, "Poverty in the Midst of Abundance: Governance Matters for Overcoming the Resource Curse," The Brookings Institute, <http://www.brookings.edu/research/opinions/2012/09/13-poverty-governance-kaufmann>, 2012.
- Kolk, Ans & Francois Lenfant, "MNC Reporting on CSR and Conflict in Central Africa." *Journal of Business Ethics* 93(2): 241-255, 2010.
- Le Billon, Philippe, "Extractive sectors and illicit financial flows: What role for revenue governance initiatives?" CHR Michelsen Institute, No. 13, 2011.
- Lawson-Remer, Terra & Joshua Greenstein, *Beating the Resource Curse in Africa: A Global Effort*, Council on Foreign Relations (August), Available at: <http://www.cfr.org/africa/beating-resource-curse-africa-global-effort/p28780>, 2012.
- Mbat, David, Enefiok Obok, Ekong Daniel & Akpa Campus, "Exxon-Mobil and Corporate Social Responsibility in Akwa Ibom State, Nigeria: Past and Present," *Public Policy and Administrative Research* 3(3), 2013.
- Newell, Peter, "Citizenship, Accountability and Community: The Limits of the CSR Agenda," *International Affairs* 81 (3): 541-557, 2005.
- Nwete, Bede, "Corporate Social Responsibility and Transparency in the Development of Energy and Mining Projects in Emerging Markets; Is Soft Law the Answer?" *German Law Journal* 8 (4): 311-340, 2007.
- Pegg, Scott, "Chronicle of a Death Foretold: The Collapse of the Chad-Cameroon Pipeline Project," *African Affairs* 108/431: 311-320, 2009.
- Revenue Watch Index, *Transparency: Governments and the oil, gas and mining industries*, Revenue Watch Institute, Available at: <http://www.revenuewatch.org/rwindex2010/index.html>, 2010.
- Ross, Michael, *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations*. Princeton: Princeton University Press, 2012.
- Sagebien, Julia and N. M. Lindsay, *Governance Ecosystems: CSR in the Latin American Mining Sector*. New York, NY: Palgrave Macmillan, 2011.

- Teka, Z., *Backward Linkages in the Manufacturing Sector in the Oil and Gas Value Chain in Angola*, MMCP Discussion Paper No. 11, Cape Town, University of Cape Town, 2011.
- Tsui, Kevin K., "More Oil, Less Democracy: Evidence from Worldwide Crude Oil Discoveries." *The Economic Journal* 121 (551): 89-116, 2011.
- United Nations Industrial Development Organization (UNIDO), *Promoting Industrial Diversification in Resource Intensive Economies: The Experiences of Sub-Saharan Africa and Central Asia Regions*, Vienna International Centre, Vienna, 2011.
- UNECA and Africa Union Commission, *Unleashing Africa's Potential as a Pole of Global Growth*, Issues Paper E/ECA/COE/31/3 and AU/CAMEF/EXP/3(VII), Addis Ababa, January 2012.
- US Geological Survey Minerals Yearbook, 2010.
- Ushie, Vanessa, *Dodd-Frank 1504 and Extractive Sector Governance in Africa*, The North-South Institute, Policy Brief, 2013.
- Warhurst, A. (ed.), *Mining and the Environment: Case Studies from the Americas*, International Development Research Centre, Ottawa, 1999.
- World Economic Forum, *World Economic Forum on Africa: Delivering on Africa's Promise*, Conference Report, Cape Town, South Africa, May 2013.
- Yakovleva, N., *Corporate Social Responsibility in the Mining Industries*. Hampshire: Ashgate Publishing, 2005.