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The role of the private sector in achieving Canada's international development interests

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Thank you for this opportunity to address the Committee on what is a most important and timely subject.

My contribution will be centred on the relationships between mining and development and will draw on several decades of research concerning investment in the mining sector, the reform of regulatory frameworks and the contribution of mining to social and economic development in Africa. It draws as well on my participation as a member of the Advisory Group to the National Round Tables on CRS in 2006-2007 and as a member over the last four years of the International Study Group created in 2007 by the United Nations Economic Commission for Africa (UNECA) which released its report in December 2011. This study, *Minerals and Africa's Development. The International Study Group Report on Africa's Mineral Regimes*, is now an official of report of the African Union and UNECA.

In my brief presentation I would like to make three points and conclude with 6 recommendations.

1. **First and as someone who has worked in the area of international development for some thirty years, I would like to question a central premise of much of the ongoing discussion.**

For the past two decades, the thinking and strategies concerning developing mining activities have rested on the hypothesis that <u>investment</u> in the mining sector would drive <u>growth</u> which would bring <u>development and reduce poverty.</u>

This was the hypothesis at the origin of the World Bank studies on Africa (1992) and Latin America (1996) which translated into policy recommendations that ushered in very important reforms notably concerning the reform regulatory frameworks for mining and the liberalization of the sector.

In October 2008, the First African Union Conference of Ministers Responsible for Mineral Resources Development adopted a document called the "African Mining Vision" which in February 2009, was adopted by the African Union Heads of State and Government of the entire continent. This document notes in its introduction:

> "Africa's efforts to transform the mining sector away from its colonial – created enclave features have so far met with very limited success ."

I shall come back to why this is the case and what can be done about it in my second point.

In the Canadian context, the problematic assumption about the role of investment in international development is illustrated in a statement by Pierre Gratton, President and CEO of the Mining Association of Canada (Embassy Magazine, 15. 02 2012):

> "In the long term, sustainable growth and prosperity are driven by the private sector, and forward thinkers in the development aid policy field recognize that the effectiveness of aid can be enhanced when aligned with private sector investment."

This affirmation is at the root of the erroneous formulation of arguments put forward to justify current strategies, of a lack of awareness of important debates in this area led by decision makers, notably in Africa, and more deeply, of a clear misconception of what is at stake when it comes to issues related to international development.

Let's begin with a fact:

Investment by the private sector of itself does not translate into sustainable economic and social development. There is no historical example anywhere on the earth where sustainable growth, social and economic development and poverty reduction took place through private investment ***in the absence*** of appropriate public policies and state interventions needed in order to plan strategically, regulate and monitor investment, in order that the presence of the private sector be harnessed to meet the development objectives determined by the country concerned.

2. Listening to where policy discussions and proposals are at in Africa.

If we are concerned about the policy relevance and effectiveness of current Canadian initiatives with regard to mining and development in Africa, it is essential to pay very serious attention to the recommendations which have been put forward by processes which are driven by African experts and decision makers and which have been adopted by the African Ministers of Mines and Heads of States of the African Union.

Recognition of the failure of investment-led strategies in the mining sector to contribute to development is documented in the recent UNECA report which notes in its introduction that "the major problems confronting Africa in the field of natural resource development" more than 30 years ago when the Organization of African Unity, the precursor to the African Union (AU) adopted the Lagos Plan of Action for the economic development of Africa, "ring familiar today."

This recognition is at the origin of the very fundamental shift in thinking which has taken place concerning the role of the mining sector in development in Africa. It has been accompanied by a process of in-depth analysis concerning why the past model was inappropriate, why it is now outdated, and what changes should be made. This has led to the emergence of African perspectives in this area in response to the continuing challenges. It is of paramount importance that Canadian actors and notably CIDA be attentive to where thinking and expectations are now on the continent.

The reforms, regulatory frameworks and institutions introduced over the last 20 years to open the mining sector of mineral rich countries of Africa to investment pursued specific objectives –

- The focus was on mining in abstraction of broader development considerations.

- The reforms were undertaken overwhelmingly from the perspective of mining companies rather than that of promoting development strategies.

- The contribution of mining activities to the local economy was seen to be tax revenues and foreign exchange receipts rather than developing linkages and countries were encouraged to be competitive which meant low taxes and generous incentives.

- Environmental consequences of mining activity, and subsequently, social impacts which were in fact much less developed than other aspects of regulatory frameworks, were seen as side effects, considered as secondary and marginal to the positive consequences. It was assumed that they could be regulated by the introduction of voluntary performance standards for which the responsibility was seen to rest above all with companies.

- Above all else and most important – was the stringent retrenchment of state which took place, the new delineation between public and private spheres of authority and the transfer of what were previously public responsibilities to private actors. The private sector was to become “owner and operator” – the role of government was relegated to that of facilitator and promoter.

The assumption put forward was that investment would bring growth and translate into development.

This has not happened.

As is well known, the particular forms which the liberalisation process took resulted in major cuts in royalty levels, a reduction or a disappearance of other tax measures (see Ghana)[1], increased fiscal exemptions, which resulted in a relative decrease in the portion of revenue which theoretically could be claimed by governments from productive activities in the sector.

Moreover, the liberalisation measures withdrew governments from the sphere of production thereby reducing or putting an end, on the one hand to access to basic statistical information which they had had previously. On the other, the decreased administrative capacity of governments contributed to a weakening of the capacity of control and enforcement of states. Together these dimensions contributed to the possibility of an increase in the transfer of revenue

[1] With regard to the liberalisation of the Ghanaian mining code in 1986, it is helpful to recall, that corporate income tax, which stood at 50-55% in 1975, was reduced to 45% in 1986, and further scaled down to 35% in 1994. Initial capital allowance to enable investors to recoup their capital expenditure was increased from 20% in the first year of production and 15% for subsequent annual allowances in 1975 to 75% in the first year of operation and 50% for subsequent annual allowances in 1986. The royalty rate, which stood at 6% of the total value of minerals won in 1975, was reduced to 3% in 1987. Other duties that contributed significantly to government revenue from the sector before the reforms, such as the mineral duty (5%), import duty (5-35%), and foreign exchange tax (33-75%), were all abolished. See T. Akabzaa in B. Campbell (ed.) 2004. ***Regulating Mining in Africa : For Whose Benefit?.*** Coll. Discussion Paper 26. Uppsala : Nordiska Afrikainstitutet,.and T. Akabzaa in B.Campbell. (ed.). 2009. *Mining in Africa : Regulation and Development*. Copublication London : Pluto Press, Ottawa :IDRC, and Uppsala : NAI.

abroad, whether through licit measures (transfer pricing, etc.) or illicit measures. The materialization of such trends is now well documented.

The impact of the liberalisation measures on institutional arrangements and political processes and the strong retrenchment of the state from the mining sector have been accompanied by an ongoing process of the reduction of state sovereignty.

These far reaching trends have had important implications for the operations of companies – notably by contributing to a legitimacy problem for companies. Why?

Weakened states in mineral rich countries were caught between the competing imperatives of attracting foreign investment and at the same time responding to national and local concerns, with their latitude for action often circumscribed by the legal and practical conditions set out in reformed regulatory frameworks. Among the coping strategies adopted by governments to deal with new mining regimes has been one of the 'retreat of the state' or of 'selective absence'. The state basically absented itself from substantial parts of the legal regimes intended to help mediate between investors and community interests.

The liberalization of the mining sector has thus led increasingly to the delegation or transfer of what in the past were public functions of the state to private operators. These include service delivery and also rule-setting and implementation. The tendency has been for an increased assumption of state-like responsibilities by transnational mining enterprises at the discreet behest of weak governments. While such trends may allow governments to shift the locus of responsibility for what were previously considered state functions (such as clinics, roads, infrastructure and security) to the private operators of large-scale mining projects and NGOs, and help explain the pressures on companies to engage in CSR, such transfers not only silence the legitimate and indeed necessary right of governments to offer services to their populations, a precondition to their being held publicly accountable, they also contribute to obscuring the issue of government responsibility itself. The current sidestepping of the state, by suggesting companies can gain better legitimacy for their operations by offering social services, runs the risk of undermining a precondition for building responsible governments and the basis of democratic practice: the need for governments to be accountable to their populations.

These past patterns - the enclaved, mono sectoral nature of mining activities, the weakened institutional capacity and profoundly asymmetrical relations between the negotiating capacity of governments and companies which have resulted are part of a heritage which is now deeply questioned and in fact contested.

Discussions at UNECA and AU which have taken place since 2007, have given rise to a very fundamental shift in thinking concerning the role of the mining sector in development in Africa. It has been accompanied by a process of in-depth analysis concerning why the past model was inappropriate, why it is now outdated, what changes should be made.

What are some of the implications of the message which is being put forward?

As opposed to the former essentially monosectoral approach, the African Mining Vision foresees, "A mining sector that has become a key component of a diversified, vibrant and globally competitive industrialising African economy."

However, there is no historical experience of industrialisation taking place without appropriate policies. The right policies and strategies are critical to create the dynamic changes required including building eventual backward and forward linkages and the possibility of value added processing of minerals. This will require a resolutely multi sectoral approach involving redefined institutional arrangements. One chapter in the report brings this out above all the others. Chapter 8 "Optimizing Mineral-based Linkages" of the ISG Report provides the strategic policy recommendations necessary to spur the impetus for the transformative changes which are required. Each of the eight major areas of policy reform will require strategic public policies[2]

[2] Policy reforms in Chapter 8 can be summarized as follows.

More consciously and consistently <u>integrating mineral policy into development policy</u>. This involves a shift away from the traditional (practically exclusive) focus on mineral extraction.

<u>Enhancing primary sector integration into the broader economy</u>. Building backward and forward linkages requires complementary strategies, primarily creating the business environment and public sector institutions that foster growth. Second is—as far as governments can—setting terms on access to mineral resources that both impose linkage conditions on mineral rights holders and provide incentives for investors to structure projects in ways that deepen the integration of mineral projects into the broader national and regional economy. Reasonable national local content and value-addition milestones need to be incorporated in mining regimes.

<u>Promoting mineral beneficiation before export</u>. The pursuit of downstream processing of minerals before export should not be placed at the top of the national agenda for the minerals industry in isolation. Beneficiation contributes to growth and diversification only when it generates above-average upstream and side-stream linkages, and should not be pursued merely because a country is endowed with mineral resources. Although some countries have used export taxes to promote downstream processing, experience is mixed and such taxes need to be applied judiciously, possibly only after an independent study has indicated that investment in the next value-addition step is feasible. (New trade agreements, particularly the Economic Partnership Agreements with the European Union, are likely to complicate use of this instrument—chapter 9.)

<u>Directing attention to developing upstream capital goods and service industries</u>. This is critical for employment generation and for generating new products and processes.

<u>Enhancing local linkage development through local participation and empowerment models</u>. Many benefits can flow from local participation and empowerment models.

<u>Extending economic infrastructure</u>. Funding and driving the establishment of economic infrastructure, particularly power and transport, is critical in prudent mineral development.[2] Policymakers need to maximize the beneficial spillover effects of infrastructure triggered by mining through resource corridors. Planning needs to explore the collateral or integral use by other economic sectors. Mineral infrastructure needs to allow third-party access at non-discriminatory tariffs. Expanded infrastructure will also promote rural development.

<u>Developing human resources and fostering innovation</u>. Effort needs to be directed to expand higher technical skills required by the minerals industry. Public support is required for innovation in fields related to natural resource exploitation through national innovation systems, such as tax incentivization of local R&D and technical human resource development, as well as the allocation of some resource rents to developing technological linkages.

<u>Pushing regional integration</u>. The gradual movement towards regional integration would go some way in overcoming barriers to establishing linkages, through creating regional common markets (customs unions). African governments need to dismantle the numerous impediments to intraregional trade in order to realize the larger regional markets and to overcome the high barriers to entry that are related to poor economies of scale for many mineral backward and forward linkage opportunities (discussed further in chapter 9). In order to soften currency appreciation (Dutch Disease) and to access regional markets, South Africa's New Growth Path[2] has mooted creating an African Development Fund to invest in regional infrastructure and so stimulate intraregional trade and investment.

without which there will be no transformative change. And this brings us to the most fundamental issue.

The policy recommendations of each one of the chapters of the UNECA report point in a similar direction. The new model cannot be driven merely by industry, the hypothesis of the past, but its realization will depend on locally owned national and regional policies. And there is an essential ingredient that is needed in order that such policies may be implemented: a "developmental state".[3] To place this observation is the current context, it should be underlined that the last UNECA Economic Report on Africa 2011 which concerns economic development more generally, " Governing development in Africa - the role of the state in economic transformation" (published by the Economic Commission for Africa, Addis Ababa, 2011, 130 pages) was precisely on this subject.

In contrast to the policies of state retrenchment which have been introduced and which have provoked the development implications which we know and as the Executive Secretary of the UNECA Mr Abdoulie Janneh has suggested, what is needed is an effective developmental state with "clear visions of development paths and coherent, consistent and coordinated planning frameworks." Only such states can be at the center of transforming Africa's economies from dependency on primary commodities to value addition processes which will spur Africa's industrialisation. This will entail a return to planning which has been largely replaced by policy prescriptions that are externally determined. Economic planning is critically important and if human resources in this area do not exist, it is essential to invest in them and create planning ministries or departments that can draft strategic and comprehensive development plans.

Public involvement is necessary as well for the provision of essential services such as a good transport system and reliable energy supplies, good education and health systems. It is also important that the state participate in strategic industries which will open the path to industrialisation. A greater involvement of the state is critical in other areas such as the taxation system. Rather than be a source only of revenue as in the past, taxation systems can be used as a transformative tool. For example, when tax levels vary inversely with the degree of local transformation, they become an incentive for encouraging local beneficiation.

3. Canada's role in contributing to international development

Should CIDA funds be used for NGOs partnering with Canadian mining companies? Absolutely not. Five reasons:

a) If the experience of the reform of the African mining sector over the last two decades has taught us one thing, it is that the perpetuation of the past investment-led strategies which tend to

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(See also, Jourdan, 2010, for a proposal for an African regional development fund to support long-term regional physical and knowledge infrastructure).

In conclusion, successful linkage development relies on simultaneous multi-factor promotion: skills, savings, business performance, governance, pricing, policy making and implementation capacity. It is also premised on maximizing the development impact of a resource endowment by optimizing potential investor market interest in realizing wide-ranging linkages, given the demand for specific resources at a given time.

[3] UNECA, *Economic Report on Africa 2011.* "Governing development in Africa - the role of the state in economic transformation". Published by the Economic Commission for Africa, Addis Ababa, 2011. 130 pages.

by-pass governments and undermine democratic process, cannot promote sustainable social and economic development in the future.

b) In order to contribute to development objectives in the mining sector, it is essential that CIDA embrace the shift of paradigm which has been called for by African governments and ensure that its policies support the call for transformative measures which will contribute to industrialising African economies and in this way contribute to democratization and more equitable and sustainable social and economic development.

c) Current partnering strategies which propose to use aid budgets to reinforce CSR run the risk of further blurring the lines of responsibility and accountability between public and private actors, hence perpetuating and even aggravating problems of legitimacy.

d) Such externally initiated CSR strategies could reduce the motivation of government to fulfill its responsibilities to its citizens and the latter could come to see the company as the provider of those services for which they should be looking to the state.

e) A thorny issue posed by the expectations of CSR in community development is defining the boundary between the state's responsibilities to its citizens and how mining company's CSR complements the state's efforts. In many African countries, the coordination between state planning and investment and CSR investments is inadequate. Better coordination between planning and investment of the state and corporate outlay under CSR could improve the value of both streams of expenditure. For example, the sustainable use of a school or clinic built as part of CSR is better assured if the project is coordinated with the state—to ensure that it fits into a larger plan and that the state can support health staff or teachers should the mine cease its support.

To summarise, CSR initiatives should not be considered a substitute for government responsibility towards its citizens in providing basic infrastructure and other public goods. Indeed, CSR initiatives should complement government efforts through local government institutions and local authorities. But before this takes place, there must be in place appropriate frameworks which are part of and result from a national policy debate on the mining industry's obligations regarding social development objectives. Without such debate, there is danger that the CSR requirements in a jurisdiction will be left to the industry to determine. Such an ad hoc approach would lead to uncertainty of how much should be spent on CSR and what types of CSR projects should be developed as well as the mechanisms for their development. Indicators around assessing the impact of good CSR projects must be built into the framework and applied by a range of stakeholders, such as civil society. The framework must focus on stakeholder consultation and allow for review of obligations and commitments. This review must be based on reporting requirements that should be part of the CSR framework.

The last three points are in fact the recommendations which are put forward by the recent Report of the UNECA.[4]

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[4] African Union and UNECA *Minerals and Africa's Development. The International Study Group on Africa's Mineral Regimes*, Chapter 6, "Corporate Social Responsibility Initiatives," 2011, pp 81-89.

They underscore the imperative need to recognise the legitimacy and indeed the right of governments to provide services to their population which are also the condition for them to be held accountable. They also underline the importance of the mandate of bilateral aid agencies, such as CIDA, which through their programmes, seek to reinforce the medium and longer-term development objectives, promoted through strategies put forward by the countries concerned and again, for which their governments are held accountable.

CIDA's thematic focus on sustainable economic growth raises the potential for important initiatives by the Agency that address the economic conditions that sustain poverty and inequality. In order to succeed in the mining sector, it is essential that CIDA embrace the shift of paradigm which has been called for and ensure that its policies support and not undermine the call for transformative measures which will contribute to industrialising African economies and in this way contribute to more equitable and sustainable social and economic development.

Recommendations

1. CIDA should not entwine its mission with the public relations interests of Canadian companies and partnering NGOs but concentrate on strengthening developing country government institutions to carry out the visions they have themselves developed with accountability to their own citizens.
2. Canada should be attentive to and seek ways of supporting current initiatives of the UNECA and African Union in ensuring that mining activities contribute to development by reinforcing country owned policies and strategies in this area.
3. In keeping with the U.N. Protect, Respect and Remedy Framework, Canada should issue a policy statement expressing its expectation that Canadian companies comply with host country laws and that they fulfill the corporate responsibility to respect internationally protected human rights. Canada should explore mechanisms to compel corporate compliance with these norms.
4. At present there is no overall framework to ensure oversight of government agencies which become involved in promoting the role of the private sector in achieving Canada's international development interests as Bill C 300 attempted to do. Such a framework which sets out clear guidelines and procedures for monitoring and evaluation should be put in place in order that government agencies act responsibly and may be held accountable.
5. Canada should create an independent, effective and transparent non-judicial complaint mechanism, as recommended in the National Roundtable report (2007). This office should be mandated to make public findings of fact regarding extractive operations. The participation of companies in such investigations should be mandatory.
6. Those companies found to be in non-compliance with international human rights norms (or internationally recognized standards of best practice), should become ineligible for financial and political support from the Government of Canada.

Thank you for your attention.

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