Broadening the scope of governance assessments

Civic space and comprehensive transparency build foundations for stable mining projects


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For too long, conceptions of investment attractiveness and risk in the extractive sector have been largely zero-sum. Investment attractiveness metrics give boosts for minimal government regulation, and investment risk models allocate penalties for significant government take and discontent. This can foster a problematic implicit message: that investment benefits when governments and citizens have a smaller role in the sector. This message should be challenged.

Extractive industries are coming under growing scrutiny due to environmental and civic space concerns. In this context, mining investors that want to maximise long-term commercial returns should reframe their investment analysis to emphasise reducing a variety of harms in host countries and identifying appropriate levels and types of regulation that increase shared benefits between commercial and public actors. This requires a broader approach to assessing governance.

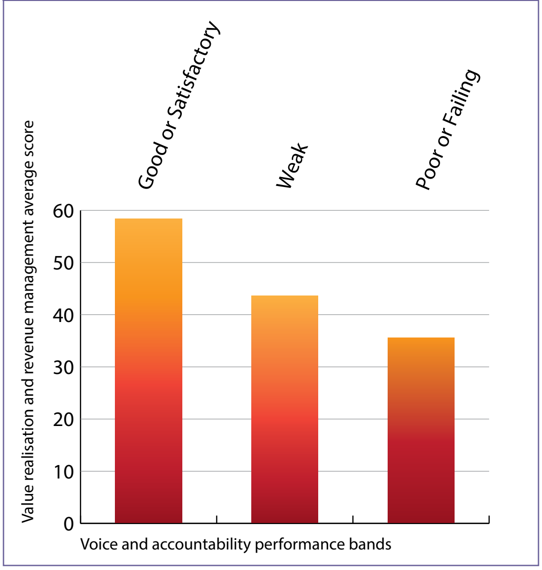
Market pressures are driving such broader integration of governance factors in mining-sector risk analysis; this is signalled by several risk agencies' use of Worldwide Governance Indicators. Among others, the growing demand for battery metals used in electric vehicles, renewable energy storage, and mobile phones has brought increasing consumer concerns about conflict and child labour linked to these materials.

The result has been a surge in the number of mineral supply chain risk frameworks that seek to monitor conflict and human rights violations. Monitoring these factors is essential, as they represent some of the most harmful circumstances surrounding mining. But an even more comprehensive approach would also give significant weight to monitoring two broader governance factors: civic space and transparency.

Civic space risks and opportunities

Civic space is the freedom and ability of citizens to influence the political and social structures around them. Civic space and good governance in the extractive sector are highly interrelated. The 2017 Resource Governance Index indicates that the absence of civic space goes hand-in-hand with opacity and

Countries with good or satisfactory voice and accountability perform better in extractives value realisation and revenue management



NRGI was not involved in the computation or analysis of the Investment Risk Index within the World Risk Report poor governance of extractive resources and that, on average, countries where civic space is strong exhibit stronger extractives governance performance.

According to monitoring group Civicus, civic space is highly constrained in many resource-rich countries, meaning that members of mining-affected communities are often not free to express their views during company consultation processes.

This undercuts the entire purpose of such consultation and can reduce the sustainability of these projects. Further, our analysis suggests that where civic space is constrained, corruption risks tend to be significantly higher, in turn resulting in the lack of implementation of laws and policies in extractives, and in higher investment risks.

To develop a more accurate sense of the medium and long-term risks of poor government accountability and social discontent, investors should take into account the freedom of civil society actors and other stakeholders to express their views and concerns about natural resource governance. Related to civic space, corruption risks need to be fully integrated as well.

In addition to calculating risks, smart investors will spot opportunities that are likely to pay off, at least in the medium term. Extractive companies can make important contributions to the governance of host countries by supporting and complying with recognised good governance standards in the execution of their projects; this includes regard for civic space.

A growing number of companies are sending a strong signal by withholding investment until conditions improve. More generally, companies should explore ways to facilitate civic space in host countries, such as partnering with civil society organisations in multi-stakeholder initiatives and proactively speaking out against infringements on civic space. More empirical analysis about how civic space factors impact commercial operations would also be additive.

Transparency troika

Investment risk assessments often focus on the presence or absence of transparency mechanisms that facilitate commercial clarity, such as on permitting and judicial procedures. While this is important, investors should also consider a much broader aspect of transparency: its role in increasing public understanding and accountability in the sector.

> "Mining-affected communities are often not free to express their views"

An increase in environmental, social, and governance (ESG) investing has helped to raise the bar on certain aspects of publicly relevant transparency, especially on critical environmental issues. Too often, however, ESG investing frameworks fail to emphasise transparency and best practice on some of the drier, but equally socially important aspects of extractive projects. In this respect, investors should track best practice on the disclosure of 'transparency troika' basics – who (beneficial ownership), what (contracts), and how much (project-level payments).

Hidden beneficial ownership often plays a central role in extractive sector corruption, particularly during the allocation of licenses and contracts. NRGI analysed over 100 cases of corruption in extractive sector license and contract allocations, and found that over half involved hidden beneficial owners who were government officials or their close associates (known as 'politically exposed persons' or 'PEPs').

The Extractive Industries Transparency Initiative (EITI) has established ambitious milestones for beneficial ownership transparency. By 2020, more than 50 EITI countries must publicly disclose beneficial ownership and PEP information for companies that apply for or hold extractive licenses or contracts.

Investors should proactively monitor country progress on implementing beneficial ownership transparency regimes in their extractive sectors and extractive companies should make timely and comprehensive beneficial ownership disclosures.

Contract transparency presents an important avenue for citizens and communities to hold both public officials and company representatives accountable for the deals they make. When negotiators know that the outcome of their work will be public and subject to legal, public and commercial scrutiny, they have powerful incentives to draft more carefully, which can reduce the likelihood of conflicts down the line.

NRGI has tracked nearly 40 countries that have disclosed extractive industry contracts and Oxfam found at least 18 leading extractives companies including Rio Tinto, Freeport-McMoRan, BHP, Goldcorp, Newmont Mining, Barrick Gold and Vale have recently developed policies supporting contract disclosure.

Along with disclosure of ownership and contracts, publication of payments made from companies to governments complete the troika. Over 30 international investors with more than $5 trillion in assets under management have documented their support for Canadian, EU and US payment transparency rules, specifically noting risk reduction as a basis for such support.

Companies should support mandatory payment transparency rules, comply with any reporting regime under which they are subject to payment transparency requirements (including, but not limited, to Chapter 10 of the EU Accounting Directive and the Extractive Sector Transparency Measures Act in Canada), and provide links to disclosures made in accordance with each regime.

By focusing on strong civic space and implementation of the transparency troika and thereby reducing corruption risks, investors can do more to mitigate operational risk and optimise outcomes for citizens.

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