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THE McLEOD GROUP

OF MINES AND MINEFIELDS: CANADA, THE EXTRACTIVE SECTOR & DEVELOPMENT

A McLEOD GROUP
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A McLeod Group Foreign Policy Perspective

One of the most controversial issues facing Canada in coming years will be the country's role in the booming extractive industries of the developing world. A rich country, but in many ways still a metaphorical hewer of wood and drawer of water, Canada has taken on an important role in the fast-growing global trade in minerals, and is today a mining superpower. About half of all mining capital in the world is raised on the Toronto and Vancouver Stock Exchanges. Canadian mining companies have an accumulated stock of $56 billion in direct foreign investment abroad (primarily in the U.S. and Latin America) fuelled by the recent boom in commodity prices.[1]

The extractive sector has played an important role for two centuries in Canada's growth, our wellbeing, and our place in the world. Canada is blessed with the capital, the technology, and the entrepreneurial expertise to play a leading role in this sector globally. Some would say that Canadian mining corporations are among the best-behaved internationally as well.

Yet controversy stalks this issue. Debate is heated and polarized between equally passionate pro- and anti-mining forces. The commodities boom has been accompanied by an upsurge of anti-mining protests throughout the developing world, and Canadian-based corporations are often the target. From Suriname to El Salvador, from Papua New Guinea to the Democratic Republic of Congo, Canadian companies have been embroiled in costly and damaging scandals encompassing all manner of bad practice, including corruption, environmental destruction and human rights abuse, running roughshod over local laws and supporting unsavoury despots.

Too often the issue of good practice by foreign mining companies operating abroad—whether Canadian or otherwise—has been reduced to tokenistic and well-meaning acts of corporate social responsibility. In this paper the McLeod Group argues that Canada's role should be about much more than that. The paper sheds light on the debate about the relationship between the extractive sector and development assistance and it explores constructive roles Canadian industry and governments can and should play.

The Context: The Mining Minefield

Canadian companies have a strong interest in such dry and seemingly unconnected things as support for anti-corruption measures, adherence to environmental laws or the ability of a developing country to create and enforce equitable taxation regimes. The best companies learned this long ago. Why? Because in fostering local institutions and laws, these companies help to secure a more stable and predictable investment climate for themselves and their shareholders. In short, doing the right thing makes for good business relations. Development assistance agencies can also play an important role here. Instead of supporting small NGO projects that might be seen as contributing to Canadian companies' bottom lines, CIDA could help to strengthen developing countries' institutions so that these countries can regulate extractive industries, provide benefits to local populations, and encourage respect for international conventions and industry standards.

But there's more to it than that. Who will stand up for the rights of local communities when a bad government joins forces with a ruthless and impatient company? This is where international oversight is indispensable.

These are challenging issues that have too often been overlooked by companies and policy makers. This needs to change. Developing countries should no longer be seen as a place of expedient profiteering, where foreign companies can operate in ways that would never be tolerated in their home countries.

Institution-making—or in some cases effective institution-*supporting*—takes time. But the win-win situation that comes from a stable investment climate and positive development outcomes will elude the Canadian government and Canadian companies if they take short cuts, or insist that there is no need for transparency and accountability. Countries with responsibly managed resources (including legacy funds which have benefitted the wider public good) did not achieve their success by accident. Principled adherence to a long-term, well thought-out, public policy wins the day. Just ask diamond-rich Botswana.

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As Canadians wrestle with the question of how the country can contribute to the debate about extractives and development, both industry and policymakers would be wise to identify and apply practices that advance sustainable business and development outcomes in poor countries—not just a self-interested trade agenda.

Like Canada, many developing countries are increasingly reliant on revenue from the extractives sector. Developing countries view the rise in natural resource prices as a badly-needed revenue source for their long-term economic and social development. These countries are often aware of the pitfalls that can be associated with the extractive industries, but argue that effective natural resource governance is essential to their economic future. Advocates argue that transnational mining companies bring with them invaluable economic benefits through their access to capital, skills and technology, and that they provide tangible benefits such as new jobs, economic spin-off activities and improved transportation, communications and social infrastructure.

What, then, is the problem? Canadians themselves are aware of some of the controversies that can accompany unfettered resource development. Both NDP leader Thomas Mulcair and Dalton

McGuinty, the Premier of Ontario, have raised concerns about the so-called "Dutch disease", the idea that a country or region's heightened reliance on the export of primary commodities will inflate its currency and thus endanger the competitiveness of other sectors, particularly manufacturing industries.[2] Mining projects in Canada are frequently accompanied by protest from local communities about the risks of environmental contamination and threats to indigenous land rights. But Canada is a country with relatively strong institutions of governance. The developing countries where Canadian companies are expanding their operations are often plagued with problems of corruption, rule of law, and human rights violations. Moreover their governments also often lack leverage against powerful transnational corporations.

Actors on both sides of the issue recognize both the potential benefits and the costs of resource extraction, but they differ over what should be done to maximize the benefits and minimize the costs. The more far-sighted mining companies are well aware of the risks to the bottom line of social conflict, which explains their willingness to talk about corporate social responsibility. In the context of increased competition from China's resource extraction companies, for which human rights and sustainable development in the host state are of little concern, Canada could—and we argue should—position itself as a global leader in the field of responsible natural resource development.

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Is CIDA Getting a Bum Rap?

When she addressed the 2012 Prospectors and Developers Association of Canada (PDAC) Conference in March, then CIDA Minister Bev Oda said, "More and more, when I meet with other country governments, either on my trips or in bilateral meetings, in addition to the heads of state, the ministers of finance, health, education, and agriculture, I am meeting with ministers of mining. When I ask how Canada can help, they don't always ask for aid, some ask for Canadian technical expertise and assistance in the review of their mining policies, laws, and regulations as well as increasing the capacity in their ministries of mining."[3]

Perhaps there was a fundamental difference between the former Minister's concept of "aid" and that of others in the field. Why would "technical expertise and assistance in the review of mining policies, laws and regulations, as well as increasing the capacity of a ministry of mining" *not* be understood as part of a responsible and responsive "aid" program? Aid, surely, is not about handouts, and it's not exclusively about health and education and children.

The Minister quoted a PricewaterhouseCoopers report, *Mine 2010*,[4] which said that the mining industry had entered a new era, and that many governments are looking to reform their mining codes, taxation and royalty regimes and to improve their policy frameworks. From an investor's point of view, stability and certainty are important. These are no less important to developing countries.

There is something else, of course. Just like Canada, developing countries want to wring the most they can out of the mining sector. And if they see mining as a contributor to development—which is not the same as *growth*, but on that, more later—then they will aim to ensure that codes and investment regimes take into consideration not just royalties and taxes, but also the impact of a project on local communities, its environmental footprint and its potential for job-creation and value-added.

The Economist recently reminded its readers that "Resource nationalism is nothing new… Nor is the practice confined to developing countries that feel they came off second-best when negotiating resource deals in years gone by. Australia is set to raise some $8 billion a year through a controversial new tax on miners; Britain has previously dipped into the profits of oil companies in the North Sea."[5]

The Economist points out, however, that in recent months "resource nationalism has jumped to the top of the list of things that worry the 30 biggest global miners. This was prompted by 25 countries worldwide announcing plans to boost their take of profits," according to an Ernst & Young survey.

In the aftermath of the financial crisis, many cash-strapped governments have viewed large multinationals as easy targets. In Africa, mining companies are especially vulnerable. As *The Economist* put it, "they are usually the biggest corporate beasts around. Widespread poverty has provided a ready excuse for governments dependent on income from resources. The trick for miners is to ensure not only that the money keeps flowing but also that the miners agree to the spending on roads, railways, schools and hospitals that are now a customary part of the package the industry offers to acquire mineral rights."

China, of course, has become a past master in this kind of spending, getting out in front in a field where aid agencies once led. For China, this is not about development, of course. It's about access to mineral rights.

The challenge for CIDA in all of this is to ensure that Canada's aid program is not lured away from areas where it has knowledge, history and a legal obligation—"roads, railways, schools and hospitals"—into acting as a shill for companies that do a bit of this on the side as "a customary part of the package the industry offers to acquire mineral rights." In the context of growing Chinese investment, Canada has a golden opportunity to position itself as a leader in corporate social responsibility.

Then there's the bad government/bad company nexus: who should take responsibility when a Canadian firm ignores disputes over land, labour or human rights with the blessing of a weak or corrupt government? Africa and Latin America are littered with a poisoned political legacy from generations of such deals. One answer, proposed by the Roundtable exercise set up by the

Department of Foreign Affairs in 2008, was the creation of a Canadian ombudsman whose office would arbitrate disputes that arise between Canadian companies and their international stakeholders. That recommendation, disparaged by many short-sighted Canadian mining firms, was ignored by the government. This will almost certainly come back to haunt both companies and a government promoting Canadian leadership in the extractive sector.

In many cases what's needed is not so much arbitration, but the assurance of compliance with laws and established standards of behaviour. The World Bank's Compliance Advisor Ombudsman[6] can, as the name implies, act as an advisor and an arbitrator, but the office also acts as a compliance auditor when there are unresolved disputes, carrying out audits of projects financed by the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) to ensure that they meet clearly stated social and environmental standards.

Fear that Canada is heading in the opposite direction—a mini China in Resourceland—is what drove public criticism of CIDA's much ballyhooed 2011 trilateral agreements with NGOs and mining companies. The announcement last September that CIDA would fund CSR "partnerships" between several Canadian mining giants and Canadian NGOs[7] in Ghana, Peru and Burkina Faso was met with charges that CIDA was being used to subsidize the responsibilities and public relations of highly profitable companies. Unless CIDA's policy is clear in this respect, there will continue to be much more heat than light in an area where Canada really can play a useful role.

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Lost in the hullabaloo was a much bigger concern. Corporate subsidies aside, such funding sent a worrying message that CIDA was prepared to help companies outsource even the most basic of civic responsibilities. In doing so it demonstrated a troubling disconnect between CIDA and current debates on best practice by multinationals operating in the extractive sector.[8]

Such partnerships bear little relation to the principles and objectives of either the African Union's African Mining Vision[9] or the Natural Resource Charter[10], championed by former World Bank economist Paul Collier. Both initiatives are currently at the heart of efforts by developing countries to articulate how they plan to improve governance in the extractive sector and ensure that natural resources contribute to improvements elsewhere in their economies.

If CIDA wants to be taken seriously it should look to both of these documents for pointers on how to advance a credible international mining strategy that dovetails with what developing countries want and need.

CIDA's rumoured plan to open an office in Mongolia—where Canada has large mining interests—looks very much like the Chinese model. As part of a package related to oil concessions in Uganda, for example, China is building President Museveni a new twin-tower office. It is also providing military assistance and building a highway, a hospital and a football stadium. Is this where Canada is heading?

Even at its best, CIDA will face two issues where the extractives are concerned. The first is that in a time of deep cuts, any new priority—no matter how good—will encroach on existing commitments. New CIDA money for the mining sector will not be “new”, it will be money diverted from some other area such as education or health. CIDA is, for example, under fire for its low and diminishing interest in basic education.[11]

The second issue is a bigger one—it is the trade-off between spending directly on proven poverty-reducing sectors such as basic education, or betting on longer-term developmental outcomes that might be predicted in the economic growth to be derived from investments in the extractive industries.

This is a bet that CIDA seems willing to make. “Growth” has become CIDA’s new mantra and then Bev Oda said it clearly at the PDAC Conference: “Our government believes that economic growth in developing countries is the best way to reduce poverty." Here is where the warning bells begin to peel and where the government’s approach and the former Minister’s understanding cry out for clarification. For two generations, development economists have understood that in developing countries, growth is a necessary but insufficient component of development. Growth and development, in fact, are two very different things. And unless the emphasis on development includes a clear focus on poverty, getting from growth to poverty reduction, as the former Minister did in one sentence, is by no means assured.[12]

The Canadian International Institute for Extractive Industries and Development

At the October 2011 Commonwealth Heads of Government meeting in Australia, Prime Minister Harper announced the creation of a Canadian International Institute for Extractive Industries and Development. This is getting off to a slow start, with a lengthy period of consultation and internal debate and a call by CIDA for proposals from interested universities by Sept. 6. Any programming efforts by the Institute—whose aims and objectives remain aspirational at best—are unlikely to see the light of day before 2014, which gives everyone plenty of time to get the initiative right.

The Institute’s biggest challenge in offering the kinds of services outlined in Bev Oda’s PDAC speech will be the huge potential for conflict of interest. The idea behind the Institute is to provide services to other governments in the creation of stable, developmentally and economically sound regulatory systems and tax codes. Many will ask how a Canadian Institute funded by a government that is systematically reducing its own environmental oversight in the extractive sector, one that on the commercial side is actively promoting Canadian mining firms abroad, can be taken seriously as an honest and objective broker. Would Stephen Harper trust China to advise him on a tax code for Chinese investors in Canada?

There are other problems. A CIDA consultation note on the Institute says that it will exclude anything that looks like civil society advocacy. This runs directly counter to its ambition to foster "multi-stakeholder negotiations and engagement". The note doesn't mention the vexed issues of artisanal mining, human and aboriginal rights and the need to tackle at a generic level the kinds of conflict that so often arise when mining companies come to town. If the Institute can get past the conflict of interest problem, these are all areas where—based on its own experience and history—Canada could have much to offer.

> Would Stephen Harper trust China to advise him on a tax code for Chinese investors in Canada?

What might Canadian companies legitimately expect in the way of assistance from CIDA?

CIDA should not be used as a promotional tool for Canadian commercial interests. Within the caveats described above, the McLeod Group believes CIDA can contribute to the creation of a secure, stable and predictable playing field for Canadian and other companies in countries where this kind of assistance is welcome and in areas of special interest to investors: a secure investment environment; good and consistent policies on environmental protection, labour rights, occupational health and safety, land tenure, rule of law. CIDA can also promote these needs among other bilateral and multilateral agencies. Canada could become a leader in this field. But the minute it becomes a huckster for Canadian commercial interests, any semblance of objectivity or credibility will evaporate.

Other Government Departments: Leading or Lagging?

The development agenda discussed in this paper does not preclude the involvement of other government departments in advancing Canadian commercial interests through trade agreements, export promotion efforts, loans or guarantees. While these must meet—and be seen to meet—international norms and standards, they are distinct from Canada's development agenda and any effort by CIDA to create climates for developmentally sound investment in the extractive sectors of developing countries.

The Roundtable and the Bill C-300 exercises ended in acrimony and deadlock, but Canadian companies and the government should think long and hard about what is likely to transpire in the near, medium and longer terms. Short-term grab-and-run tactics may work in some places, but they cannot be the standard to which any company or country aspires in the longer term.. The objectives of any efforts to improve the performance of Canadian companies operating abroad must be revisited if Canada is to be a true leader in all respects in this industry.

Many of Canada's biggest companies would have absolutely no problem in meeting the standards contained in any of a dozen voluntary codes of conduct. The problem is not the best companies, it is others that do not respect or care about the codes. Instead of opposing any kind of Canadian government oversight, responsible companies in the sector should—and will sooner or later have to—wake up and smell the ammonium nitrate.

Abiding by clear-cut rules and obtaining meaningful seals of approval will not be costly for companies seeking stable, long-term relationships abroad. They are part of today's cost of doing business and of obtaining a *sustainable* "social license" to operate. Here is an area where the Canadian government could and should lead rather than lag.

To paraphrase Paul Collier, the challenge for Canada internationally as well as at home, is to chart a course between unchecked profiteering on the one hand and environmental romanticism on the other, and to offer realistic and sustainable solutions to dauntingly complex issues.[13] The window for Canada in this is open, and it is not unimportant if it can be managed well.

NOTES

[1] Mining Association of Canada, *Facts and Figures 2010: A Report on the State of the Canadian Mining Industry,* accessed at http://www.mining.ca/www/media_lib/MAC_Documents/Publications/2010/Facts_and_Figures_2010_English.pdf , last accessed June 20, 2012.

[2] A June 2012 report by the OECD on Canada's economic performance reiterated this concern. See for example: http://www.cbc.ca/news/business/story/2012/06/13/oecd-canada-outlook.html

[3] Remarks for the Honourable Beverley J. Oda, Minister of International Cooperation, At the Opening Reception of the PDAC 2012 Conference, March 4, 2012, Toronto

[4] http://www.pwc.com/gx/en/mining/issues-trends/mine-2010-back-to-the-boom-analysis-of-financial-performance-and-trends-in-mining-industry.jhtml

[5] http://www.economist.com/node/21547285

[6] See http://www.cao-ombudsman.org/about/

[7] http://www.acdi-cida.gc.ca/acdi-cida/ACDI-CIDA.nsf/eng/CAR-929105317-KGD

[8] See for example, the work of Harvard Professor John Ruggie and UN Guiding Principles on Business and Human Rights or OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas

[9] http://www.africaminingvision.org/

[10] http://naturalresourcecharter.org/

[11] "Basic Education Too Low a Priority for CIDA", John Edwards, *Embassy Magazine*, May 23, 2012

[12] Details on CIDA's growth strategy can be found at http://www.acdi-cida.gc.ca/acdi-cida/ACDI-CIDA.nsf/eng/NAT-4794829-J7U

[13] Paul Collier, *The Plundered Planet*, OUP, 2011.