

## **Extractive industries transparency: The benefits of EU legislation to African citizens**

June 2012

### Summary

The European Parliament and Council of Ministers have the opportunity in the coming months to make sure that EU based companies engaged in the oil, gas, mining and forestry sectors help empower poorly governed or exploited communities.

African citizens need better and more detailed information to play their part in preventing corruption and illicit capital flight. Mandatory corporate reporting would be the simplest method of providing this information. That was the clear message sent to EU policy makers by civil society activists from the Democratic Republic of Congo (DRC), Ghana, Liberia and Zimbabwe at a recent roundtable event in Brussels. The boom in commodity prices has added urgency to their demands for greater transparency and accountability with regard to extractive revenues. This briefing gathers together material presented at the roundtable, as well as other evidence relevant to the highlighted countries.

The information provided by detailed reporting (by country and by project) would help ensure that communities received their fair share of natural resource revenues, reduce the flow of illicit funds to political and paramilitary groups and open up the terms of extractive contracts to proper oversight. For example:

- ▶ In **Ghana**, mining communities are beset with intractable poverty levels despite their entitlement to a share of mining royalties. Gold exports alone from Ghana in 2010 were worth \$3.8 billion.<sup>1</sup> There are no mechanisms to track the distribution of revenues from central government to these communities.
- ▶ In **Zimbabwe**, detailed disclosure of payments by companies would help to prevent the financing of political violence from diamond revenues that could be used as a cash cow by ZANU-PF loyalists in the military and police.
- ▶ In **DRC**, regional governments are imposing their own taxes on companies to compensate for the lack of revenue-sharing by the central government.
- ▶ In **Liberia**, unfair concessions agreed by a transitional government have been renegotiated but the revenue flows from these projects still remain secret.

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<sup>1</sup> Bank of Ghana 2010 Annual Report

## The benefits of EU extractive transparency legislation to African citizens <sup>2</sup>

As the prices of oil and other non-renewable commodities begin to soar once again,<sup>3</sup> resource-rich African countries have a once-in-a-generation opportunity in their grasp: the possibility of setting their economies on a stable and sustainable development path.<sup>4</sup> It is a path that has been blocked by corruption, waste and mismanagement in the past, with few exceptions to the depressing correlation in sub-Saharan Africa between the abundance of natural resources, poor governance and poverty.

Where there have been partial successes, such as Botswana or Ghana, greater accountability and transparency has been central to the progress made.

Much of this progress is a result of improvements to the host country legal framework and governance institutions. The improvements have been incremental and rely on the varying appetite for reform and shifting political will across countries, particularly in terms of implementation. This report explores how these reform efforts can be complemented by improvements in corporate accountability, specifically through the disclosure of payments made by companies to host country governments. The information provided will allow civil society – journalists, NGOs and other activists – to hold governments to account for the revenues that they receive.

### EU extractive transparency proposals

In October 2011, the European Commission proposed new mandatory disclosure rules for listed and large unlisted companies with activities in the extractive and logging sectors. These companies must report on payments (e.g. taxes, licenses, royalties) to foreign governments. The objective of disclosing payments to government is to strengthen transparency and thereby fight corruption, misuse of public money and illegal capital flight from countries rich in resources. The legislative vehicles for these proposals are the Transparency and Accounting Directives.

Following similar legislation passed in the US in 2010, the proposals would require companies to disclose their payments to host-country governments for every project that they operate in each country. Only material payments would be disclosed, but the Commission is clear that materiality should be defined with reference to the recipient of the payments, i.e. host country administrations.

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<sup>2</sup> This report builds on the views and evidence gathered for the Open Society Foundations/Transparency International roundtable event “Resource Watchdogs: Africa’s commodity boom and the role of civil society” on 27 March 2012. Particular thanks to Rebecca Morse at Revenue Watch Institute for providing additional material.

<sup>3</sup> Within the longer-term trend of rising prices and increased government revenues there will of course be a lot of volatility, as the wild swings in oil prices over the last 5 years has demonstrated. This, however, simply underlines the need for better oversight of revenues and public spending decisions, a point emphasized by economists such as Paul Collier.

<sup>4</sup> See for example the Gates report to G20 leaders, “Innovation with Impact: Financing 21<sup>st</sup> Century Development”, November 2011 <http://www.thegatesnotes.com/~media/Images/GatesNotes/G20/G20-Documents/g20-report-english.pdf>

## How EU mandatory reporting rules will help citizens in African countries: Evidence from Democratic Republic of Congo, Ghana, Liberia and Zimbabwe

### ➤ *Improving transparency and preventing corruption*

Natural resources are particularly important to the **Zimbabwean** economy. More than 15% of the central governments' budget is supported by the mining sector. There is a danger that if the mining sector generally – and diamonds in particular – does not perform, the government will virtually shut down and citizens will be denied basic services. This makes the fundamental opacity of the sector all the more alarming. Three areas in particular threaten the ability of ordinary Zimbabweans to benefit from the country's vast mineral wealth:

(i) Open procurement and legislative oversight of licensing and contract negotiations are completely lacking. In general neither Zimbabwe's legislators nor its citizens have access to information on mining license sales or the negotiation of development agreements. Instead, a Mines and Mining Affairs Board handles these crucial management functions independent of oversight, and its decisions are approved directly by the President. Corruption easily invades such a system, and indeed Zimbabwe's Minister of Mines was recently accused of threatening Board members to award mining licenses to a certain company in exchange for kickbacks from its shareholders.

(ii) The government itself lacks basic information on mining reserves and production figures. Zimbabwe's government lacks the necessary technical capacity and resources to properly assess reserves and production, information critical to ensuring companies are paying what they owe in exchange for access to resources. Mining companies, however, undoubtedly have access to this information and may benefit tremendously from this information asymmetry.

*Zimbabwe's Marange diamond field has been called the '8th wonder of the world' but in 2011 the diamond mining sector contributed a mere \$300 million to government revenues*

(iii) Government revenues from diamond mining are not maximized, despite the potential of the sector and the vast resources at the Marange diamond field in particular. "Marange has been called the '8<sup>th</sup> wonder of the world'", noted Nyaradzo Mutonhori (Project Coordinator at Transparency International Zimbabwe), "but last year, Zimbabwe's diamond mining sector contributed a mere \$300 million to government revenues". Taxpayer accountability and inadequate government revenue management systems are part of the problem. By law, the Zimbabwean government is entitled to dividend payments and resource depletion fees operators pay directly to Treasury, whilst payments to the Zimbabwean Revenue Authority (ZIMRA) include royalties, VAT and non-resident

shareholders' tax. The majority of mining revenues, however, are currently retained by the wholly government-owned Minerals Marketing Corporation of Zimbabwe (MMCZ) There is very little monitoring or oversight of these revenue streams, and this lack of transparency puts Zimbabwe's revenue collection efforts in jeopardy.

In **Ghana**, the imperative to get resource development right is just as clear. Revenues from oil are estimated to average US\$1 billion per year from 2011 to 2029, or about 5% of GDP. If used well, Ghana's oil and gas resources can create greater prosperity for current and future generations; if used poorly, they can lead to economic instability, social conflict and environmental damage. With almost

80% of Ghana's population living on less than US\$2 dollars a day, the need for good governance in the country's extractive sectors is acute.<sup>5</sup>

In recent years Ghana's government has made notable strides toward improving the legal and regulatory oversight of oil, gas and mining sectors. Ghana's implementation of the Extractive Industries Transparency Initiative, and its promise to expand the initiative to the oil sector, is promising. So is the passage of a 2011 Petroleum Revenue Management Law, which contains serious safeguards for transparent and accountable governance, including rigorous rules for reporting on oil fund assets and investments. However, major challenges remain. A historical lack of citizen participation and transparency, the absence of open and competitive licensing processes, a weak approach to contract transparency and low levels of revenue collection have cast suspicion on the government of Ghana's ability to properly manage oil, gas and mining development.

According to Nana Yaw Saah Aboagye, Programme Officer at the Ghana Integrity Initiative, "Many of the problems in Ghana's extractive sector are a result of the difficulties civil society and ordinary citizen have in accessing information about activities, regulation and revenue flows within the sector". Without proper information, citizens struggle to hold policy makers, state institutions and companies accountable for their actions.

For example, while in 2009 President Atta Mills promised to make all oil contracts signed with international firms publicly accessible, these contracts are not freely available and Ghana has no legal requirement mandating the disclosure of contracts and related documents. The Ghana National Petroleum Corporation (Ghana's state-owned oil company), for instance, has published only narrative summaries of the developments it participates in with outside operators – despite the fact that some of these operators, including Kosmos Energy and Tullow Oil, have independently made their contracts with Ghana's government public. Broadly, access to reliable, timely information on Ghana's extractive sectors and public revenue flows remains limited; Ghana's Parliament has yet to pass the Freedom of Information Bill, an important cornerstone of good governance which would reinforce transparency safeguards in the oil and gas sector.

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Similarly in **Liberia**, citizens in communities endowed with natural resources are given little or no access to information about the processes that lead to the exploitation of their resources and the expenditure of revenues generated. Civil society is often weak and the government has little consideration for their views in the award of contacts and concessions. Most of the time, these communities have to live with contracts that often do not represent their interests. Over the years, communities have been victims of exploitative concessions that affected them developmentally and environmentally. Proceeds from concessions have been diverted to benefit personal interest.

Most of the controversial resource contracts signed before or during the transitional governments in Liberia were subsequently cancelled or thoroughly revised, including the cancellation of all logging contracts and revisions to Mittal Steel and Firestone contracts. With more attention devoted to improving contractual terms by international bodies including NGOs and civil society, there is still

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<sup>5</sup> Statistics from Revenue Watch Institute

much at stake in Liberia given the size of the mining projects, where abuses are entrenched and the capacities of bureaucracies and civil society remain limited, and there is inadequate political will to enforce contracts. A good deal of conflict is experienced in the extractive sectors, such as the impacts of mining operations on local communities, and the working conditions and pay in industrial ventures.

### ➤ *The need for mandatory corporate reporting by country and project*

While frequently acknowledging the need for greater transparency at the level of the host country, policy makers have questioned the added value of disclosure at the level of individual projects. However, the impact of extractive projects is borne most often by local communities, which are often legally entitled to a share of revenues. But these communities frequently receive little benefit and have no data to determine or contest their entitlements. Communities need information about the projects that affect them – to assess whether they are receiving their fair share, to ensure that funds for environmental and social protection are managed responsibly, to track who receives revenues and to build the trust so essential to reducing risk of conflict and instability.

To improve the development impacts of extractive (oil, gas and mining) activities in this sector, the European Union’s new reporting requirements under the Accounting and Transparency Directives<sup>6</sup> should reflect the structure of these industries and require disclosures that significantly reduce risk and improve accountability. To meet this aim, companies should report payments to governments on a project-by-project as well as a country-by-country basis.

Transparency International **Zimbabwe** has called for public and disaggregated disclosure of receipts from mineral extraction as a step towards a credible national budget out of reach of factional politics. This is crucial in the light of upcoming elections. Detailed disclosure of payments by companies would help to prevent the financing of political violence from diamond revenues. “There is the potential for these revenues to be used as a cash cow by ZANU-PF loyalists in the military and police”, warned Mutonhori, referring to allegations that the directors of one of the largest companies mining diamonds in Marange are active or retired members of the military and police. Since the army took over the alluvial field in 2008, concessions have been awarded to companies under questionable circumstances. In this context it is notable that 90% of diamond mining in Zimbabwe is controlled by companies listed on the London Stock Exchange, all of whom would come under the scope of the EU legislation.

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In **Ghana**, local mining communities are entitled to a proportion of royalties paid to central government. However, there is no mechanism to track whether the right payments have been rendered to the community through the appropriate channels, especially in tracking revenue from upstream.

The Minerals and Mining Act 2006 sets royalties between 3 and 6 percent of value extracted. The distribution of revenues from then mining sector across levels of government is also regulated by Ghanaian law. Of the royalties received, the centrally administered Office of the Administration of

<sup>6</sup> [http://ec.europa.eu/internal\\_market/accounting/other\\_en.htm](http://ec.europa.eu/internal_market/accounting/other_en.htm)

Stool Land retains 1 percent. The Office then distributes revenues to producer regions (4.95 percent), producer traditional councils (1.8 percent), and customary land title holders or the stool (2.25 percent). This represents the country's typical sub-national level revenue distribution in the mining sector

The fact that mining communities are beset with intractable poverty levels is an indication that these distributions of revenues have not served its intended purpose. "Either the right amounts are not made available or revenues end up lining the pockets of corrupt officials and groups", explained Aboagye.

*Either the right amounts are not made available or revenues end up lining the pockets of corrupt officials and groups. The burning question is: why does poverty persist in communities in producing regions? What is the missing link between revenues and poverty reduction?*

"The burning question is, after so many years of mining, why does poverty persist in communities in producing regions? What is the missing link between revenues and poverty reduction efforts?"

The major issues have been the lack of monitoring of allocations and accountability mechanisms.

To a large extent, Stools and Traditional Councils lack the upstream information to monitor whether or not they are receiving the correct amounts from the regional branches of the Office of Administration of Stool Land. The lack of transparency at the upstream level affects directly transparency at the lower levels.

There are also no accountability mechanisms to ensure prudent management of extractive industry revenues. The country does not have adequate procedures to check the handling of funds in the districts assemblies and traditional authorities.

Similarly in the **Democratic Republic of Congo (DRC)**, vastly more information on project profits must be made public in order for sub-national governments and affected communities to know whether they are getting their fair share. In DRC, the Mining Code stipulates that a share of 25% of tax revenues from a mining project should go back to the province, and 15% back to the local territory or town. However, communities are currently not in a position to claim the tax money they are entitled to, because there is no way of knowing how much the local project is generating in taxes. For instance, First Quantum Minerals claimed to have paid \$55 million to the DRC treasury in 2009. In that year it had several projects in Katanga province; subsidiaries Frontier SPRL and COMISA ran the copper mine in Sakania, and subsidiary Kinganyambo Musonoi Tailings (KMT) was the Joint Venture running the copper and cobalt project in Kolwezi. Technically, Katanga province should have been entitled to USD 13.75 million in taxes from those operations, but the communities of Sakania and Kolwezi have no way of determining their entitlement if First Quantum is only made to publish country-level data, rather than presenting it on a per project basis. It is important to note that as the payments are made to the DRC treasury, these payments would not be captured by the disclosure of payments made directly to each level of government. World Bank data suggests that the provinces are not, in fact, getting any share of the revenues at all from Kinshasa and are imposing their own direct taxes on companies to compensate. This is particularly concerning given the history of separatism and conflict in Katanga.

In **Liberia**, agreements are usually reached and arranged at the national level and imposed upon local communities. There is a limited space for citizens at the sub-national level to access information



related to resource allocation, with public accountability and concrete participation by local communities a huge challenge. As Shine Williams, Research and Policy Officer at the Centre for Transparency and Accountability in Liberia pointed out, "citizens of natural resources communities in Bassa, Bong, and Nimba counties have little or no opportunities to access and interpret information on natural resources to match their expectations on resource allocation and management".

### ➤ *What is “material” to African communities?*

In an effort to reduce the reporting burden for extractive companies, the European Commission proposals only require material payments to governments to be disclosed. It however endorsed the principle that “materiality” in this context needs to be defined in relation to the budgets of African governments, rather than the global revenues of multinational corporations. Recent discussions among member state governments have not heeded this principle and sums as high as \$1 million have been suggested.

To see how such a high materiality threshold does not reflect the fiscal reality in large parts of Africa, take the case of the Asutifi, a gold mining district in **Ghana**. In 2008, the total district budget was less than €1 million to serve a population of approximately 108,000 people. This included revenue from mining that in total, from all kinds of payments, was worth €92,970 (639,452 Ghanaian cedi), or 32% of the total district budget. Thus payments that may have seemed relatively small to the companies that made them have a huge impact at the local level in Asutifi.

The bulk of the above transfers are from mining royalty payments. But looking at property rate payments is also informative. Total property rate payments by all major mining companies in 2008 across the whole of Ghana were worth approximately €380,000 (829,234 Ghanaian cedi); averaged across the ten mining districts, this works out to an average of €38,000 (82,923 Ghanaian cedi) per district for all major mining companies. These numbers are small. But this payment is one of the very few that is paid directly to the local government responsible for responding to local community needs. Thus payments amounting to ‘merely’ tens of thousands of Euro are clearly material to local government budgets.

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For further information on this report, or the proposed extractives disclosure legislation, contact:

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For further information on the global civil society campaign for oil, gas and mining revenues to form the basis for development and improve the lives of citizens in resource-rich countries, see:

Publish What You Pay - [www.publishwhatyoupay.org](http://www.publishwhatyoupay.org)

## Annex: roundtable programme



### Resource watchdogs: Africa's commodity boom and the role of civil society

13.00 – 15.00, Tuesday 27 March 2012

Luxembourg Conference Room, Science 14 Atrium

14b Rue de la Science, Brussels 1040

Thanks to growing investment and strong demand for commodities, sub-Saharan Africa is poised for an economic transformation. Translating high growth rates into long-term prosperity and stability will depend to a large degree on the careful management of natural resource revenues. In 2008, exports of oil, gas and minerals from Africa were worth roughly 9 times the value of international aid to the continent (\$393 billion vs. \$44 billion).

A note of caution is necessary however. Windfalls from previous commodity booms have been squandered, partly as a result of corruption and mismanagement. Will it be different this time? How can the fruits of natural resource wealth be used to ensure that African economies are set on the road to inclusive and sustainable growth? What can an empowered civil society do to ensure this is a reality? What role can the EU play?

Transparency International and Open Society Foundations are joining forces to provide policy makers in Brussels a rare opportunity to hear directly from civil society activists from **Democratic Republic of Congo, Ghana, Liberia and Zimbabwe** on these crucial questions. As EU member states and MEPs deliberate extractive transparency legislation that would help citizens of resource-rich countries hold their governments to account, it is a timely occasion to reflect on the benefits of such initiatives. The session will also look at the respective obligations of companies, governments and civil society to ensure a more fair distribution of natural resource revenues.

#### Speakers:

Nana Yaw Saah Aboagye, Ghana Integrity Initiative

Arlene McCarthy MEP

Georges Mukuli, Southern Africa Resource Watch

Nyaradzo Mutonhori, Transparency International Zimbabwe

Shine Williams, Center for Transparency and Accountability in Liberia