Chapter 2
The Context of Benefit Sharing in the Mining Industry

The mining industry has a number of characteristics that draw it into economic and social development at the local, regional, and sometimes national levels:

- Because mining operations are often conducted in environments where government institutions may be absent, weak, or lacking in capacity, there may be gaps in essential public services.
- The social and environmental footprints of mining operations often have negative effects on local communities that require compensation or mitigation programs.
- The remote location of many operations heightens expectations for employment and economic development in host communities.
- The enclave nature of the mining industry can limit the trickle down of benefits unless specific social investment programs are undertaken.

In this context, mining companies and governments must often take action to share benefits at the local level and sometimes to establish an instrument dedicated for that purpose.

Sharing Benefits at the Local Level

Mining projects can contribute to development through a number of channels, ranging from employment and tax payments to local procurement and community investment projects (figure 2.1). Sharing benefits and compensating for damages generated by mining operations within communities is widely recognized as a necessity. The sharing may be mandatory or voluntary.

This publication focuses on three of these benefit-sharing channels: government payments, compensation, and community investment. Changes in the mining industry and in community expectations have
focused growing attention on benefit-sharing approaches in each of these areas in recent years.

**The Company Perspective: Providing Compensation and Acquiring a Social License to Operate**

Compensation for landholders and populations affected by the granting of a mining lease is typically a legal obligation that the leaseholder must fulfill on top of regular tax payments. Management and disbursement of compensation funds can be a challenge, and companies do not always find mechanisms in place that will help them to meet existing laws and regulations. Not only does the value of the compensation need to meet expectations, but also its form, with growing recognition that one-off cash payments are not a sufficient answer. The lack of authorized and transparent mechanisms also makes it difficult for communities to hold companies accountable for payment of the compensation they owe.

Companies and governments are under great scrutiny to ensure that benefits from mining projects are not limited to compensation for damages and to contribute positively to communities affected by mining developments. Where this obligation is enforced, mining projects can operate only when a “social license” to do so is granted by the surrounding communities. To gain and retain a social license, companies typically need to go beyond the government’s requirements for taxation and compensation and actually invest in community development.

The role of community investment around mining projects has grown significantly in the last two decades for a number of reasons:
• **Sectoral changes.** Between 1989 and 2001, more than 75 countries liberalized their investment regimes for mining, oil, and gas exploitation and privatized state mining companies (BSR 2010). This had the dual effect of increasing foreign investment by multinational mining companies in developing countries and reducing the provision of “social wages”—subsidized housing, education, and health care—for workers in state-owned companies. Technological improvements have reduced the labor needs of mining projects. Along with an increase in “fly-in, fly-out” operations, these changes are diminishing many of the traditional benefits received by communities. Pressure has risen to replace them with new benefit-sharing instruments, often in the form of community investment.

• **Operational drivers.** Improved access to communications across the world and an increase in the number of advocacy groups focused on the mining sector have raised community expectations from mineral developments. Employees have also raised their expectations of the companies they work for, increasing the focus on corporate social responsibility (CSR) in operations.

• **Expectations of corporate social responsibility.** The growth of CSR across all industries has led shareholders and stakeholders to review the social contribution of private industry in far more detail than in the past. Peer performance has also raised the bar for more strategic and effective community investment with a long-term view of sustainable development (ICMM 2005). Commercial investors also review these commitments and contributions.

Unless mining companies address these changing expectations of benefit sharing, they may fail to obtain and retain a social license to operate. In turn, community rejection of a project because of inadequate or inappropriate compensation can disrupt the project and swing popular opinion against mineral development in the country.

**The Government Perspective: Demonstrating Locally Positive Impacts from Mining**

The concept of promoting sustainable development in communities affected by mining operations has gained currency over the past decade. Governments are increasingly under pressure to demonstrate the local positive impact of mining throughout a project’s lifecycle, from exploration to mine closure, in order to gain political support for continued mineral development. To achieve that support, one option is
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to establish mining tax regimes that include direct or indirect payments to decentralized development authorities. Along with taxes based on property value, royalties levied mine by mine are well suited for financing local distributions. The extent to which royalty collection and expenditure are decentralized from the general budget varies widely (table 2.1).

Legal provisions to impose redistribution at the local level are often implemented when only limited benefits accrue to the host communities that bear most of the negative impact of mining operations. However, in practice, royalties payable to the central government rarely revert back to the affected region, even when the legislation specifies that this should be the case. While decentralization of benefit sharing from mining activities is becoming increasingly common, it must be noted that many nations still prefer to see all major taxes flow to a general fund, allowing central or provincial governments to determine where and how monies should be expended for the good of the public as a whole.

Among communities and governments, recent escalating mineral prices have placed additional focus upon the benefit-sharing arrangements in place in mineral-dependent economies. Countries with multinational mining corporations using ad valorem\(^1\) taxation and royalty schemes have seen the majority of windfall profits leave their national borders, causing local controversy and sometimes a reassessment of the means by which both production and profit can be shared.

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\(^1\)Ad valorem refers to duties which are levied on commodities at certain rates per centum on their value.

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<thead>
<tr>
<th>Royalty/tax</th>
<th>Percentage Allocated to Decentralized Authorities by Law</th>
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<tbody>
<tr>
<td>Madagascar royalty</td>
<td>42 percent to communes of extraction; 21 percent to region; 7 percent to province</td>
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<tr>
<td>Peru royalty</td>
<td>20 percent to the district of exploitation; 20 percent to the province; 40 percent to other districts and provinces in the region; 20 percent to the region, including 5 percent to universities</td>
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<tr>
<td>Indonesia state receipts from natural resources, including mining</td>
<td>80 percent to the region (split as 64 percent to the regencies and 16 percent to the provincial government)</td>
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Establishing Dedicated Instruments

General Drivers

Recognizing the need for development contributions at the local level, governments and companies alike have considered the role of a dedicated instrument, such as an FTF, to deliver this contribution. As independent vehicles to channel revenues generated by mining operations to communities, FTFs can be designed to meet multiple goals, including the following specific cases, each of which is addressed in greater detail in this section.

- Companies can work in partnership with local communities through shared FTF governance arrangements to fund development projects.
- FTFs can support government decentralization processes by increasing the transparency and traceability of financing from mining regions into development initiatives.
- Agreements between indigenous people and mining developments can be formalized and made actionable through the creation of an FTF.

This is not to suggest that these goals can be achieved only through the use of a dedicated instrument such as an FTF. In fact, companies and governments may choose to develop systems internally or partner with development agencies as an alternative to establishing an FTF. While the appropriate means of channeling development contributions from mining projects depends heavily on site-specific conditions, dedicated instruments can bring particular value in the following situations:

- **Lack of local capacity.** Where funds are allocated to decentralized authorities or groups with limited capacity, the use of a dedicated vehicle such as a foundation can increase the resources available to the group for delivery of sustainable development outcomes from mining. The creation of a specific vehicle can also increase the accountability of those responsible for delivering the development projects, increasing the likelihood of a positive outcome.
- **Weak or absent public services.** Mineral projects are increasingly being developed in frontier regions of developing countries, outside the reach of government-provided public services such as water, sanitation, and electricity. The responsibility for providing public services in these situations often falls to mining companies. Through use of a foundation model in partnership with local authorities the potential for blurring of roles can be minimized.
- **Continued benefit beyond mine closure.** Ideally, the exploitation of mineral resources transforms natural capital into other forms of capital...
to be shared among project beneficiaries over the long term. When delivered through an endowed FTF, benefit-sharing approaches, such as community investment initiatives, experience a smoother and more likely successful transition to sustainability after the mine closes.

**The Company Perspective**

In the absence of a government framework mandating an approach to benefit sharing, companies are often left to develop their own approaches in consultation with communities and government representatives. The IFC’s community investment strategies handbook (2010) provides a detailed analysis of the business case for community investment by companies and the basis for choosing a dedicated instrument to deliver such activities, a summary of which is provided below.

The vast majority of FTFs are initiated by companies and are used to deliver community investment programs. The choice of an FTF over other models (such as in-house management of community programs or partnering with an external development actor) is based on a number of advantages identified with FTFs. While these advantages can be found individually outside FTFs, the combination that FTFs can deliver presents a significant benefit. The use of FTFs can:

- Signal commitment and establish a formal, professional, and systematic approach to development that can help to build an informal expression of consensus (“social license to operate”).
- Support long-term, multi-year development projects without necessarily being tied to annual company budget cycles.
- Foster stakeholder participation in the management and operation of community investment programs. Independent management and governance structures can provide a more formal approach to shared decision making and to the inclusion of the community, nongovernmental organizations, and governments.
- Build bridges to other development actors and formalize collaboration between a company and other stakeholders by providing a neutral facilitator. The role as a neutral party can also increase the likelihood of being able to find and obtain external financing.
- Separate legal liability for the actions of community development programs from those of a mining company, thereby minimizing company risk.
- Provide a guarantee of financial support for development independent of the boom-and-bust cycle of mining.
• Provide financial benefits, such as tax advantages, that may not be available through other community investment vehicles.
• Develop long-term institutional knowledge and attract and retain specialized expertise from the development sector.
• Represent a participatory, transparent, and accountable mechanism for investing revenues in development, particularly in situations where public and private institutions are distrusted or seen as corrupt.

The payments made by mining companies as compensation for social and environmental impacts can be considerable. A trust structure can help ensure effective management of funds intended for compensation-related community projects and payments over time.

Benefit-sharing agreements between mining companies and communities can also generate significant funds, and the need for a dedicated instrument to manage these funds can emerge during the process of negotiating a community development agreement (CDA, box 2.1).

Box 2.1: The Use of FTFs in Community Development Agreements

As part of the development agreement for the Lihir gold mine in Papua New Guinea, an integrated benefits package (IBP) that includes compensation as well as community investment was approved in 1995. A progress review of the IBP was to be conducted every five years. Disappointment in the early results led to the recasting of the IBP as the Lihir Sustainable Development Plan (LSDP) in 2007, with an increased focus on long-term outcomes. Included within the LSDP are agreements on trust fund payments and a broadening of ownership of the plan, now shared between the company and landowners.

The Ahafo Social Responsibility Agreement (ASRA) is the first of three CDAs in existence at Newmont’s Ahafo mine in Ghana. The ASRA defines the roles and responsibilities of stakeholders in the CDA process and includes a commitment to establish the Newmont Ahafo Development Foundation (NADeF). NADeF is financed by a payment from Newmont of US$1 per ounce of gold sold by the company from the Ahafo lease, as well as a commitment that 1 percent of net before-tax income will be paid to the foundation.

FTFs and other dedicated instruments have figured prominently in the negotiation of benefit-sharing arrangements between mining companies and indigenous peoples, as discussed at the end of this section.

The Government Perspective
Governments may establish FTFs or promote their use for the following reasons:

- To bypass existing structures, processes, and politicians and establish direct channels to beneficiaries.
- To manage mandatory or voluntary funds received from companies through taxes, royalties, or fees.
- To stabilize economic contributions from the mining sector to weather severe fluctuations in commodity prices.
- To set communities and regions on a path to sustainable development that will extend beyond the life of the mine.

Some countries’ mining regulations include requirements for benefit sharing or other initiatives designed to help communities grow. However, such mandates are still comparatively rare. Countries with strong policy and regulatory approaches include Chile, Papua New Guinea, and South Africa. In addition, Egypt, Eritrea, Guinea, Mozambique, Nigeria, Sierra Leone, and Yemen have recently introduced community development regulations, and the Democratic Republic of Congo (DRC), Ghana, Namibia, and Tanzania are reportedly seeking to embed community development initiatives within their policy framework.

In 2009, the Mining Law Committee of the International Bar Association established a project to prepare a model mining development agreement (MMDA) to be used by mining companies and host governments. The project is aimed primarily as a tool for use with and in developing countries, in particular where a mature mining code is not in place or has proven ineffective. The MMDA is being developed in a public fashion. A version 1.0 dated April 4, 2011, includes an explicit recommendation for the establishment of a community development foundation by mining companies:²

The Company shall provide an annual payment of [X AMOUNT] to a Community Development Foundation established as part of the Community Development Plan, which shall be managed and disbursed, in efforts to promote local and regional development, or health education and welfare in the communities affected by the Project. The governing body

²For further details on this project see www.mmdaproject.org
of the Community Development Foundation shall include members of communities affected by the Project. The annual budget and disbursements from the Community Development Foundation shall be public and shall be subject to audit procedures provided for by Applicable Law and the terms of the agreement. Periodic reports and audit reports shall be made available to the Company, to the State, and to the public.

Given the difficulty governments face in renegotiating taxation arrangements with companies, which often come under particular scrutiny during times of changing mineral prices, governments may also resort to FTFs for the following purposes:

• To invest a portion of the taxation and royalties received from mining into a stabilization fund to help balance annual budgets and allow the government to plan longer-term projects. This approach is particularly relevant where taxation is strongly based on in personam\(^3\) taxes, over which the government can exert little or no control, and where mining constitutes a significant portion of the country’s GDP.

• To avoid renegotiating contracts during times of windfall profits where taxes are based heavily on the use of in rem\(^4\) taxes, some governments have turned to the implementation of “voluntary contributions” from companies using FTF models to manage these contributions for immediate implementation at the community level.

• Where public services are inadequate, governments may promote the establishment of a company FTF model to provide complementary resources to fill gaps in service provision or extend the scope of services. Ideally, these programs are targeted toward building the capacity of local governments to implement the projects in the future. The use of FTFs in such situations can allow a beneficiary to experience more rapid development than would have resulted from government distribution of revenues for infrastructure owing to resource limitations, low capacity, political factors, or corruption. Implicit within this model, however, is a blurring of the roles between the private sector and government.

• In some jurisdictions the negotiation of mineral licenses identifies the whole package of benefits and payments due to communities. This integrated approach to benefits can generate large lumped sums of

\(^3\)In personam taxes are charges against some definition of net revenue and, as such, are tightly linked to the profitability of the mining project.

\(^4\)In rem taxes include taxes on fixed and variable costs of production, such as unit-based royalties.
money payable to communities over an extended period of time. By using an FTF model, transparency can be maintained between communities, government, and companies in such cases.

Box 2.2 provides examples of two governments that have set up FTFs.

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**Box 2.2: Government-Authored Benefit-Sharing Schemes Using FTFs: The Cases of Madagascar and Senegal**

**Madagascar.** After centuries of artisanal mining, in 2005 the first world-class industrial mining investment was committed in Madagascar. The joint venture between Rio Tinto and the state (represented by OMNIS, a public agency) started exporting ilmenite in 2009 amid considerable concern over the collection, redistribution, and use of royalties. Madagascar’s national mining code (passed in 1999 and reviewed in 2005) allocated part of the royalties to decentralized authorities. However, the distribution rules in the code were designed for application to small-scale and artisanal mining and could not easily be adapted to large-scale enterprise.

If the distribution rules had been applied directly, only two small villages would have benefited from the royalty, with the adjacent city of Fort Dauphin receiving nothing. The distribution system was also incapable of accommodating the mobile nature of a dredging operation that affects different communes over time, depending on the company’s mining decisions. Despite these problems with the existing mining code, the government was reluctant to propose a new law. Instead, it convened a dialogue with local stakeholders to consider a variety of options that would respect the spirit of the law while providing a pragmatic and inclusive solution. From this dialogue a proposal was developed for a “Mining Community Foundation.” This dedicated instrument was to have the following attributes:

- It would channel a part of the royalty stream to a wide list of beneficiary communes to achieve greater equity.
- It would be endowed, with the mining company (QMM) agreeing in principle to make significant contributions.
- A community forum would be established and meet regularly with the foundation’s board to ensure that the commune’s authorities and members of civil society would be able to participate in programming choices.

Because of a political crisis that hit Madagascar at the time, the proposal stalled before the Mining Community Foundation could be implemented.
The Special Case of Indigenous Communities

Negotiated agreements between indigenous peoples and mining companies have become commonplace in the past two decades in Australia and North America, where customary ownership has been formally recognized (ICMM 2010). Typically, the agreements cover financial payments, disbursement arrangements, employment commitments, governance structures, and other locally important provisions. The ICMM's Good Practice Guide on Indigenous Peoples and Mining (2010) provides additional information on this topic.

The proposal also faced some opposition, as critics felt that the creation of the dedicated instrument would undermine existing governance institutions and the broader decentralization process. There was also fear that the structure might allow payments to be captured by central elites and that it was not sufficiently owned by local communities.

Senegal. An alternative approach to a comparable situation was chosen in Senegal, where the 2003 mining code stipulated that “part of the fiscal revenues generated by mining operations are paid into a Balancing Fund to be allocated to local authorities.” However, detailed provisions were left to subsequent regulations. After extensive consultation, Decree n° 2009-1334 (November 20, 2009) clarified that 20 percent of mining revenues (taxes and royalties) would be used to create a national equalization fund. The local authorities from the mining region would receive 60 percent of the fund, with the remaining 40 percent being shared by other local authorities in the country. The funds are shared between mining regions in amounts that are proportional to the revenues generated and the local population.

In parallel, the government negotiated a Mining Social Plan with companies, financed by annual contributions from the companies as agreed in their respective mining agreements. The ministry in charge of mining approves and supervises the use of these resources. The first Mining Social Plan is dedicated to the population living in the areas around the operation of three companies: OROMIN Exploration Limited, Mineral Deposits Limited, and Arcelor Mittal.
The agreements often use FTF structures to implement the agreed financial disbursements, both for immediate use and for longer-term investments. Some agreements include the allocation of funds for future generations, and FTF structures are often used to make the resulting investments. FTFs can present significant advantages in such cases owing to their potential independence, tax-efficient status, and capacity to attract funding from other sources. The structure can also present good opportunities for long-term sustainability and for gradual transition of ownership (box 2.3).

Box 2.3: Benefit-Sharing FTFs between Indigenous Peoples and Mining Companies

Canada. Signed in 1995, the Raglan Agreement has been used as a benchmark for First Nations agreements in the mining industry. The Raglan mine is located in the Nunavik Territory. The agreement was signed between the two closest communities to the mine (Salluit and Kangiqsujuaq), the Makivik Corporation (an Inuit owned company which oversees the political, social, and economic development of Nunavik), and Raglan mine, now owned by Xstrata Nickel. The Agreement is governed by the Raglan Committee, comprising equal representation from Inuit groups and the company (six members in total). The profit sharing arrangement includes a commitment to provide 4.5 percent of operating profit to community partners (this equated to a payment of close to C$17 million in 2007). All funds are placed in a Trust which in turns distributes 25 percent of the money to the Makivik Corporation, 30 percent to Kangiqsujuaq, and 45 percent to Salluit, who then distribute the funds to the fourteen communities in Nunavik based on a needs assessment.

Australia. The Gnaala Karla Booja (GKB), who are part of the Noongar Nation, are the ‘traditional owners’ of the land in the Newmont-owned Boddington gold mine’s area of operations in Western Australia. A Community Partnership Agreement was signed between the Gnaala Karla Booja and the mine operators and owners in 2006 to acknowledge the traditional owners and to assist in building an economic base for GKB People and their children. The agreement covers employment opportunities, as well as commitments for annual financial assistance which started in 2009. A charitable trust structure has been established to manage these funds for investment in local business development and community development projects. The
Trust is jointly managed by a Traditional Owner Liaison Committee and mine representatives.

Elsewhere in Australia, the Indigenous Land Use Agreement (ILUA) and Argyle Management Plan Agreement (AMPA) together were considered the most comprehensive agreements ever negotiated between a resource company and traditional owners in Australia in 2006. The Rio Tinto owned Argyle Diamond Mine is located in the East Kimberley region of Western Australia and occupies the traditional country of a number of indigenous groups. The ILUA is a voluntary agreement entered in good faith by all parties and it was the result of three years of negotiation, replacing an earlier “Good Neighbour Agreement” dating from the 1980s. The ILUA established two trusts: the Gelganyem Trust and the Kilkayi Trust. The Gelganyem Trust comprises eleven trustees, nine representing the seven traditional owner estate groups that are party to the ILUA and two independent trustees. This Trust administers the Sustainability Fund, the Law and Culture Fund, the Education and Training Fund, and the Miriuwung and Gija Partnership Fund. The Sustainability Fund provides future generations of Miriuwung and Gija people with a significant capital base including money for future generations.

The Gelganyem Trust has developed a number of projects including an indigenous business development facility, scholarships funds, renal health care, and holiday programs for youth at risk. The Trust is funded through royalty payments and has successfully used these payments to leverage funding from the federal and state governments and private funding partners. The Kilkayi Trust has only two trustees and has been established to administer payments from Argyle to individual families party to the ILUA.

Laos. The Sepon Trust Fund was established to implement the Community/Indigenous Peoples Development Plan developed for the Sepon gold and copper project in Laos. The Trust Fund was specifically chosen to reduce the risk of the mine becoming the provider of government services at the local level. All projects supported by the Trust Fund have to be aligned with the broad government plan for the area to improve sustainability. An eight member board comprised of representatives from the company, government, and the two main ethnic groups govern the Fund, and a 17 member committee manages its day-to-day operations.