TCD Andes
Territory, Conflicts and Development in the Andes

"Extractive industries, fiscal systems and human welfare: national policy and local development in Peru, Chile and Bolivia"

University of Manchester/ICMM seminar

October 24th 2008
Anglo American
20 Carlton House Terrace
London
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SPEAKERS

Welcome:
Dr John Groom, Chief Operating Officer at ICMM; Professor Anthony Bebbington, University of Manchester

Presentations:
Dr Alan Roe, former Chairman, Department of Economics, The University of Warwick, and principal consultant OPM.
Jose Carlos Orihuela, PhD economics candidate, Columbia University, US
Dr Leonith Hinojosa, University of Manchester, UK.
Maritza Paredes, PhD political science candidate, University of Oxford and formerly Oxfam America Peru
Javier Arellano, PhD development studies candidate, Institute of Development Studies, University of Sussex, UK

Commentators:
Dr Tony Addison, Executive Director, Brooks World Poverty Institute, University of Manchester, UK.
Prof. Jeffrey Bury, University of California, Santa Cruz, USA

RESOURCES

- Alan Roe's powerpoint presentation
- Jose Carlos Orihuela's powerpoint presentation
- Leonith Hinojosa's powerpoint presentation and paper
- Maritza Paredes's powerpoint presentation

- Javier Arrellano's powerpoint presentation and summary

Background

Between 2007 and early 2010, the School of Environment and Development at the University of Manchester is running a programme entitled: "**Conflicts over the countryside: civil society and the political ecology of rural development in the Andean region.**" The project is made possible by an ESRC Professorial Research Fellowship awarded to Tony Bebbington (RES-051-27-0191). The programme includes a seminar series that aims to produce dissemination and debate of research findings.

The third seminar was organized in collaboration with the International Council on Mining and Metals (ICMM) which, since 2004, has been running the "**Resource Endowment Initiative**." This is a programme of research, analysis and dissemination that seeks to identify the key factors that can contribute to the successful transformation of mineral endowment into forms of development that are genuinely sustainable. http://www.icmm.com/resourceendowment.

The theme of the seminar was: "Extractive industries, fiscal systems and human welfare: national policy and local development in Peru, Chile and Bolivia". It was organized in two parts, each one with presentations followed by specialized comments and questions. The seminar concluded with an open discussion. Forty five participants from UK academic institutions, the corporate sector and civil society organizations attended the meeting.

MEETING REPORT

John Groom and Tony Bebbington, in the chair, opened the event with an overview of the TCD Andes research project, the Resource Endowment Initiative and a summary of the two previous seminars held in Manchester and Oxford. (www.sed.manchester.ac.uk/research/andes/seminars/).

Part 1: National and Cross-National Perspectives

Alan Roe: "ICMM's Resource Endowment initiative: partnerships for the management and use of mineral revenues in Peru".

Alan summarized the ICMM's initiative and highlighted the role of minerals in the development process of mineral-rich countries. He contextualized the recent mining boom and pointed out the contrast between countries in terms of mineral rents distribution and economic performance; whilst countries such as Chile and Ghana have developed on the basis of their mineral wealth, others have shown very poor performance. He noted that in ICMM's research experience discussion of the factors that explain those differences was still insufficient.

He then presented the ICMM's initiative, describing it as an attempt to further understanding of the conditions that need to be in place in order to turn mining into development. The focus of that work has been on the institutional arrangements which underlie the relationships between mining and development. Their research in Peru, Chile, Ghana and Tanzania has concluded that policies for revenue capture and distribution, as well as the overall nature of social relationships underlying these processes, are the factors which exercise most influence over the final impact of mining. For instance, in Ghana the creation of a new district development fund to redistribute resources, along with donor commitment to a far more harmonized use of resources, have helped the country's development process considerably. ICMM has developed a toolkit to help companies integrate their thinking not only on how mining influences the economy but also influences political processes.

He then addressed what it he referred to as "the essence of the problem for mining" – namely that, while at a national level the amount of profits, FDI, exports and revenue are immense, at local levels there are huge problems of disappointing impacts on poverty and of dispute over the resources used and generated by mining.

With regards to success factors, he emphasized that, in addition to those that have traditionally been identified in the literature, ICMM has concluded that the nature of relationships among stakeholders is particularly important. These conclusions derive not from comparing indicators of governance at a national level but rather from looking to what happens on the ground. At that local level, the key factors in determining success are whether mining generates broad-based income growth and employment. In ICMM's research, decentralization of fiscal resources does not seem particularly useful. Consequently, he concluded, deepening governance reforms is critical to ensuring a more effective integration of mining activity into its inherently local settings – that is what helps to a better use of resources.

Jose Carlos Orihuela. "The seizure and allocation of resource rents: Peru and Chile compared".

Jose Carlos presented his comparative study of Peruvian and Chilean mining economies. He began with an overview of the Chilean copper fund describing it as a countercyclical fund allowing savings during periods of boom and as a tool for good resource management. Such a good management would have been evident since the democratic period started, strengthened in 2000 with the Structural Fiscal Surplus Rule. The scheme built on the "Copper Rent Compensation Fund" (1986), created by Pinochet's economists after the 1980s financial crisis. According to his findings, the Chilean system for managing resources is based fundamentally on rules rather than laws. It was only in 2006 when those rules became legally binding giving place to Fiscal Responsibility Law, the Social and Economic Stability Fund and the Pensions Fund Following that development, in 2007 the controversial royalty bill passed in the Parliament and then it has been used to fund innovation and technology policies.

The factors explaining the overall success of the Chilean model have been, Jose Carlos pointed out the following: the existence of a political consensus; the autonomy of Chile's Ministry of Hacienda (Finance); the existence of a strong Ministry of Hacienda within an overall strong state; the presence of a Keynesian macroeconomic view; and the fact that overall there is less contestation of the Chilean political economy. He also noted the important contribution of CODELCO to success.

In the case of Peru, the country does have laws which allow for the creation of a countercyclical fund, but regulations are not fully enforced. There is also far more contestation and debate than in Chile. There has also been a strong decentralization process of mining revenue allocation without sufficient support to creating regional capacities.

Comparing the two cases, he concluded that: both countries have managed to save resources being generated in the recent boom of mining prices, but Peru was very less cautious A key reason of differences between savings is the differences between rent seizure: the state ownership of copper giant CODELCO in Chile, nationalized by Congress during Allende and kept public under Pinochet.

Leonith Hinojosa: "Poverty reduction and social policy in mineral dependent states".

Based on a co-authored paper, Leonith presented first an overview of the relationships between mineral wealth, revenue and social policies in mineral-rich developing countries. Then she addressed in more detail the outcomes of such relationships in terms of revenue capture and poverty reduction at sub national scale in Peru and Bolivia.

Using a social welfare framework, she explained that the most recent boom in mineral prices has generated expectations that mineral expansion should be favourable for social policy. Based on correlation and cluster analysis applied to 74 countries in the period 1995-2005, the paper analyzed: first, the extent to which state revenue and mineral export dependence are connected; second, the likely effects that mineral wealth may produce on the level and composition of social expenditure, and on the promotion of new social policy initiatives; and third, the role that government quality plays in determining mineral revenue capture and expenditure.

Their conclusions suggest that there is no conclusive evidence regarding a general pattern among mineral-rich countries with regards to the linkages between mineral wealth, state revenue and social welfare. However, the negative association between state revenue and levels of mineral export dependence, and the positive association between state revenue and social policy found in that analysis – together with insights from case-based literature – suggest the need to analyse the relationship between mineral wealth and social policy within an integrative framework. They also suggest that the inflow of mineral taxes has the potential to be the basis for transformative social policies and social development, which would overcome the underinvestment in social services and social protection so far seen in most of mineral rich countries.

With regards to the cases of Peru and Bolivia, she showed that the linkages between mineral revenue and its distribution across regions show no particular pattern in either country. However, in Bolivia as well as in some Peruvian regions, there is a notable co-existence of poverty and mineral activity.

Tony Addison: Commentator

Tony commented in thinking through the relationships among mining, revenue capture and distribution, employment and growth, the role of state institutions appears to be fundamental.

Observing that the state is a complex beast, he noted that analytical discussion tends to be focused at the central level, while a lot of the action is at local level. Therefore, the debate has hinged around governance issues - state effectiveness, democratic decision-making and accountability. Factors of geography and history weigh heavily here (though they are not deterministic).

He reflected on the case of Botswana, which is typically (and correctly) presented as a case of good macro-management of mining. Yet it is also the case that in Botswana, human development and various local indicators remain very disappointing. Speaking of and assessing "success" therefore requires much effort.

Another point he highlighted regarded the use of public income generated by mineral resources. Chile, he said, has a good system for managing this income (via inter-temporal transfers). The Chilean experience also shows that such systems for saving have to be constructed politically, and not just technocratically. On the other hand, given that savings are influenced by inflation, which come from non-national factors, there are hedging issues that need to be considered.

He concluded his comments emphasizing that, if chronic poverty is the issue, maybe the most effective use of mineral resources would be to invest them in human capital. Human capital is an input into all sectors of the economy. In that sense, social policy instruments such as pension funds can be designed in such a way that they help to reduce poverty while also supporting human capital formation.

Open discussion

Evelyn Dietsche suggested that when looking at the relationships between mineral dependence, fiscal issues, growth and social policy it was very important to distinguish between metal exporting countries and hydrocarbon exporting countries, and then treating them all as a single category of "mineral dependent economies" is misleading. Taxation systems and other qualities vary according to the nature of the resource dependence. Furthermore, within the category of metal dependent economies it is also important to differentiate according to the type of metals that are extracted.

Rosemary Thorp said that in the analysis of point resources geography becomes important – this because the human and social environment at the point of extraction matters greatly. In some cases (for instance Peru), mineral extraction occurs in areas that are populated (often by poorer people), while in other places (like Chile) the picture is completely different. She added that, together with geography and remoteness, the issue of expectation and trust becomes more important. She referred to the example of Tintaya (in Peru) where the company in question (Xstrata) is having difficulty spending resources locally because of community dynamics.

Andy Higgingbottom suggested that the role of multinational corporations in extracting a country's mineral wealth means that the issues should not be dealt with or discussed in terms of the relationship between 'the national and the local', but rather between 'the national and the international'. He added that it is in that international context that the relationships between companies and states need to be assessed. The introduction of mining codes – as a way of fostering economic growth – has adverse effects on welfare. He also drew attention to those instances in which, in support of extractive activity, the national state has criminalized the protest actions of local communities. Because national authorities rely on companies for the revenues they derive, companies' rather than citizens' interests have been given priority.

John Crabtree commented that presentations showed well the strengths and weaknesses of the state. He said the same applies to social movements and asked if there are particular factors that influence the presence and capacities of social movements at local levels. With regards to fiscal revenue, he said that the flow of this revenue over time series is unstable and then it is difficult to translate revenue into expenditure.

Alberto Hart from the Peruvian Embassy mentioned that FDI and particularly mining FDI occupy an important place in Peruvian development strategy. He also recognized that, in recent years, there has been frequent social conflict and opposition to large scale mining throughout the national territory. In response to this, the Peruvian government has implemented dialogue initiatives in order to foster a favourable environment for investments as well as propitious conditions for local development.

Richard Solly from the London Mining Network (LMN) pointed out that, although benefits from mining activity are being redistributed across space, there is no inter-generational redistribution occurring. The potential lack of resources for future development and the long term impacts and costs of mining may have appalling consequences for future generations. In response to A. Hart, he said that, in LMN's view, while local communities from Peru are invited to these dialogues, in practice the government and companies have taken their decisions in advance. In that sense, he emphasized that the ILO 169 Agreement gives to indigenous communities' more space to defend their rights than do these dialogues.

Various other interventions suggested the need to: conduct more comparative institutional analysis of the sector; do further study on the autocratic ways in which mining codes are established; conduct deeper analysis of local level relationships between communities, donors and companies, further understanding of the particularities of state bodies at national and local levels; work with more precise definitions of the nature of social policy and opportunities for poverty reduction; further differentiate between the sectors when talking of the mineral industry (especially between hydrocarbons and mining) and conduct deeper study of the relationships between these sectors; do more work on who wins and who loses in the process of mineral expansion; expose and measure hidden costs of mineral expansion; and deepen understanding of the negotiation and convening roles that states need to play in every community where mining is present.

General responses from presenters drew attention to:

- the role of expectations and trust;
- the general vacuum observed in local and national governments;

- the difficult position in which mining companies are placed when they are obliged; to assume the roles that the government ought be playing;
- the need to understand local governments from a political economy point of view;
- the importance of conceptualizing social policies not just as social services; provision but as sources of social protection and enhanced human development;
- the importance of analyzing mining impacts across different time spans.

The morning session concluded with interventions from John Groom and Tony Bebbington. John Groom reminded the room of the usefulness of the toolkits that have been created to help improve the relationships between companies, communities and governments. Tony Bebbington noted that certain themes had been recurrent in the discussion, drawing special attention to the questions of geography raised by R. Thorp.

Part 2: Subnational perspectives

Maritza Paredes: "Building institutions - the politics of the use of rents from the mining sector: Peru, Chile and Bolivia compared."

Maritza presented a comparative analysis of the distributive schemes in Peru, Bolivia and Chile to share mining and hydrocarbon revenues with sub-national levels. She suggested that in the three countries mining revenue has increased significantly since 2001. In Peru and Bolivia, the existing schemes have directly transferred more than half of the resources to sub-national levels of government. However the capacity of sub-national governments to manage these resources has proved to be still very problematic. Unlike Peru and Bolivia, Chile has no particular rule for regional distribution. Yet, Chile counts with other mechanisms of regional redistribution of revenue but not credited to the production of mineral resources, such as the National Fund for Regional Development (FNDR). By 2007, the percentage of national investment decided through these instruments at regional level has been close to 60%. This type of redistribution not attached to the production of minerals or hydrocarbons has permitted a more equal redistribution across regions, but recently some contesting voices from the producers regions have been heard. Another characteristic of the Chilean scheme is the strong presence of the central state to ensure a growing capacity of sub-national level in the management of these resources.

With regards to revenue utilization by local governments (regional governments and municipalities), she showed that the schemes of discretionally are quite different in each of the countries. While Chile has a more open portfolio with the only condition that they comply with the budget law and the national investment system (SNI). In Peru started with little discretionally but has become more permissible over the last seven years, going from infrastructure projects only in 2001 towards almost all sorts of local development projects in 2007. All these changes have been made by small amendments to the law and as a response to the demands of regional and local governments. In Bolivia, under the decentralization law, it was decided that 85% of the funds must be used in investment projects and the Direct Tax on the Hydrocarbons Law also declared that these fund must be used in "investment in education, health, roads and economic development" but the "Operational" laws have opened the door for a wide range of uses.

She concluded suggesting that these schemes are developed several times by politicians in contexts in which the abundance of resources is not considered a problem. At the end, she said that further research is needed to understand how the institutional structures allow policy innovation and how much space is left for discretion at the several levels of government units.

Javier Arellano: "Fiscal transfers and challenges to local public management in mineral economies: the *canon minero* and local development in Perú".

Javier addressed the challenges faced by local units of government when they receive mineral revenue transfers and have to use these for local development investments. He presented Peru as a paradigmatic example of the 'resource curse' at a local level due to observed weaknesses in the government, both at national and local levels. As a result, the relationships between local governments, mining companies and a variety of local groups are difficult to negotiate. This is what gives rise to conflicts and poor quality public investment.

With regards to fiscal transfers and their relation to conflicts between mining companies and local communities, he suggested that conflict is increasingly related to the transfers of the "canon minero" – poverty rates have become progressively less powerful as an explanation of the incidence of conflict. The majority of these conflicts can be understood as 'tactical" in that they are means of gaining access to resources from companies. Although local populations have framed their claims using ecology, ethnicity and social justice discourses, the real negotiations usually focus on employment opportunities, economic compensation, promotion of small local business and the implementation of social projects.

Javier suggested that conflicts over the control and use of mining resources are directly related to 'mining canon' transfers and can be grouped as follows:

- Conflicts between the local population and local authorities regarding the inability of local institutions to invest *canon minero* transfers efficiently
- Conflicts between different levels of government over distribution of the canon
- Conflicts over the territorial limits between jurisdictions (as these define the proportion of the canon going to different authorities

He concluded suggesting that the mining bonanza has revealed structural limitations in the Peruvian mining regime and the ways in which it seeks to transform mineral wealth into peoples' well-being. The most notorious symptom of a new form of resource curse at a local level is the growing incidence of conflict in mining regions.

Jeffrey Bury: Comments

Jeff's comments on the two presentations emphasized the need to understand the ways in which conflicts emerge and how they evolve. He added that a historical perspective on conflicts provides opportunities to researchers to look at the political economy factors that underlie conflicts in the mining sectors and how these are related to the different conceptions and interpretations of natural resources use.

He highlighted the differences among in the ways in which discussions and decisions regarding the distribution of mining revenue had entered public debate in different countries. Common to the cases discussed is the influence of politicians' priorities and views on the use of resources.

In a broader view of mining in Andean environments, Jeff said that much more will now need to be done to understand the effects that the financial crisis and associated reallocation of capital and investments will have on the sector. There is also a need for more careful assessment of the environmental impact of mining over the last 15 years, particularly with regards to water sources. Such an assessment would have to take into consideration issues such as population density, water scarcity in mountain environments, the proximity of mining concessions to towns and the institutional structures that exist in each country for governing water use and management.

Open discussion

Questions from participants focused on:

- the possibilities of countercyclical management of mineral resource management;
- the likely future scenarios in local territories after mining and hydrocarbons activities end;
- the tensions between national and sub national levels of government;
- the role of the state in a neoliberal model which facilitates large scale mineral expansion.

Presenters replied highlighting the need to understand processes of institutional development and state formation in historical perspective. For instance, Maritza said that in Chile institutions that are currently in place have been built over centuries. Furthermore the party system is strong too (another product of history). While this leads to tensions between the legislative and the executive bodies of the state, in practice there is agreement in Chile on a national strategy in which resources generated by mining are invested in innovation. By contrast, in Peru institutions and parties are weak and tensions are more apparent between regional and national government than between the legislative and executive branches. Javier noted that in the Fujimori period, tensions between Peru's regional and local governmental units increased because of the tendency of the central national government to prioritize transfers to district municipalities. In that process some capacity building may have been facilitated, however according to his research findings district level local government can only guarantee expenditure efficiency up to some limited amount of money. On the other had, he said, the emblematic conflicts are complex, but the Peruvian government cannot distinguish among them and it tries to solve problems one per one. The easiest answer to conflicts has been to suggest that terrorism is involved and, notwithstanding the fact that the local army says that this is not the case, senior government technocrats and politicians continue to label people and conflicts in this way.

The discussion then moved to an overall view of both morning and afternoon sessions. A group of comments hinged around the issue of government capacities.

Sulemanu Koney from the Ghanaian Chamber of Mines mentioned that Ghana has many commonalities with what has been discussed for Andean countries. He added that Ghana has an institutional structure which guarantees efficient spending. John Crabtree recalled the Bolivian experience of decentralization (with the Law of Popular Participation) and pointed to its importance for capacity building at a local level. In a similar line, another participant mentioned that in Bolivia, despite all the limitations, the Popular Participation law continues to be highly valued.

Evelyne Dietsche said that ICMM's study concluded that, in general terms, countries have two different types of revenue management systems. One system is more political-administrative in style (as in Peru) while the other is more technocratic (for instance in Tanzania). She added that further study is needed to see the extent to which the relationships between and relative power of the legislative and the executive branches of government determine the way in which government expenditure is influenced. Leonith Hinojosa suggested that to assess the efficiency of different levels of government (national and sub national) requires care in determining the time period over which changes in the capacities for revenue management are analyzed; she added that in countries like Peru the central government has always had the monopoly of revenue capture and expenditure and it has not shown much efficiency. Decentralization to regional and local levels is only a recent phenomenon – post 1990s – and so it is too soon to draw quick conclusions about the ineffectiveness of these levels of government on the basis of the recent experience of the limited capacity to spend the *canon minero*. Jumping quickly to these conclusions could lead to the argument that resource management should be recentralized and that is not necessarily desirable. Patricia Oliart suggested government spending in local communities often reflects clientelistic relations, and that the absence of political parties in local government means that there is little scope for strategic decision making. Jose Carlos Orihuela noted that given in a context in which populism underlies much decision making, technocrats see little purpose in strategic planning.

On the mining companies' role in institutions building, Javier Arellano suggested that in many cases they have not helped build social capital at sub national levels. One problem is that they make too many promises and they then cannot fulfil all the expectations created in local communities. Although companies often have good professionals for managing community relations, these teams often have tense and difficult relationships with the mine's 'operations' section. For instance, while the operations department works with quite short run time horizons, the community relations department often needs more time to establish relationships and trust. Once conflicts happen, it is then difficult for the company to restore trust and good relations with communities because the local fabric is broken.

Several participants agreed that institutions must be in place before resources flow into sub national government units in order to ensure efficient expenditure. However, it was also noted that institution building take many years and that there is a mismatch between the period during which fiscal resources become available and the periods required to build adequate government structures. In that sense, companies should not only be concerned with obtaining social licence at a community level, but also work well in advance with states in order to build the local capacities necessary for effective management and investment of the resources generated by mining. Some companies' experiences may well show that such effort can pay off. Jeff Bury added that talking about companies as a single unit is itself problematic and wondered whether there are different degrees and types of conflict depending on companies' origin (national, international, particular countries and so on). In a similar vein, Fernanda doz Costa called for more care in distinguishing between state and government.

Closing the discussion, a final round of interventions pointed to the need for further research on: the geographies and politics of changes in the composition of mining and hydrocarbon sectors; the role of nationalist states; the several interests involved in natural resources extraction not just at national level but at regional Latin American level and the roles being played by new actors (China, India); how to avoid a purely technocratic view of fiscal systems and bring political analysis into the picture (making explicit the relationships between mineral wealth, fiscal systems, poverty reduction, human capital formation and social movements); and the lessons that can be learnt from Latin America for Africa (particularly in the realms of conflicts and financial resource management).

John Groom and Tony Bebbington formally closed the seminar acknowledging the importance of the collaborative work between ICMM and the University of Manchester to carrying out the event. Further reading from the material produced by ICMM was suggested and the 4th seminar in the TCD Andes series was announced. It will be held in Newcastle on March 20th, 2009, and jointly organized with the Developing Areas Research Network based at Newcastle University.