THE EMERGING INTERNATIONAL FRAMEWORK FOR THE SUSTAINABLE DEVELOPMENT OF NATURAL RESOURCES: *Some Questions for Investment Lawyers*

Luke Danielson

I. Growth of Rules Governing Extractive Industries

A. Explaining Poor Development Results

Markets without rules often produce bad results.[1] Where there is no common understanding of what buyers and sellers have a right to expect in terms of quality and metrics, or there are no consequences for failing to meet such standards as may exist, commerce is slow and inefficient, and transaction costs are very high, as the parties have to engage in lengthy due diligence on every transaction.

If there is a notable difference in bargaining power, access to relevant information, and expertise between buyers and sellers, there is considerable room for chicanery and abuse, particularly if there are no authorities capable of detecting and punishing it. If in addition there is a lack of transparency in the process, all forms of corruption can thrive.

Where there is no effective restraint on buyers and sellers who are trying to externalize costs onto third parties, the level of negative social or environmental externalities can lead to conflict as the people who are suffering those consequences seek to vindicate their interests.

Many observers see these conditions as prevailing too frequently where international resource investors and poor developing countries negotiate the terms on which mining, oil and gas, and other resource companies gain access to mineral resources. And these issues are probably central to the difficult and very important question of why developing countries have had such great problems making resource based development strategies, and countries with considerable resource endowments in many cases have lower economic growth than countries less well endowed, the "paradox of plenty."

There seems to be an intuitive 'deal' that could be reached in which the wealthy consumers in the global North obtain access to the mineral resources they so desperately want, and the poor countries of the South leverage these financial flows to create schools, clinics, housing, and infrastructure to create a better life for their populations. But this 'deal' is not working, or at least not working well enough to meet the expectations of the poor, or to keep damage to earth's ecosystems within tolerable limits.

[1] Indeed, if there are no rules at all, there may be transactions, but it is very hard to say there is a market.

The paradox that nations rich in mineral wealth may suffer slow development and related adverse consequences is known as the "resource curse" hypothesis. Professor Gylfason has identified its main symptoms as:

> […] [N]ations that depend heavily on their natural resources tend to have (a) less trade and foreign investment, (b) more corruption, (c) less equality, (d) less political liberty, (e) less education, (f) less domestic investment, and (g) less financial depth than other nations that are less well endowed with, or less dependent on, natural resources.[2]

Concern about a "resource curse" grew from the late 1980s onward, as numerous studies found low levels of economic growth in mineral-rich nations over long periods.[3] Empirical studies in the late 1990s and early 2000s found that nations that relied more heavily on mining were more likely to experience slower growth after controlling for other factors.

Jeffery Sachs and Andrew Warner published some of the most influential work in this area, finding that an inverse link between natural resources wealth and economic growth persisted even after correcting for a variety of other suggested variables.[4]

While there are those who question the strength or importance or even the existence of the resource curse,[5] the real test may be not whether economists think that poor people are better off, but what the world's poor think. And they seem to be overwhelmingly of the opinion that resource extraction, even when it occurs very near them, is not delivering the expected results. The current crisis in South Africa is just one of many examples.[6]

---

[2] Thorvaldur Gylfason, "Natural resources and economic growth: From dependence to diversification" (Zurich: Center of Economic Research at Eidgenössische Technische Hochschule Zurich, 2004), p. 1, available at: http://www.cer.ethz.ch/resec/sgvs/029.pdf (last visited July 16, 2012).

[3] Graham A. Davis and John E. Tilton, *The Resource Curse*, 234 Natural Resources Forum 29 (2005). One important early study is by Richard M. Auty, *Resource Based Industrialization: Sowing the Oil in Eight Developing Countries* (Oxford: Clarendon Press, 1990).

[4] Jeffrey D. Sachs and Andrew M. Warner, "Natural resource abundance and economic growth," National Bureau of Economic Research Working Paper (Cambridge, Massachusetts: Harvard University Center for International Development and Harvard Institute for International Development, November 1997), pp. 26–28. (This work provides an excellent overview of relevant resource curse literature going back to the emergence of the theme in the development literature of the 1950s and 60s.) (Sachs and Warner published other influential studies in 1995, 1999, 2000, and 2001.)

[5] E.g. Brunnschweiler and Bulte, The Resource Curse Revisited and Revised: A Tale of Paradoxes and Red Herrings, CER-ETH (2006).

[6] Reuters, S.African Mine Unrest Spreads, Toyota Hit by Strike, Oct. 4, 2102, http://www.reuters.com/article/2012/10/04/safrica-strikes-idUSL6E8L458S20121004 (accessed October 4, 2012).

B. Natural Resource Projects and Social Conflict

It has become evident that the closed system in which the terms of resource development are of concern only to the investors and the host state is under serious challenge.. A very recent case from Peru is illustrative. Newmont, one of the world's major mining companies, was trying to develop the Conga deposit in the Andes, in the same region as Newmont's largest producing property, the Yanacocha Mine. Newmont announced in 2011:

> *"Newmont is developing its portfolio of world-class mining opportunities, including the Conga project in Peru, a large, copper-gold porphyry located 24 kilometers northeast of Newmont's Yanacocha gold mine.*
>
> *Conga is part of Newmont's strategic plan to reach 7 million ounces of gold and 400 Mlbs of copper by the year 2017 while developing a diverse South American asset base."*
>
> * * *
>
> *As of December 31, 2010, Conga held approximately 6.1 million attributable ounces of gold reserves and 1.7 billion attributable pounds of copper reserves for the Conga Project."*[7]

Less than a year later, in August, 2012, after public protests against Conga grew dramatically and ultimately ended in violence,[8] both the Peruvian government, which had already approved the Semi-Detailed Environmental Impact Study (sdEIS), a First Modification of the sdEIS, and the Environmental Impact Assessment for Conga,[9] and Newmont have taken a major step back, as reported in the industry press:

> **Peru suspends Newmont's Minas Conga copper-gold project**
>
> *With the suspension and likely cancellation of the Minas Conga project, Newmont is about to lose its goal of achieving 7 million ounces of annual gold production by 2017.*
> Author: Dorothy Kosich
> Posted: Friday, 24 Aug 2012
>
> RENO (MINEWEB) -

[7] Newmont, Conga Fact Sheet, http://www.newmont.com/sites/default/files/u87/Conga_FactSheet.pdf (last accessed 9/18/2012).

[8] *Fifth Person Killed in Minas Conga Protests,* Andean Air Mail and Peruvian Times, Jul. 6, 2012, *available at* http://www.peruviantimes.com/06/fifth-person-killed-in-minas-conga-protests/16179/.

[9] Timeline, http://congaeuropa.wordpress.com/el-proyecto-conga/timeline/.

> *Even the Peruvian government appears to have thrown in the towel on Newmont Mining's controversial Minas Conga Project as the nation's prime minister announced Thursday the project is now on the "back burner."*
>
> *A recent poll conducted by Peru's most respected polling firm, Ipsos, found 78% of the 250 people polled in the province of Cajamarca are opposed to the proposed gold mine.*
>
> *After the poll was made public Wednesday, Prime Minister Juan Jimenez told reporters, "We have entered a different scenario, the project has entered a new phase of suspension that the company already decided on and the government of course asked for."*[10]

This kind of event is not new or unique. Indeed, it is not even new and unique to Newmont, or to Newmont's experience in Peru, a country where this major company has two decades of experience as a major mine operator.

In 2004, Newmont was forced by similar events to suspend its Cerro Quilish project, a deposit in northern Peru with proven and probable reserves of 3.7 million ounces of gold.[11] Attempts to move forward with Cerro Quilish ended when thousands of local people occupied the site and announced they would not leave until Newmont abandoned development.[12]

There are a considerable number of such project failures in recent years, many of them in South America, and many of them affected by that region's rapidly growing indigenous movement. Some of the project failures that come to mind, beyond Conga and Cerro Quilish are:

Rio Blanco	Perú
Tambo Grande	Perú
Santa Ana	Perú
Junín	Ecuador
Esquel	Argentina
San Jorge	Argentina
Cerró Colorado	Panamá
Imperial Project	California, USA
Mt. Emmons	Colorado, USA
Jabiluka	Australia
Tampakan	Philippines

[10] Dorothy Kosich, *Peru Suspends Newmont's Minas Conga Copper-Gold Project*, Mineweb, Aug. 24, 2012, *available at* http://www.mineweb.com/mineweb/view/mineweb/en/page34?oid=157590&sn=Detail.

[11] Emily Russel, *Protests continue over Cerro Quilish, Resolution Pending*, Business News Americas, Sept. 14, 20014, *available at* http://www.bnamericas.com/news/mining/Protests_continue_over_Cerro_Quilish,_resolution_pending.

[12] Cajamarca, Peru, No Dirty Gold, *available at* http://www.nodirtygold.org/cajamarca_peru.cfm - F9.

Bougainville	Papua New Guinea
Rosia Montana	Romania

What would be tens of billions of dollars worth of minerals if they could be mined remain in the ground despite immense efforts of some of the world's largest mining companies.

In at least one of these cases, social protest forced shutdown of an already operating mine. In some of these cases, developers stopped or suspended work when it became clear that their efforts would be unsuccessful. In others, government issued permits, but then either moved to revoke them or requested companies voluntarily to stop moving forward in order to defuse massive social conflicts. In yet others, the permitting process was suspended, or permits were denied.

A key point is that in circumstances where mineral projects have failed to gain a social license and become the focus of major opposition social movements, the question of whether a permit is granted or denied is really secondary: the project simply cannot be developed.
Any attempt to push forward is likely to result in unacceptable levels of social conflict and violence. Most governments are reluctant to use overwhelming military or security force against their own citizens. And this conflict is extremely costly to investors.

Even where mines can go into production, the cost of staying open is enormous. The following table shows the security costs, both payment for internal security managed by the company and external payments to the Indonesian military and police forces by Freeport McMoran, for the protection of one mine, Grasberg.

TOTAL REPORTED SECURITY COSTS -- DIRECT[13]			
YEAR	**INTERNAL**	**EXTERNAL**	**TOTAL**
2001	$6.8 MILLION	$4.7 MILLION	$11.5 MILLION
2002	$7.7 MILLION	$5.6 MILLION	$13.3 MILLION
2003	$11.2 MILION	$5.9 MILLION	$17.1 MILLION
2004	$12.3 MILLION	$6.9 MILLION	$19.2 MILLION
2005	$11.3 MILLION	$6.2 MILLION	$17.5 MILLION
2006	$14.2 MILLION	$8.5 MILLION	$22.7 MILLION
2007	$17 MILLION	$9 MILLION	$26 MILLION
2008	$22 MILLION	$8 MILLION	$30 MILLION
2009	$18 MILLION	$10 MILLION	$28 MILLION
2010	$28 MILLION	$14 MILLION	$42 MILLION
2011	$37 MILLION	$14 MILLION	$51 MILLION
		Total=	**$278.3 MILLION**

[13] From Freeport's Form 10-K filings with the United States Securities and Exchange Commission.

C. Creation of Standards

Improving on these poor results is on the top of the industry agenda. One solution has been rapid development of standards in the natural resource markets, in order to achieve a variety of objectives:

a. reducing transaction costs and the costs of due diligence by agreeing on standard practices and standard obligations;
b. creation of systems that help to balance the disparities in information and bargaining power to create more equitable transactions;
c. increasing the transparency of the system to reduce corruption and ensure greater accountability of all actors;
d. protecting the rights of third parties affected by development; and
e. reducing negative externalities and creating a more equitable sharing of the benefits and burdens.

In short, the concept is to create better and more clearly understood rules for mineral resource markets in the interest of supporting sustainable development of host countries and communities. This in turn has the potential to create greater social acceptance of mining, and more stable and predictable conditions of investment, a cherished goal of investors.

A major problem has been this: global markets require some kind of global rules. But there is a real shortage of international institutions with attributes that allow them to make and enforce rules. There is thus a powerful demand for rules, but a very limited supply of institutions capable of creating them.

The news is that there has been some success in working around this problem. The last twenty years have seen the rapid development of a considerable set of standards, principles and guidelines for international mining investment.

Developed in different ways, applied by very different types of bodies, and observed with varying degrees of strictness or flexibility, they nevertheless now form an indispensable and increasingly unavoidable part of the landscape for mining investors, host governments and others. Some of them are driven by a desire to improve environmental protection, or to ensure that the basic human rights of the most vulnerable are observed. The most widely observed rules were developed by financial institutions precisely for the purpose of reducing social and environmental project risk.

A compilation of most if not all of these rules is set out as Table I.

Table 1[14]
Baseline for Generally Accepted International Best Practice
In the Mining and Minerals Industries[15]

Report of the Mining Minerals and Sustainable Development Project

In 1999, key leaders in the minerals industry, government and civil society initiated what became a three-year process of consultation, research and dialogue, the Mining, Minerals and Sustainable Development Project. The report of that effort, submitted at the World Summit on Sustainable Development in Johannesburg, is widely recognized as a base line for performance in the minerals industries. The final report from 2002 is entitled, *Breaking New Ground: Mining, Minerals and Sustainable Development*, and is available on the website of the International Institute for Environment and Development at: http://pubs.iied.org/9084IIED.html (last visited: July 16, 2012).

Extractive Industries Review

In 2002, the World Bank began a three-year review of its policies in the extractive industries under the leadership of Indonesia's former Environment Minister, Dr. Emil Salim. While the World Bank failed to accept all of its recommendations, the Extractive Industries Review's (EIR) final report in 2004, *Striking a Better Balance – The World Bank Group and Extractive Industries: The Final Report of the Extractive Industries Review*, is a widely recognized source of best practice and is available at: http://www.ifc.org/ifcext/eir.nsf/AttachmentsByTitle/FinalMgtResponseExecSum/$FILE/finaleirmanagementresponseexecsum.pdf (last visited July 16, 2012).

International Council on Mining and Metals Principles and Toolkits

The International Council on Mining and Metals (ICMM)has produced the "ICMM Principles," widely regarded as a consensus statement of the expectations for the social, economic and environmental performance of mining companies. The ICMM Principles are available at:

---

[14] This Table will appear in Danielson And Phillips, The International Bar Association Model Mine Development Agreement Project: A Step Toward Better Practice and Better Development Result, in teh forthcoming 2012 Columbia INVESTMENT YEARBOOK.

[15]There are other authoritative statements of practice applying to specific issues affecting particular segments of the minerals industries. Examples are the Kimberly Process (diamonds) and the Cyanide Management Code (for processing employing cyanide).

http://www.icmm.com/our-work/sustainable-development-framework/10-principles (last visited July 16, 2012).

The International Council on Mining and Metals has further produced "Toolkits" that are widely recognized as best practice guidance on the subjects that they address. These Toolkits include topics such as *Planning for Integrated Mine Closure, Indigenous Peoples and Mining, Mining: Partnerships for Development*, and many more are available at: www.icmm.com/library (last visited July 16, 2012).

Global Reporting Initiative

The Global Reporting Initiative (GRI) is a network-based organization that produces a comprehensive sustainability-reporting framework of principles and performance indicators that organizations can use to measure and report their economic, environmental, and social performance. This GRI (and its *Mining and Metals Sector Supplement*) forms the base line for reporting on environmental, social and economic performance in the minerals industries. The GRI and the *Mining and Metals Sector Supplement* are available at: https://www.globalreporting.org/reporting/sector-guidance/mining-and-metals/Pages/default.aspx (last visited July 1, 2012).

Global Compact

"The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. By doing so, business, as a primary driver of globalization, can help ensure that markets, commerce, technology and finance advance in ways that benefit economies and societies everywhere." Global Compact Website, http://www.unglobalcompact.org/AboutTheGC/ (last visited August 3, 2012).

Model Mine Development Agreement

The International Bar Association has developed, through a highly consultative process, a drafting tool designed to result in more informed and equitable negotiation of mine development agreements. The goals of this effort include facilitating greater development benefits for host countries and their communities, and greater stability of investment conditions for investors. www.mmdaproject.org (last accessed August 3, 2012).

Extractive Industries Transparency Initiative

The Extractive Industries Transparency Initiative (EITI) is a set of principles and procedures aimed at strengthening accountable and transparent governance in resource-rich countries

through the verification and full publication of company payments and government revenues from oil, gas and mining. It's centered on a coalition of governments, companies, civil society groups, investors and international organizations. More information on the EITI is available at: http://eiti.org/ (last visited July 1, 2012).

Voluntary Principles for Security and Human Rights

The Voluntary Principles for Security and Human Rights provide a broad framework that can help companies operate in ways that provide security to their facilities while respecting human rights and fundamental freedoms. Unveiled in December 2000 by the U.S. State Department and the Foreign and Commonwealth Office of the United Kingdom, after a yearlong process involving government officials, oil and mining companies, and non-governmental organizations (NGOs). The Voluntary Principles for Security and Human Rights provide guidance to companies operating in zones of conflict or fragile states and are available at: http://www.voluntaryprinciples.org/files/voluntary_principles_english.pdf (last visited July 1, 2012).

IFC Performance Standards

The Performance Standards of the International Finance Corporation (IFC) are applicable to all projects supported by the IFC and the Multilateral Investment Guarantee Agency (MIGA), both arms of the World Bank Group. The Performance Standards are available at: http://www.ifc.org/ifcext/sustainability.nsf/Content/PerformanceStandards (last visited July 16, 2012).

The Performance Standards are also broadly applicable to projects supported by most private financial institutions, through their adherence to the Equator Principles, which are available at: http://www.equator-principles.com/ (last visited July 16, 2012).

Furthermore note that the Performance Standards have recently been revised considerably; more information from Mehrdad Nazari, "Updated IFC Performance Standards and changes to Equator Principles" (Wausau, Wisconsin: Prizma, 2011), available at: http://prizmablog.com/2011/05/24/updated-ifc-performance-standards-and-changes-to-equator-principles/ (last visited July 16, 2012).

Human Rights

The United Nation's Guiding Principles on Business and Human Rights, which now represent the UN's official position on corporate duties toward human rights, are available at: http://www.business-humanrights.org/media/documents/ruggie/ruggie-guiding-principles-21-mar-2011.pdf (last visited July 16, 2012). The Special Representative's online portal is available at: http://business-humanrights.org/SpecialRepPortal/Home (last visited July 16, 2012).

OECD Guidelines for Multinational Enterprises

The *OECD Guidelines for Multinational Enterprises* were updated in 2012 to incorporate human rights into corporate duties. They are available at: http://www.oecd.org/dataoecd/43/29/48004323.pdf (last visited July 16, 2012).

Indigenous Communities And Extractive Industries

James Anaya, the United Nations Special Rapporteur on the Rights of Indigenous Peoples, issued a preliminary report on August 30, 2011, which is available at: http://unsr.jamesanaya.org/notes/annual-report-to-the-human-rights-council-with-preliminary-assessment-of-extractive-industries-operating-in-or-near-indigenous-territories (last visited July 16, 2012).

The Special Rapporteur's online portal further contains a variety of useful national studies and is available at: http://unsr.jamesanaya.org/index.php (last visited July 16, 2012).

Akwé: Kon Guidelines

The *Akwé: Kon Voluntary Guidelines for the Conduct of Cultural, Environmental and Social Impact Assessments Regarding Developments Proposed to Take Place on, or which are Likely to Impact on, Sacred Sites and on Lands and Waters Traditionally Occupied or Used by Indigenous and Local Communities (Akwé: Kon Guidelines)*, prepared by the Secretariat of the Convention on Biological Diversity, are designed to set out accepted processes for consultation of indigenous communities where development may impact indigenous lands and resources. The *Akwe-Kon Guidelines* are available at: http://www.cbd.int/doc/publications/akwe-brochure-en.pdf (last visited July 16, 2012).

Framework for Responsible Mining

The Framework for Responsible Mining is a joint effort by N-G Os, retailers, investors, insurers, and technical experts working in the minerals sector. It outlines environmental, human rights, and social issues associated with mining and mined products and it is available at: http://www.frameworkforresponsiblemining.org/ (last visited July 16, 2012).

The Natural Resource Charter

The Natural Resource Charter is a set of principles for governments and societies on how to best harness the opportunities created by extractive resources for development and is available at: http://www.naturalresourcecharter.org/ (last visited July 16, 2012).

Extractive Industries Source Book

A website that attempts to collect widely recognized statements on current best practice in the extractive industries -particularly in oil, gas and mining. It is run from the Centre for Energy, Petroleum and Minerals Law and Policy at the University of Dundee. The Extractive Industries Source Book is available at: http://www.eisourcebook.org/ (last visited July 16, 2012).

There are standards for corporate observance of human rights, disclosure of information, consultation of affected stakeholders, resettlement of displaced people, existence and character of grievance mechanisms for people who allege they have been harmed by project activities, environmental management, impacts on indigenous communities, biodiversity, and cultural resources.

One question worth exploring is what has driven this very considerable development of norms in this sector, and whose needs it serves to have such standards. It appears that in most cases these norms are wanted by many different interests, rather than being imposed on the unwilling.

A second initial question is how such norms can legitimately be developed in the absence of international law making bodies with the characteristics of sovereignty.[16] With any body of rules with pretensions to affect behavior of commercial actors in markets, it is important to ask what the rules are, how they were developed, and by whom. It is also important to ask about verification: who decides whether the norms are being complied with? Finally, the question of

[16] Luke Danielson and Caroline Digby, Architecture for Change: An Account of the Mining, Minerals and Sustainable Development Project, Linda Starke ed., (Global Public Policy Institute 2006), *available at* http://www.gppi.net/fileadmin/gppi/MMSD_Full_Report.pdf.

consequences is critical: what are the incentives for compliance, or disincentives for noncompliance.

But the demand for such rules is so strong that they are being taken up, used and institutionalized at a remarkable rate.

The body of norms in the extractive industries is becoming more important and more influential as a result of several trends, among them cross-linkage (one set of norms requiring compliance with other sets of norms), stronger verification mechanisms, and stronger incentives for compliance, as well as increasing user familiarity and the force of habit. In addition, pieces of these privately agreed and "voluntary" rules are increasingly being incorporated in hard law.

II. Standards as a Means of Mediating Conflict and Reducing Risk

Many of the standards on which we are focusing were created for the specific purpose of reducing project risk. For example, the Equator Principles website announces that:

> *"The Equator Principles is [sic] a credit risk management framework for determining, assessing and managing environmental and social risk in project finance transactions."*[17]

The Performance Standards of the International Finance Corporation were developed for similar reasons. " IFC's Sustainability Framework articulates the Corporation's strategic commitment to sustainable development, and is an integral part of IFC's approach to risk management."[18]

In short, a considerable number of the international standards are bank-originated, bank-driven and bank-enforced. They are oriented to the things that the best experts in the field say will reduce project risk.

Saying that complying with these standards is unnecessary, or that the need to observe them can be contracted away is to accept a much higher degree of risk to the project.

III. Mine Development and Negotiated Agreements

Much of the discussion in this area focuses on mine development agreements, contracts under which host states and mineral investors negotiate the terms under which mineral deposits are

[17] http://www.equator-principles.com/

[18] IFC, Overview of Performance Standards on Environmental and Social Sustainability, http://www1.ifc.org/wps/wcm/connect/bff0a28049a790d6b835faa8c6a8312a/PS6_English_2012.pdf?MOD=AJPERES

developed. Most of the wealthy more "developed" countries do not use this system. They have laws under which development occurs, and do not negotiate each separate mineral license is issued. Yes many of the poorest countries do use such agreements. And since the role of mineral resources in development is at the center of this article, we will focus on negotiated agreements with investors.

But we need to keep in mind that in the view of many, mine development agreements simply should not exist. Countries that want to enter the hazardous business of a development path based on mineral endowments should, in this view, instead have mining laws, tax laws, environmental laws and so forth, and follow them; everyone would follow the same rules. The advantages of this path are many, which is why so many experts want to move away from contracts as the basis for mineral development to licensing or leasing systems such as those typically found in the more advanced economies.

Among the advantages to such a uniform system of concessions would be that decisions to about which mineral deposits to develop are more likely to be based on underlying scarcity relationships and less likely to be based on distorted economic relationships created through negotiation.

This kind of system creates a greater perception of fairness and is easier to administer: all investors are taxed under the same system, receive the same kind of property rights, and follow the same environmental or labor laws.

Trying to negotiate every one of the legal elements of a project can place enormous burdens on the capacity of the institutions of some of the poorest governments in the world. If corruption is an issue, negotiation of rights to government owned resources has been one of the most fruitful sources of government corruption. Having a single set of standards, written in law, that apply to everyone, may make corruption at least marginally more difficult.

For whatever reason, however, many countries do negotiate "one off" mining deals. How emerging international standards may affect the negotiation and enforcement of such agreements is at the heart of the question of whether the minerals-based development model can be made to work for the poorest countries, a question or real moment for us all. This is not least in part because the leading institutions in the world economy have not come up with a convincing alternative plan. If minerals based development doesn't work, it is not at all clear where our hopes might be pinned.

IV. Possible Roles for International Standards

An obvious set of questions arise as to the legal effect of these international norms. If an investor fails to comply with recognized international practice, does that defeat some kinds of claims investors might otherwise be able to make in lawsuits or arbitration? Is it grounds for termination of the agreement? For denial of a permit by a government agency?

The question may have enormous importance for the future of some arrangements that are very important for development of host countries, and for the stability of commercial arrangements involving very large amounts of invested money.

There are at last four possible cases for international standards in negotiated agreements:

1. The agreement between host country and investor requires application of "international standards", or "best practice" generally;
2. The agreement mentions some specific standards but not others;
3. The agreement is entirely silent on the subject.
4. The agreement purports to excuse the investor from complying with some or all of these international standards.

We will look at each of these possibilities in turn.

A. What is the Effect of a Contract Requirement of "International Standards" or "Best Practice" Generally?

The agreement between the government of Mongolia and Ivanhoe Mines for the development of the massive multibillion dollar Oyu Tolgoi copper deposit[19] provides, in part:

> "The Investor shall continue to prepare, conduct, implement, update on an appropriate basis, and make public socio-economic baseline studies, socio-economic impact assessments, socio-economic risk analyses, as well as multi-year communities plans, community relations management systems, policies, procedures and guidelines, and mine closure plans, *all of which shall be produced with community participation and input and be consistent with international best practice.*" [emphasis supplied][20]

Chapter four of the agreement on regional development references "international best practices" multiple times in different sections. Elsewhere, the agreement states that the agreement will continue in force if:

---

[19] Euan Rocha, *UPDATE 2-Ivanhoe finalizes Oyu Tolgio investment agreement*, Reuters, Mar. 31, 2010, *available at* http://www.reuters.com/article/2010/03/31/ivanhoe-oyutolgoi-idUSN3120661520100331?type=marketsNews.

[20] Investment Agreement Between The Government of Mongolia and Ivanhoe Mines Mongolia Inc LLC and Ivanhoe Mines LTF and Rio Tinto International Holdings Limited, Oct. 6, 2009, Chapter 4, 4.7, p. 15, *available at* http://www.mmdaproject.org/presentations/MMDA Mongolia Ivanhoe Agrt-1.pdf.

> "The Investor demonstrates that the OT Project has been operated in accordance with *industry best practice* in terms of national and community benefits, environment and health and safety practices;" [emphasis supplied][21]

An agreement in the Philippines imposes the obligation

> "To conduct Mining Operations within the Contract Area in accordance with this Agreement, the Act, … including the principle of sustainable mining and other principles embodied therein and with efficient, *internationally accepted Mining Operation practices*." [emphasis supplied][22]

Section 5.4 on social impact assessment of the MDA Liberia-China Union Investment states:

> *"The SAP[Social Action Plan] shall include a Resettlement Action Plan ("RAP") component if communities located in or adjacent to such Proposed Production Area or to Mining Plant or Infrastructure not located in the Proposed Production Area should under International Standards be resettled for health or safety reasons."* [emphasis supplied].[23]

There are many agreements that contain clauses of this nature. It may be that the majority of new agreements have some such kind of clause.

The International Bar Association's recently released Model Mine Development Agreement contains a number of "examples" taken from actual agreements.[24] In its main text, or lead clause, it contains, at 3, this definition, which tries to give some greater guidance:

> *"Good Industry Practice" means the exercise of that degree of*

---

[21] *Id.* at p. 33.

[22] Financial or Technical Assistance Agreement—Philippines, Section XIII, 13.1 Obligations of the Contractor, sub point a., pp. 35-38, *available at* http://www.mgb.gov.ph/files/info materials/primerftaa.pdf.

[23] Mineral Development Agreement Between The Government of Liberia, China-Union (Hong Kong) Mining Co., LTD. and China-Union Investment (Liberia) Bong Mines CO., LTD., 5.4 Social Impact Assessment and Social Action Plan, p. 23, *available at* http://www.mmdaproject.org/presentations/MMDA Liberia-China Union Investment-1.pdf.

[24] "The Feasibility Study shall be prepared on the basis of sound engineering and economic principles in accordance with generally accepted international mining industry practice;" [MMDA 1.0 p. 17] "be according to good international mining industry practice;" [MMDA 1.0 p. 17] "…and in accordance with applicable Law and International Standards." [MMDA 1.0 p. 18]

> *skill, diligence, prudence and foresight which would reasonably and ordinarily be expected to be applied by a skilled and experienced person engaged in the international mining industry and includes but is not limited to the guidance provided, as applicable, by the International Council on Mining and Metals, by the IFC Performance Standards, and by ISO 14001 standards."*[25]

But where, as so often, the clause simply commits the investor to comply with "international best practice" or "international standards," what does this mean?[26] One view is that these are essentially meaningless generalities, inserted into contracts to fool gullible host countries, or serve as window dressing for their even more gullible publics. Another is that they essentially import into the agreement all or most of what is in Table I, to the extent it is applicable to the particular issue in controversy.[27] Certainly, there is reason to give them some effect, under the principle that contracts should be construed so as to give effect to all their terms.

Sometimes there is an attempt at definition of "international standards;" more often there is not. Some of these clauses apply to specific areas (e.g. "international environmental standards") and others appear to apply generally.

What is a reasonable and balanced view of these clauses, and how should they be applied or enforced? Will the thirty year contract renewal of the Oyu Tolgoi project, one of the more valuable mineral properties on the planet,[28] turn on whether

> "The Investor demonstrates that the OT Project has been operated in accordance with industry best practice… ."

How is the investor to make this demonstration? On what basis is the demonstration to be judged adequate? What happens if the company and the government disagree?

---

[25] MMDA 1.0 Model Mine Development Agreement (Apr. 2011), *available at* http://www.mmdaproject.org/?p=1727.

[26] John P. Williams, *International 'Best Practice' in Mining: Who Decides and How—and How Does it Impact Law Development?*, 39 Georgetown Journal of International Law 693 (2008).

[27] If the issue is, for example, water pollution, a best practice standard directed at community development or labor practices would not be relevant.

[28] See Bloomberg, *Ivanhoe Sees Oyu Tolgoi Net Asset Value at $16 Bln* (Correct), August 4, 2010, http://www.bloomberg.com/news/2010-08-04/ivanhoe-mines-values-oyu-tolgoi-project-in-mongolia-at-net-16-08-trillion.html (accessed October 4, 2012).

B. The Agreement is Silent on the Subject

There are contracts that say nothing at all about "best practice" or "international standards."

There are in the author's estimation fewer and fewer of them, but they do exist. One possibility in such cases would be to say that the only guidance on acceptable practices in such cases are either the requirements of national law, or the terms of the agreement.

But many countries, including some of the poorest of the mineral-rich developing countries, have very uneven development of legislation. This is one of the very arguments for using investor contracts in such cases: that permitting and licensing legislation is simply not sufficiently established to allow for the granting of leases or concessions under a uniform statutory scheme.

Does this mean, for example, where environmental legislation is rudimentary, that any environmental practice not explicitly forbidden by an environmental code that explicitly forbids almost nothing is acceptable? And that any attempt by government to restrain environmental damage is therefore subject to attack as a violation of investor rights?

This is a very uncomfortable case to argue. It might be even more uncomfortable when we imagine some of the social impacts on human communities. If for example local law fails to provide for compensation for those who are dispossessed or expropriated by natural resource development, is the company free of any obligation?

Perhaps three points need to be made here. First is that if judges or arbitrators are looking for a standard that provides more protection than the sometimes weak reed of national law, they generally prefer – or should prefer – to refer to an existing standard rather than invent their own. Many of the existing international standards have been developed by very knowledgeable experts. They may have some attributes of balance because they came out of consultative or consensus-driven processes. In short, they may have considerably more legitimacy than an arbitrator or judge-invented standard.

Second, there is considerable reason to want to look to behaviorally measured standards. After all, what better way is there to know what "industry practice" is than to look at what industry is doing. In general, what industry is doing in most cases – at least the big international companies in the Western economies – is approximating the international standards set out in Table I above.

Finally, where the parties' agreement is simply silent on the subject, there is considerable reason in most cases to find that international standards apply *by implication*: that applying them is the standard practice in the industry, and that they are therefore presumed to be applicable absent some clear statement to the contrary.

For one thing, the vast majority of mining lenders in the western economies apply at a minimum the Equator Principles,[29] which incorporate the IFC Performance Standards and other international principles. The great majority of the financial institutions that fund natural resource projects adhere to these principles. It would seem reasonable that the parties would not, absent some explicit agreement to the contrary, intend to agree to deviate from international standards in ways that would make it difficult or impossible to finance the project. Indeed, where one of a country's most important and valuable assets is put at risk by conduct that jeopardizes the possibility of financing its development, the country has been done a positive injury.

An analogy might be the question of quality in the sale of goods. If there is a contract for purchase and sale of goods that says nothing about the quality of the goods delivered, it might be possible to argue that any goods, even of terrible or unusable quality could be delivered, and the seller would not be subject to claims of breach. But this argument would lose in almost all legal systems.

If a seller agreed to sell 500,000 eggs at a given price, and there was no mention of quality in the contract, would the seller be required to take delivery and pay the price if half the eggs were rotten?

All developed legal systems give the buyer a remedy in such cases. Section 2-314 of the Uniform Commercial Code, in near universal application in the U.S., says:

> "*a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.*
>
> *(2) Goods to be merchantable must be at least such as*
>
> *(a) pass without objection in the trade under the contract description; and*
>
> *(b) in the case of fungible goods, are of fair average quality within the description; and*

[29] www.equator-principles.com; "Currently 75 adopting financial institutions (72 EPFIs and 3 Associates) in 32 countries have officially adopted the EPs, covering over 70 percent of international Project Finance debt in emerging markets."

(c) are fit for the ordinary purposes for which such goods are used… ."[30]

Under the Chilean Civil Code, the general rule is that the goods being sold must be fit for their natural or foreseeable use. If the goods are not fit for such use to the extent that, had that circumstance been known by the purchaser, the purchaser would have not entered into the agreement or would have only purchased the goods at a lower price, the purchaser is entitled to rescind the sale or have the price be reduced.[31] This is typical of civil code provisions in civil law countries.

In short, if the law nowhere requires people to pay full price for rotten eggs, just because their contract fails to address this explicitly, where is the legal principle that requires a host state to accept without complaint rotten mining projects: massive water pollution, or uncontrollable social conflict as a result of the uncompensated dislocation of its inhabitants?

C. *The agreement identifies and requires compliance with certain specific standards but is silent as to others*

There are agreements that specifically identify some bodies of international standards, but are silent as to any others. The standards most often mentioned in such clauses appear to be the Performance Standards of the International Finance Corporation,[32] the Equator Principles,[33] (which incorporate the IFC Performance Standards), and the Voluntary Principles on Security and Human Rights.[34] Sometimes individual Performance Standards, such as the Performance Standard on Resettlement, are identified in specific contexts.

Obviously, the obligation written into the contract should be respected. But an interesting question is posed by the fact that many of these bodies of standards are evolving and changing

---

[30] U.C.C. § 2-314. Implied Warranty: Merchantability; Usage of Trade (2004), *available at* http://www.law.cornell.edu/ucc/2/2-314.html.

[31] Chilean Civil Code, §§ 1857-1860

[32] IFC Sustainability Framework, Performance Standards and Guidance Notes, (2012) ed. *available at* www1.ifc.org/wps/wcm/connect/115482804a0255db96fbffd1a5d13d27/PS_English_2012_Full-Document.pdf?MOD=AJPERES.

[33] The Equator Principles, EP Association (Jun. 2006) *available at* http://www.equator-principles.com/resources/equator-principles.pdf.

[34] Voluntary Principles on Security and Human Rights (2000) *available at* http://www.voluntaryprinciples.org/files/voluntary_principles_english.pdf.

over time. Should a 2007 contract be forever evaluated by the 2006 edition[35] of the IFC Performance Standards? Or if a case comes up now, should the new 2012 edition[36] of the performance Standards be applied?

But does this mean that no standards other than the ones explicitly mentioned need be observed in such a contract under the canon of construction *expressio unius est exclusio alterius?*[37]

D. The agreement purports to excuse the investor from complying with some or all of these international standards.

We have not located any contract that expressly disclaims an obligation to comply with international standards generally or across the board. But there are indeed investor contracts in which host governments have agreed to a level of investor conduct that is not consistent with international standards.[38]

For example, there is a contract in one west African country that allows mine tailings to be dumped untreated into a local river. There is a contract in which it is provided that the company need not pay more than a bare minimum of compensation to people it displaces, and the government holds the company harmless from any claims they may make.

There are a number of agreements in which the host state guarantees, often under the rubric of "no local charges," that the company will not have to spend any money on amelioration of local impacts of the project.

One view of this is that the state is a Westphalian sovereign that can do what it wants with its own people, and make whatever bargains it wishes with foreign investors. Another view is that the citizens of the country have internationally recognized human rights, and are not the chattel of the state.

---

[35] IFC Sustainability Framework, Performance Standards and Guidance Notes, (2006) ed. *available at* *http://www1.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/IFC+Sustainability/Sustainability+Framework/Sustainability+Framework+-+2006/Performance+Standards+and+Guidance+Notes/*.

[36] IFC Sustainability Framework, Performance Standards and Guidance Notes, (2012) ed. *available at* www1.ifc.org/wps/wcm/connect/115482804a0255db96fbffd1a5d13d27/PS_English_2012_Full-Document.pdf?MOD=AJPERES.

[37] "To express one is to exclude the others."

[38] Heavy Mittal? A State within a State: The Inequitable Mineral Development Agreement between the Government of Liberia and Mittal Steel Holdings NV, (Global Witness Report 2006), *available at* http://www.globalwitness.org/sites/default/files/pdfs/mittal_steel_en_oct_2006_high_res.pdf.

If agreements may sanction approaches that violate recognized international environmental norms, or that violate the human rights of host country citizens, the question is whether such an agreement is enforceable.

When, whether and to what extent the obligations of such an agreement might be enforceable could be a vexing question.

This brings up another set of issues to which this article will now turn. Since it is evident that investor agreements such as the ones we have been reviewing can have very important impacts on the rights and expectations of third parties such as local people, where and how can these people participate in the system to advocate for their own rights? And this brings the question of transparency to the fore.

Most contracts between mining investors and host governments have traditionally been confidential. The citizens of host countries do not know what is in them, Indeed, the contents may in many cases not even be shared with more than a handful of ministers, and be outside the reach of parliamentarians.[39]

V. Questions for Investment Lawyers

It is extremely important to understand how this growing and strengthening body of rules might interact with investment law.

A. *Transparency.*

Investment agreements in the extractive industries have traditionally been confidential agreements between the investor and the host state.[40] They are on one hand commercial deals between companies and host states.

Yet they are public policy documents that can be of enormous importance because they in some cases dispose of the most valuable assets of the state, which is a matter of natural and legitimate concern to host country citizens. Yet many of these agreements have in the past been treated as secret, with their terms are known only to investing companies and a few government officials.[41]

---

[39] *The Paradox of Plenty: One Day Soon Poor Countries May Actually Benefit from their Natural Resources*, Economist, Dec. 20, 2005, *available at* http://www.economist.com/node/5323394.

[40] Peter Rosenblum and Susan Maples, Contracts Confidential: Ending Secret Deals in the Extractive Industries, (Revenue Watch Institute 2009), *available at* http://www.revenuewatch.org/sites/default/files/RWI-Contracts-Confidential.pdf.

[41] *Id.*

First Quantum, a British Columbia based mining and metals company was, formerly, one of the biggest foreign investors in the Democratic Republic of Congo. In a Memorandum of Understanding between SODIMICO and First Quantum Minerals Limited and BIMZI from January 2000, the parties agreed that the memorandum was confidential and could not be communicated to any third party without written consent of the other partner and SODIMICO.[42] The new DRC government has described First Quantum's conduct as consisting of unreasonable behavior, misadventure and unspecified misconduct by company executives.[43]

Accepted international standards are increasingly demanding transparency not only of the revenue flows that are produced by such agreements, but of the terms of agreements themselves. To what extent will this influence investment law? Will we start to see limits on the willingness of investment law to enforce agreements that are not in the public domain?

Corruption is greatly facilitated by secrecy. Investment law now clearly will not enforce agreements reached through corruption.[44] Will decisions move in the direction of limitations on enforcement of contracts that are not in the public domain? Will there be some new burden-shifting rules in this area?

While we can speculate on this, the fact is that there appears to be no reason that secret contracts cannot be enforced in secret proceedings, even where the results are of immense importance to the state and its citizens.[45]

If the agreement has dramatic effects on the rights of people who are not consulted in its negotiation, the agreement is at least in the worst cases confidential, and it is enforced by arbitration in which the affected parties are not allowed to participate, and which in the worst cases is in itself confidential, the idea of justice is going to emerge severely dented.

B. *Rights of Third Parties.*

Many of the emerging standards have to do with the effects of extractive industry development on third parties, such as people who are forcibly displaced to make way for projects, people whose traditional use of subsistence resources is undermined, and the "right to development"

[42] "SOCIETE DE DEVELOPPEMENT INDUSTRIEL ET MINIER DU CONGO (SODIMICO) ET BIMZI LIMITED & FIRST QUANTUM MINERALS LIMITED MEMORANDUM D'ENTENTE MUTUELLE" [Memorandum of Understanding between SODIMICO and BIMZI LIMITED & FIRST QUANTUM MINERALS LIMITED], (Jan., 2000), *available at* mines-rdc.cd/fr/documents/avant/SODIMICO_BIMZI_FQM.pdf.

[43] Tim Webb, *Mining Companies Clash Over Congo Copper Mine*, The Guardian, Sept. 6, 2010, *available at* http://www.guardian.co.uk/business/2010/sep/06/congo-copper-mine-first-quantum-enrc.

[44] Ayesha de Kretser, *Miners Reject Anti-Corruption Reforms*, Financial Review, Mar. 1, 2012, *available at* http://afr.com/p/business/companies/miners_reject_anti_corruption_reforms_NeBuguzm9PBMNjpsVvBPmK.

[45] Jeffrey W. Sarles, Solving The Arbitral Confidentiality Conundrum In International Arbitration 5 n.26 (2005), available at www.appellate.net/articles/Confidentiality.pdf.

of affected communities. Many investment agreements in one way or another bargain away these rights of third parties, *e.g*. by limiting compensation to the displaced, limiting the application of environmental standards, or limiting rights to be consulted.

To what extent will investment law recognize the emerging international framework as a limit on what the state and the investor may agree to, where third parties are affected?

C. Emerging Standards as a Floor.

Will investment law recognize the emerging international body of standards as a "floor" on investor (and perhaps government) behavior in areas such as human rights, environmental protection, and due process? How? Might we move in a direction where these standards are regarded as a lower limit on stabilization, where stabilization, e.g. of national laws on environmental protection could not force implementation of environmental requirements less stringent than international standards?

D. Emerging Standards as a Ceiling.

Are there situations in which emerging international standards might serve as a ceiling? Might we move in a direction where these standards are regarded as an upper limit on stabilization, where stabilization, e.g. of national laws on environmental protection could not require environmental performance higher than international standards?

E. *Stare Decisis*

A common criticism of the system of investor arbitration is that it creates unpredictable results.[46] This is sometimes said to flow from the fact that the principle of *stare decisis* is not observed in arbitration, and every arbitrator is thus free to decide each case as he or she sees fit.

Perhaps adherence to emerging international standards in resource development is a way to bring more predictability to outcomes.

VI. Conclusion

Markets need rules if they are to avoid producing bad results. These results can be bad for a poor country that is inexperienced at negotiating and at the same time bad be for rich multinational investors.

[46] Gabriel Egli, *Don't Get Bit: Addressing ICSID's Inconsistent Application of Most-Favored Nation Clauses To Dispute Resolution Provisions,* 34 Pepp. L. Rev. 1045 (2007).

International standards such as the Equator Principles and the IFC Performance Standards serve to protect the environmental, social, and cultural values of residents of the host state; they also serve to help companies manage investment risk. This emerging framework for sustainable development of natural resources is fast becoming a tool that neither side to a negotiation can afford to ignore.