Supporting Inclusive Resource Development (SIRD)
East Africa
RESOURCE REVENUE MANAGEMENT AND ALLOCATION

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COURSE CONTENT

What is the legal framework for sharing of extractive revenues in Kenya?

What is the revenue allocation for host communities?

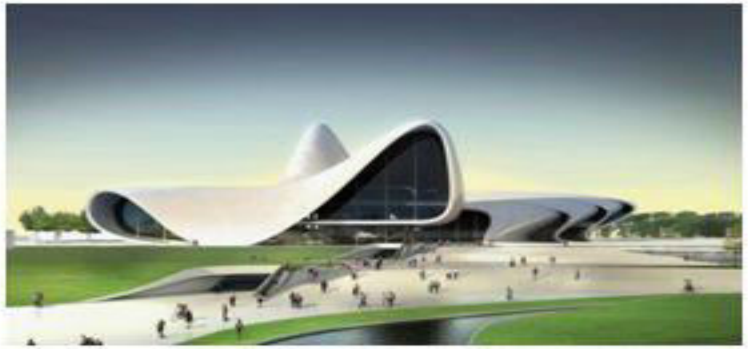
Which agencies monitor revenue allocation and expenditure?

Who is responsible for management of community revenue?

Stories

Chile

Azerbaijan



Natural Resource Governance Institute

Oil, gas and mining for development

Essential Questions

1. What are the main challenges in managing non-renewable resource revenues?
2. How *should governments manage* resource revenues?
3. How *do governments manage resource* revenues?

Legal framework for sharing of extractive revenues in Kenya

Benefit Sharing, what is it?

Distribution of monetary & non-monetary benefits of mining. Objective is to ensure significant portions of benefit is retained in the mining area for the benefit of the mining host communities.

Benefit sharing can take the following forms:

- Fair & equitable compensation for loss of land & other production resources;
- Mitigation to minimize harmful social, economic and environmental impact of mining;
- Development of socio-economic infrastructure (roads, hospitals, schools, water points);
- Training & employment in an affirmative employment quota;
- Local procurement of goods and services & growth of alternative businesses;
- Payment of taxes and royalties by a mining company

The Constitution of Kenya 2010 and benefit sharing in the extractive industry

- Arts. 62(1)(f) & 62(3) – minerals vests in National Govt. to be held in trust for the Kenyan people (a trustee, not an exclusive owner). Strict use of minerals for the benefit of beneficiaries.

- Arts. 40, 63 & 64 – right to property & land (private & community land). Landowners must give FPIC to mining on the basis of full knowledge of the benefits & burdens. Fair & adequate compensation for land & other production resources.

- Arts. 69(1)(a) & (h) – requires sustainable exploitation of mineral resources for the benefit of the people of Kenya. NG to ensure equitable sharing of benefits of mining.

- Arts. 69(1)(d), 72 & 118– public participation & popular oversight in the granting of mining concessions (people generally & parliament).

- Art. 10 & Cap 6 - good governance values of integrity, transparency & accountability. Public Office is a public trust to be exercised for the benefit of the people of Kenya. Weed out corruption & self-interest that leads to skewed mining contracts. Personal accountability for exploitative concessions.

Mining Act, 2016

- s6(1) – Minerals vest in NG as trustee for Kenyan people. Needs & interests of beneficiaries paramount in mining concession contracts (equitable benefit sharing an interest).

- s12(2) – Role of CS in managing the mining sector in line with Art. 69(1)(a)(h) of Const. (managed for benefit of Kenyans).

- Ss34, 37, 38 – entrenches FPIC by requiring CS to give notice to landowners & lawful occupiers to enable their participation b4 a licence is issued & give consent. Individuals & communities can object to the issuance of a mining licence – s43(4)&(5).

- S55 – Cabinet & Parliamentary oversight (CS to submit report detailing concessions granted & justifications for grant).

- 153(1) – Compensation if mining disturb or deprive the use of land; cause loss or damage to immovable property; deprive people of water supply; cause loss of earnings in relation to agriculture.

Mining Act, 2016

- ss46(1), 47(1), 101(2), 103(e), 106(h) – Mining operator to develop a plan on recruitment, training & employment of locals that ensures skills transfer & capacity building. He must give employment priority to mining host communities.

- ss101(2)(h), 103(d), 106(f) – local procurement of goods & services.

- ss101(2), 103(g) – a socially responsible community development plan. S109(1) requires operator to sign CDA with mining host communities to ensure socio-economic dev.

- ss117 & 118 – CS in consultation with Treasury to enter into mineral rights agreements with large-scale miners for payment of taxes & royalties; environmental obligations, domestic processing of minerals & community development (must be ratified by Parliament before execution).

- s183(5) – royalties to be distributed at ratio of 70/20/10. to NG, CG and mining host communities respectively. Too much discretion on CS to determine royalties; no legal framework for transmission of royalties to CG & mining host communities.

Community Development Agreement (Regulations)

A Community Development Agreement (CDA) is an agreement signed between the mining host community and the holder of a mining license or special mining lease to ensure that the community benefits from mining proceeds.

The investor shall set aside a minimum of one per cent (1%) of the gross revenue from the sale of minerals every calendar year to be used to implement the CDA.

The CDA shall be in force for the life of the mine and may be reviewed by both parties at least five (5) years from the date of signing of the agreement.

The investor shall draft the CDA in accordance with the regulations.

The Local Content Bill 2016

- Based on Arts. 69 of Const. – sustainable management of mineral resources & equitable benefit sharing; & 66(2) – natural resource investments to benefit local communities & their economy.

- Objective: maximisation of value addition; creation of employment; procurement of local goods & services; participation of Kenyans in the extractive sector value chain.

- Establishes a Local Content Development Committee to ensure general participation of Kenyans in the mining value chain (clauses 7-18).

- Empowers CS & Committee to set local content requirement for each mining operator (clause 19) & ensure its implementation.

- Requires each mining operator to submit local content plan & employment & skill development plan for approval before licence is granted. Operator must then submit quarterly reports on implementation (clauses 20-24).

The Natural Resources (Benefit Sharing) Bill 2014

The Bill aims to create a Natural Resources Benefit Sharing Authority with the responsibility to manage benefit-sharing agreements between mining companies and local communities, determine payable royalties as well as manage royalties from all natural resources exploitation in Kenya.

It envisages the establishment of a Natural Resource Royalties Fund to be managed by the Authority, where all royalties and fees relating to natural resources are to be deposited.

Further, the Bill creates a different formula for the sharing of royalties. It envisages 20% of the royalty revenue to be deposited in a sovereign wealth fund to serve future generations; while the remaining 80% to be shared between the National Government and the County Governments in the ratio of 60:40.

Of the 40% to the Counties, 60% is to be used for the general development of the relevant county, while 40% is to be strictly utilised for local community projects.

As drafted, the Natural Resource (Benefit Sharing) Bill 2014 is bound to generate conflict as its provisions conflict with the provisions of the Mining Act. This is in relation to the functions of the Authority vis-à-vis the Cabinet Secretary for Mining and the other institutions created under the Mining Act, as well as in relation to the formula for mining royalty sharing. As a result, it is unlikely that the Bill will be enacted into law as drafted.

Petroleum Act

The petroleum law provides a framework for contracting, exploring, developing and producing the commodity.

Create a national policy for operations and as a reference point in the establishment of petroleum institutions.

Under the new law, the national government, county governments and communities will receive a fair share of the revenue from petroleum operations.

Counties will receive 20 percent of the national government's share- BUT amount allocated shall not exceed amount allocated to the CG by parliament in FY under consideration

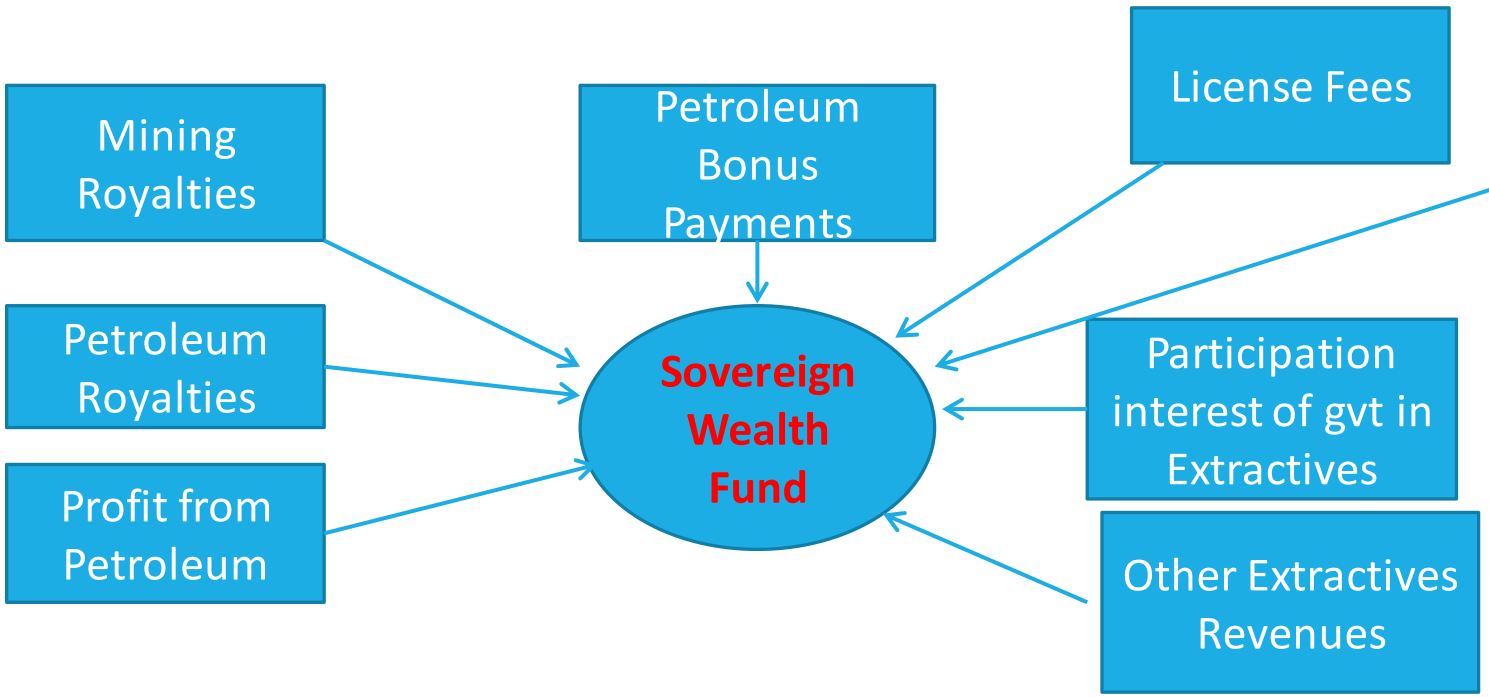
Communities will get five percent of the Government's share payable to a Trust Fund managed by a Board of Trustee established by CG in consultation with the community

Parliament is tasked with reviewing the percentages within 10 years, while considering any necessary adjustments.

Sovereign Wealth Fund Bill

A bill to establish the Kenya Sovereign Wealth Fund, to provide institutional arrangements for effective administration and efficient management of minerals and petroleum revenues.

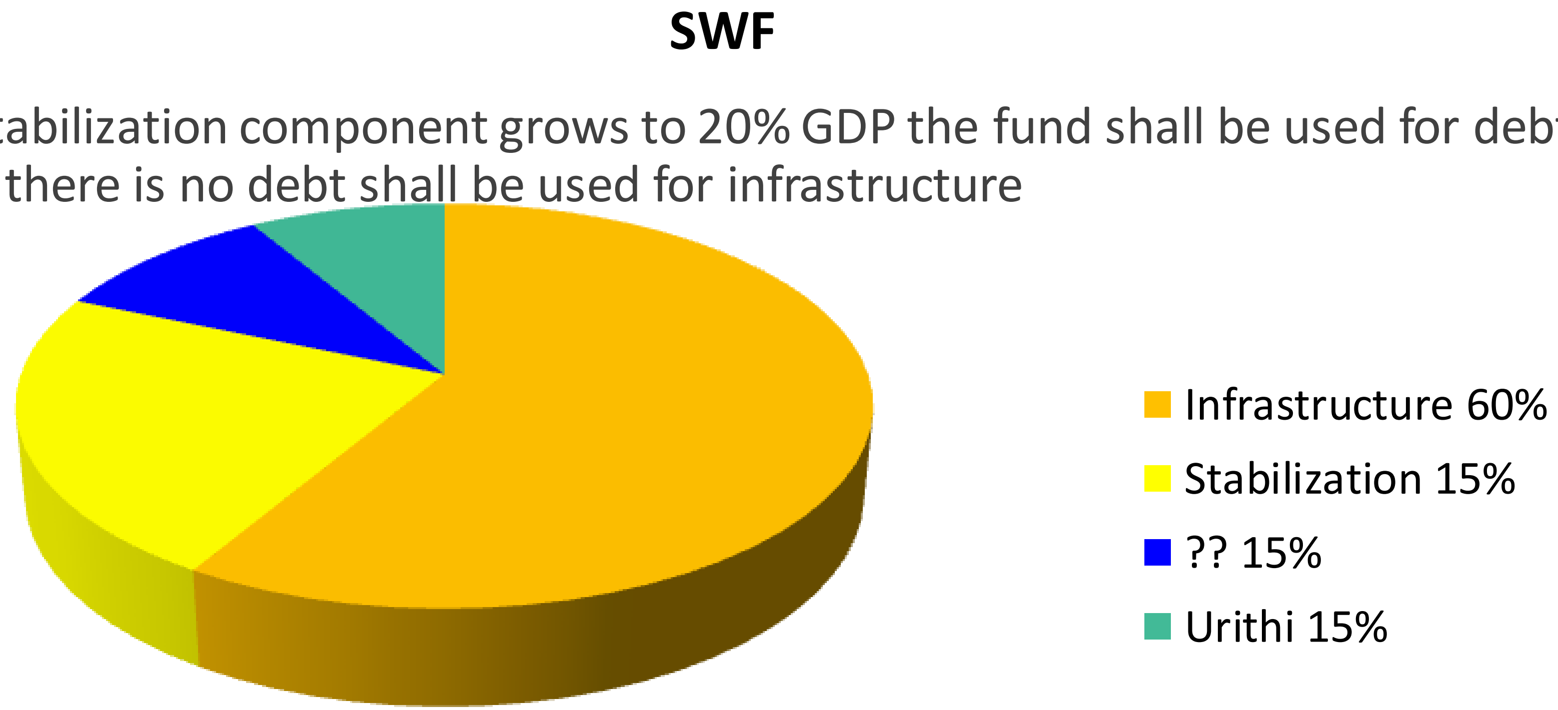
Sources of the **Sovereign Wealth Fund s.6**:



Components of the Sovereign Wealth Fund

S.8

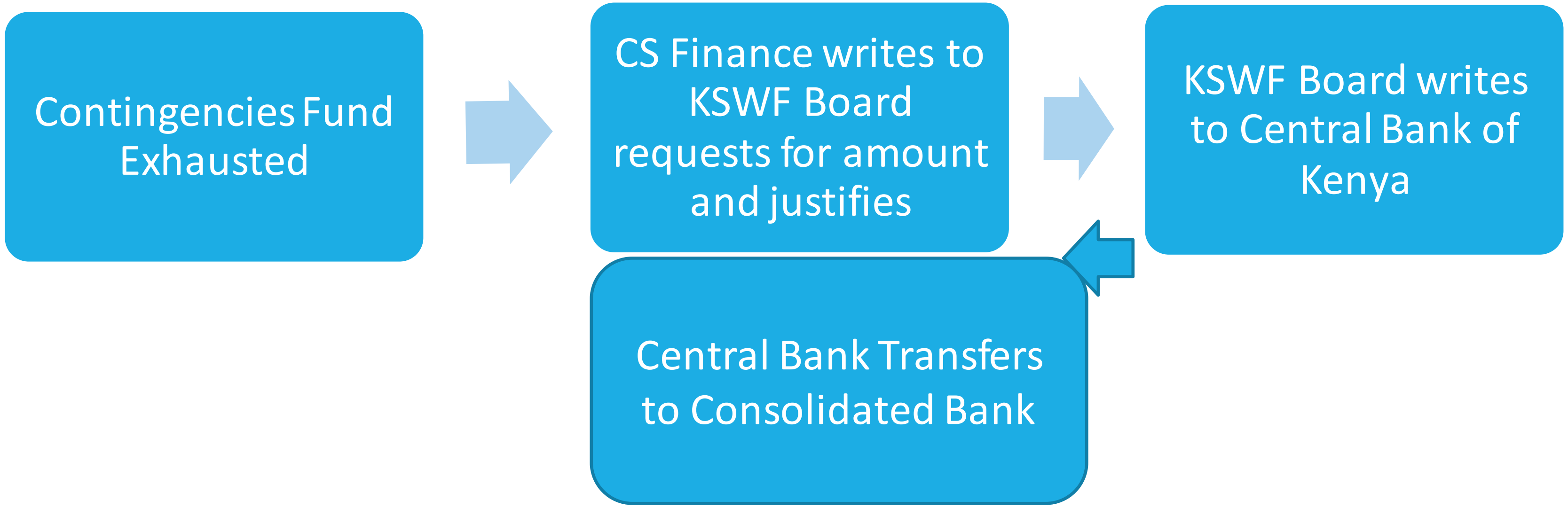
NB: Once the stabilization component grows to 20% GDP the fund shall be used for debt servicing and if there is no debt shall be used for infrastructure



Withdrawal of the Funds

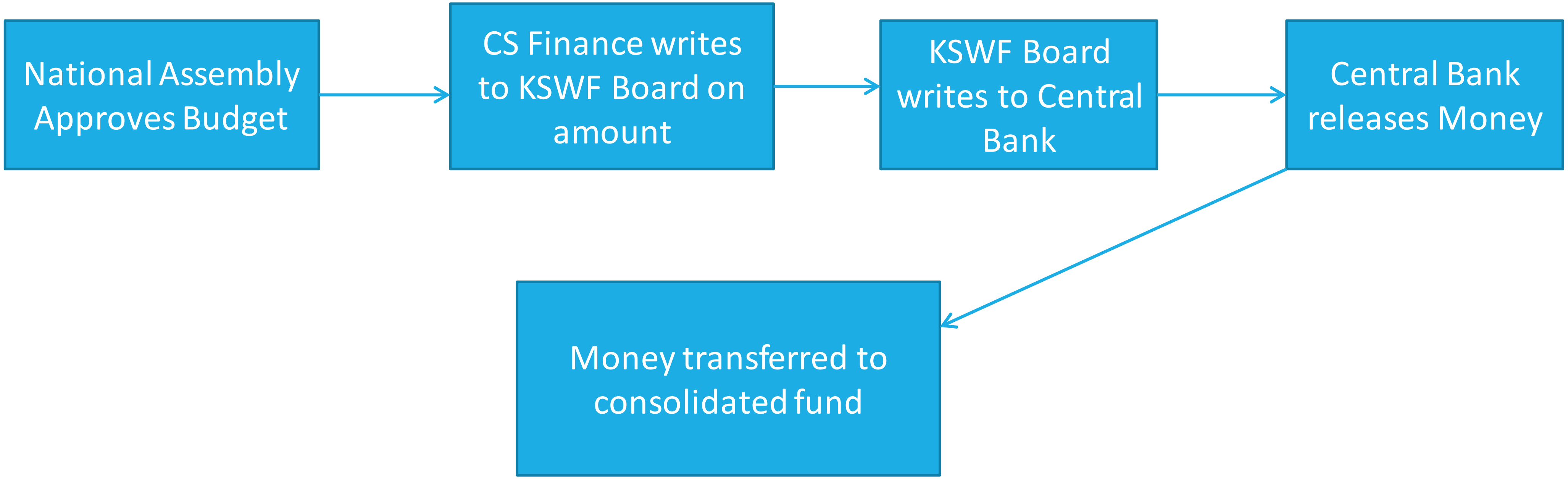
Stabilization Fund

Component insulates expenditure in national budget from fluctuations of resource revenues and manage other macro economic shocks. NB: Parliament approves limit of withdrawal and purpose of funds only limited to investments and macro economic stabilization.



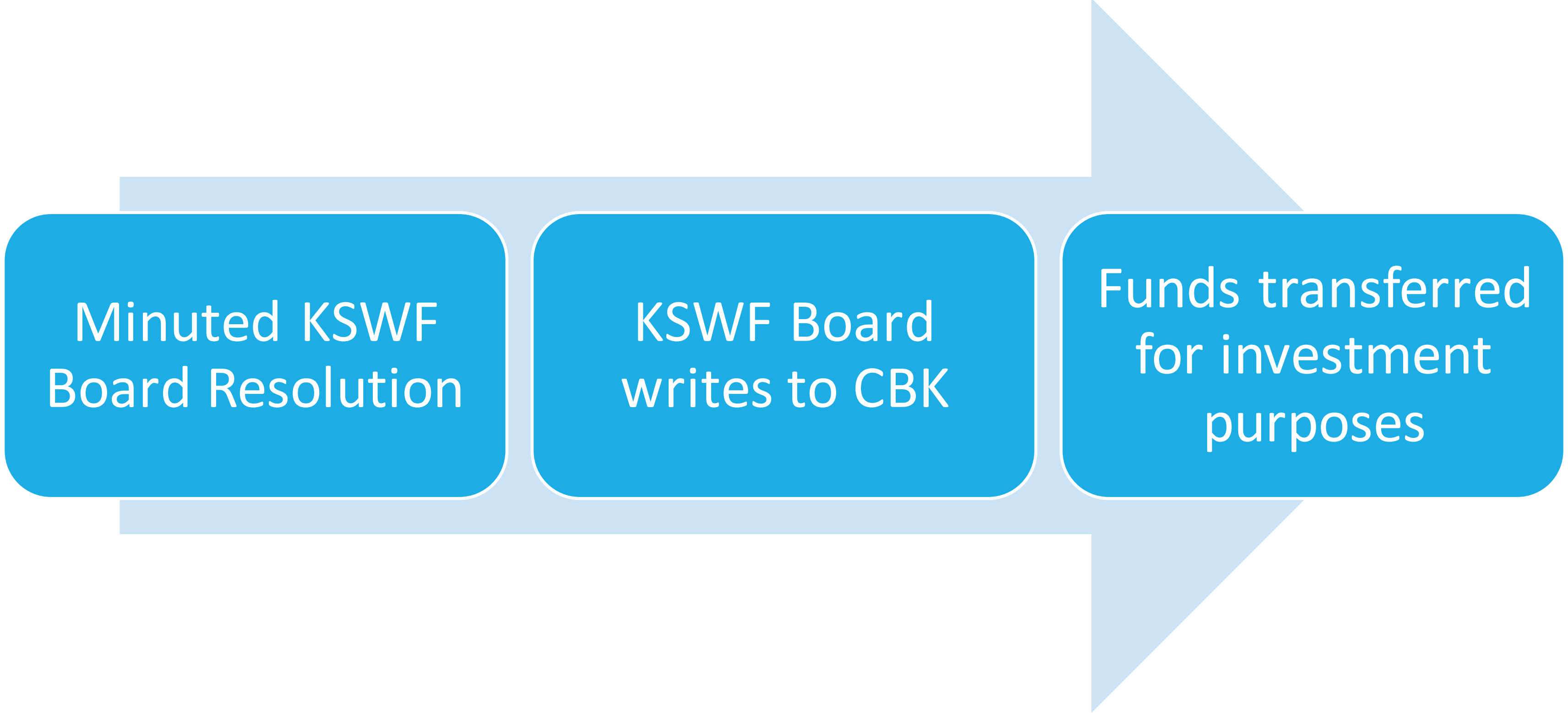
Withdrawal of Infrastructure Development Funds

Purpose is to fund public sector infrastructure development priorities in Agriculture, Transport, Housing, Energy, Water, Education and Health Sector S.12



Urithi Fund

Provides an endowment for future generations distributes wealth across generations to generate alternative streams of income when mineral and petroleum reserves are depleted S.15



Gaps in SWF Bill

1. Inadequate independence and oversight: The draft concentrates significant powers over fund management in the hands of the executive. All board members are either directly or indirectly nominated by the office of the president, as is the sole oversight actor, the auditor-general.

2. Borrowing while saving: In its latest Eurobond issue, the Kenyan government was charged **7.25-8.25 percent annual interest** on its sovereign debt. Until interest rates for Kenyan sovereign debt decline, intergenerational equity objectives would be best served by debt reduction rather than financial savings.

3. Domestic investment outside the budget process: The draft proposes the establishment of an “Infrastructure Development Component” that would absorb 60 percent of resource revenues. The domestic investment mandate raises a number of risks, specifically that home financial investment through a sovereign wealth funds could: (1) undermine the public financial management system, creating a less accountable parallel budget with its own appraisal, procurement and monitoring systems; (2) undermine public accountability by bypassing legislative oversight; and (3) lead to poor investment decisions, because financial managers specializing in maximizing financial returns are usually not trained in identifying or managing assets with a social objective in mind.

Gaps in SWF Bill

4. Failing to achieve the goals of the fund: While the draft proposal provides a list of priorities in determining how to spend oil revenues domestically, the fund can only help achieve fiscal stabilization and sustainable spending objectives if combined with fiscal rules that constrain overall government spending.

The Ghanaian experience is pertinent to the Kenyan context. Ghana established sovereign wealth funds in 2011, directing approximately 70 percent of oil revenues toward domestic capital spending and the remaining 30 percent into savings and stabilization. While these allocation rules were generally observed in subsequent years, the overall trends in public finances did not reflect the intent of the law. Spending on recurrent expenditures grew most rapidly as a result of large wage increases.

Kenya faces an infrastructure and education financing deficit which can be partly addressed by channeling resource revenues to domestic investment. But a risky fund might leave Kenya worse off than no fund at all.

History of SWFs

Texas Permanent University Fund

(1876)

• Kuwait Investment Authority (1953)

• Kiribati Revenue Equalization

Reserve Fund (1956) – British

protectorate

• Term coined in 2005

• Approximately 40 new funds since

2000

Examples of Misappropriation of SWF

Libya-70 Billion USD (biggest in Africa)

In 2016 it lost $1.2Bn in shady deals

Angola-$5 Billion USD

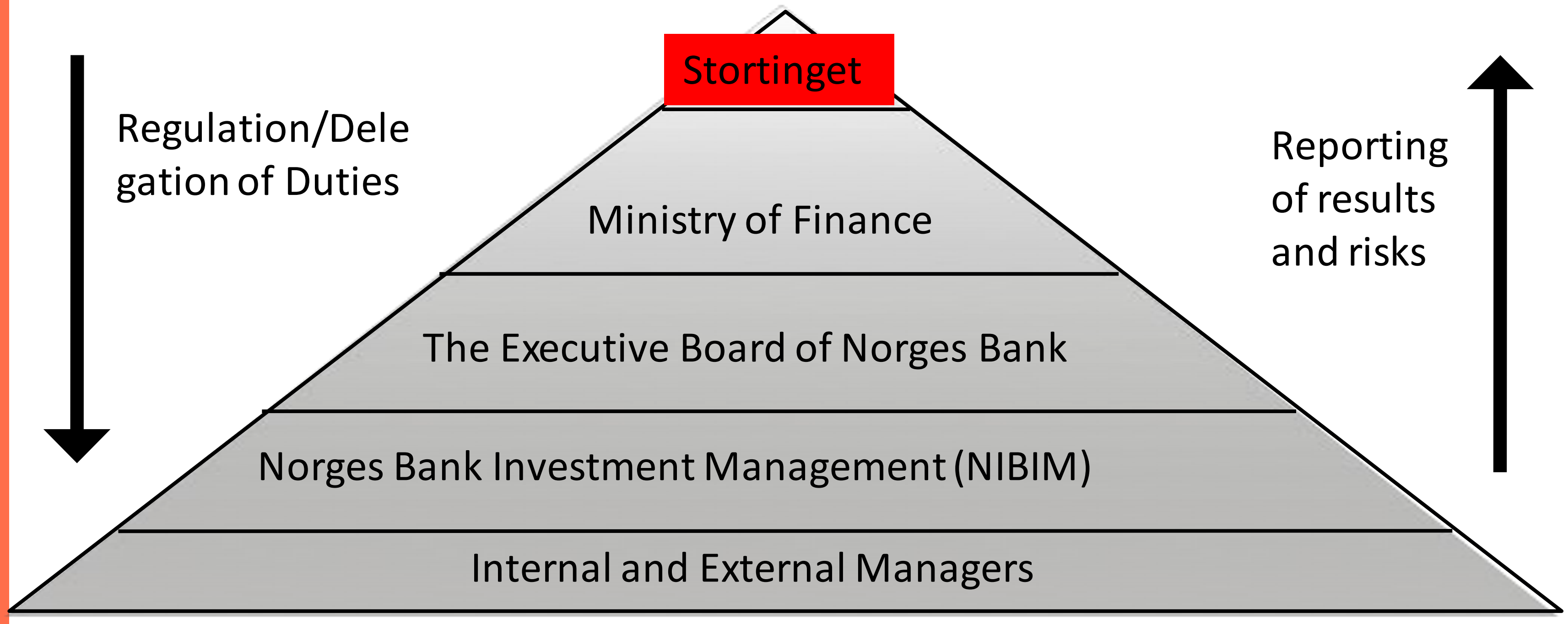
March 2018- $500mn siphoned out by

Jose dos Santos-Fmr. President’s son

Good Governance of SWF

1. Set clear fund objectives
2. Establish fiscal rules
3. Establish investment rules
4. Clarify good institutional structure
5. Require extensive disclosure and audit
6. Establish strong independent oversight

Norwegian Model- Institutional Structure



Some Local Realities: Case of Kwale County- Nguluku and Bwiti Villages

Titanium mining benefit sharing in practice

Despite the law and efforts, the reality in Nguluku and Bwiti is that titanium mining has not generated shared prosperity.

Community involvement in decision-making: FPIC was lacking in the concession granting process (people weren't given sufficient time, information & assistance to make informed decisions based on socio-economic & environmental risks as well as the expected benefits & burdens of titanium mining).

Community participation not substantive & determinative in choice of community projects & their implementation (70.6% of Bwiti & 87.5% of Nguluku not involved).

As a result of non-involvement, these communities feel that the development projects haven't met their needs and priorities.

Lack of participation has created a negative perception of BT, with the majority unsupportive of the mining operations – a lack of social license to operate.

Payment of taxes & royalties

- Taxes to National Govt. – unfair to CG (Mining should be a shared function to enable CG also levy some taxes for the development of the County – mining revenue decentralisation as CG better understands local needs & priorities).

- On royalties, impact depends on % - CS with almost unfettered discretion to determine % (s183(5)). This can be abused to the detriment of mining communities (need for reforms). BT pays 2.5% (supposed to double to 5% if government agrees to a deal proposed by them) – Mongolia & Ghana, 5%; SA, 7%, Chile, 14%.

- Royalty distribution – 70/20/10 (affected communities not involved in determining these %). Majority HH interviewed felt that local community should be entitled to 30-35% of royalties, as they suffer the direct adverse consequences of mining. Need for law reforms.

Royalties – who are local community in context of 10%

- Mining Act, s2 – group of people living around a mining operation area; group of people displaced from a mining operation area.

- Four conceptions of community based on sectarian interests:

- Those displaced from Maumba;

- Those currently living around the operation area (Nguluku);

- Original inhabitants of Bwiti who hosted Maumba people;

- The entire population of Kwale County – all affected in one way or another.

- Developing consensus – local community in the context of mining in Maumba should only include the 1st 3 groups, in line with the Mining Act.

Impact of benefit sharing, or lack of it, in Nguluku & Bwiti

- Kwale has high levels of poverty, with 74.9% of the population living below the poverty line (C-BROP 2015).
- Reasons: insecure land tenure; lack of economic opportunities; high levels of dependency (approx. 57% of population below 15yrs); semi-skilled nature of labour limiting productivity etc.
- High expectations: Discovery & mining of titanium was bound to generate hopes of shared prosperity & socio-economic development.
- BT's good intentions: 7.6 billion to GDP; employ 950, with 94% local staff; royalties of 601m annually (11.7b in 10yrs); grow local economy through procurement; community development through CDMP, with 301.3m in 2016 (2.6b in 10yrs); & scholarships.
- Reality: Titanium mining has not markedly improved the lives of the mining host communities in Bwiti and Nguluku, with the result that poverty and destitution persist.

Adverse social impacts of mining

- Led to relocation, breaking up community social structures & support systems:

- Distance to schools, shops, markets;

- Forest leading to human-animal conflict affecting agric. Production – farms less productive;

- Dam has brought about vectors like mosquitoes & crocodiles;

- Noise & dust that have caused ailments (skin, eye, respiratory);

- Access to river water & water quality (contamination)

- BT has put in place mitigation measures, question has been their adequacy.

- Need for collective work in addressing these concerns provided by Mining Act 2016 – development of an inclusive environment management plan (sections 101(2)(i), 103(c), 106(i), 109(c), 115(c) and 176).

Telegraphic Address: "LANDCON"
Telephone: Nairobi 718050
When replying please quote

Ref. No. DS/C/0078B/1072

LAND ADJUDICATION AND
SETTLEMENT DEPARTMENT
P.O. Box 30297
NAIROBI

Date: 31st OCTOBER 2007

NGEJA MWANZUMA
C/o District Land Adjudication & Sett. Officer,
P.O. Box 17,
KWALE.

Dear Sir/Madam,

SETTLEMENT PLOT – LETTER OF OFFER

I am pleased to inform you that arrangements to relocate you from **Maumba/Nguluku** have been completed.

The Government, through the Settlement Fund Trustees of Post Office Box number 30449, Nairobi, a body corporate established under Section 167 of the Agriculture Act **(Cap.318)** hereby offers you an **Agricultural** plot **No 1072** of approximately **5.5 acres** at **MRIMA BWITI PHASE II** Settlement Scheme in **Kwale District** at a cost of **KShs. 2,500/-** per acre or **Kshs. 13,750/-** per plot.

This land is offered over and above the full compensation paid by Tiomin Resources Inc. for your land at the Titanium Mining Project area. Full payment is to be effected within 90 days of the date here-of to the Settlement Fund Trustees to facilitate issuance of a title deed.

Yours faithfully,

B. O. AKUNGO
DIRECTOR OF LAND ADJUDICATION AND SETTLEMENT

C.C. **The Permanent Secretary,**
Ministry of Lands
P.O. Box 30450,
NAIROBI.

District Commissioner,
Kwale District,
P.O. Box 1,
Kwale

District Land Adjudication
& Settlement Officer,
P.O. Box 17,

Employment opportunities

- Mining is capital intensive & technologically advanced, not creating so many employment opportunities.
- 50% of its workforce is from Kwale County and 97% is Kenyan, It intends to employ 642 workers, 94% (602 employees) of them being Kenyan nationals, who will earn an average annual wage of 927, 400 that is 40% higher than the national average.
- Mining operators do have an obligation to prioritise local recruitment & training – 100% of those interviewed said local personnel are the minority at BT (in-migration into Kwale, limiting opportunities for locals).
- Has in-migration benefited Nguluku & Bwiti in relation to multiplier effects of mining? In-migrants don't live in Nguluku & Bwiti, but in Ukunda & Msambweni – no rentals, food items & other supportive services for indirect employment.
- No major derivative economy in the supply chain to create jobs – no much value addition.
- Draft Mining (Employment & Training) Regulation 2017 – requires operators to develop a detailed employment, training & succession plan that ensures local communities are trained & employed in mining operations.

Local Content

- Reality – mining requires goods & services of high technical stds – local capacity to provide these may be limited.
- Result – local procurement process dominated by local elite & political class – entrenching inequality & creating resentment.
- Local Content Bill – Operator to maintain fair tendering process that allows local communities to benefit, with priority given to local providers.
- Community Development Trust Fund (proposed) – can develop local capacity to provide goods & services through training, capacity building & financing.

Socio-economic development projects

- Previously a CSR activity, but now a legal requirement under Mining Act (s109) – community development agreements.
- Requires tripartite inclusive engagement & participation, with community participation being determinative to ensure projects respond to local needs & priorities.
- Though BT has a CDMP, majority (70.6% in Bwiti & 87.5% in Nguluku) state that they were not involved in its development & that it doesn't reflect their needs & aspirations.
- **Solution**: Mining Act & Draft Mining (Community Development Agreement) Regulation 2017 – CDA is a binding legal document that ensures mining activities are beneficial to local communities.

Multi-dimensional poverty indicators

Food access
18.2% - 3 meals; 68.2% – 2 meals; 13.6% - 1 meal.
95.5% reported going to bed hungry sometime.
5.9% - 3 meals; 84.2% - 2 meals; 11.8% - 1 meal.
100% reported going to bed hungry sometime.

Health

8-15km distance to health facilities (Msambweni, Shimba Hills, Mivumoni). Little improvement in healthcare infrastructure despite adverse health impact of mining.
Dispensary in Bwiti - poorly equipped (few qualified personnel & medication – one nurse & 2 community health workers)

Water
Poor water infrastructure. 63.6% - open wells; 22.7% - tanks by BT; 13.6% - rivers. Waterborne diseases reported due to river contamination.
82.4% access borehole done by BT. Less challenges with water.

Multi-dimensional poverty indicators

Education

3-6km distance to schools – D Ndegwa & Mwadogo. Deteriorating performance due to distance, threats of wild animals, poor infrastructure & learning environment, high teacher-student ratio. Dropouts due to poverty & early pregnancies.

Education infrastructure comparatively better. 2 nearby schools, BPS (82.4%) & MPS (17.6%). Better school performances in exams. School dropouts due to poverty & early pregnancies.

Housing & Sanitation

81.8% - mud & makuti (T); 13.6% - mud & mabati (SP); 4.5% cement & mabati (P).
Only 13.6% with title deeds; 86.4% have no title deeds.
All have access to pit latrines.
64.7% - mud & makuti (T); 17.6% - mud & mabati (SP); 5.9% - cement & mabati (P).
53% with title deeds; 35.2% without TD & 11.8% renting.
All have access to pit latrines.


THIS BUILDING OF
BWITI SOCIAL HALL
WAS FUNDED BY
BASE
TITANIUM LTD


BWITI COMMUNITY BOREHOLE
FUNDED BY
BASE
TITANIUM LTD


PRIMARY SCHOOL
MISSION
VISION

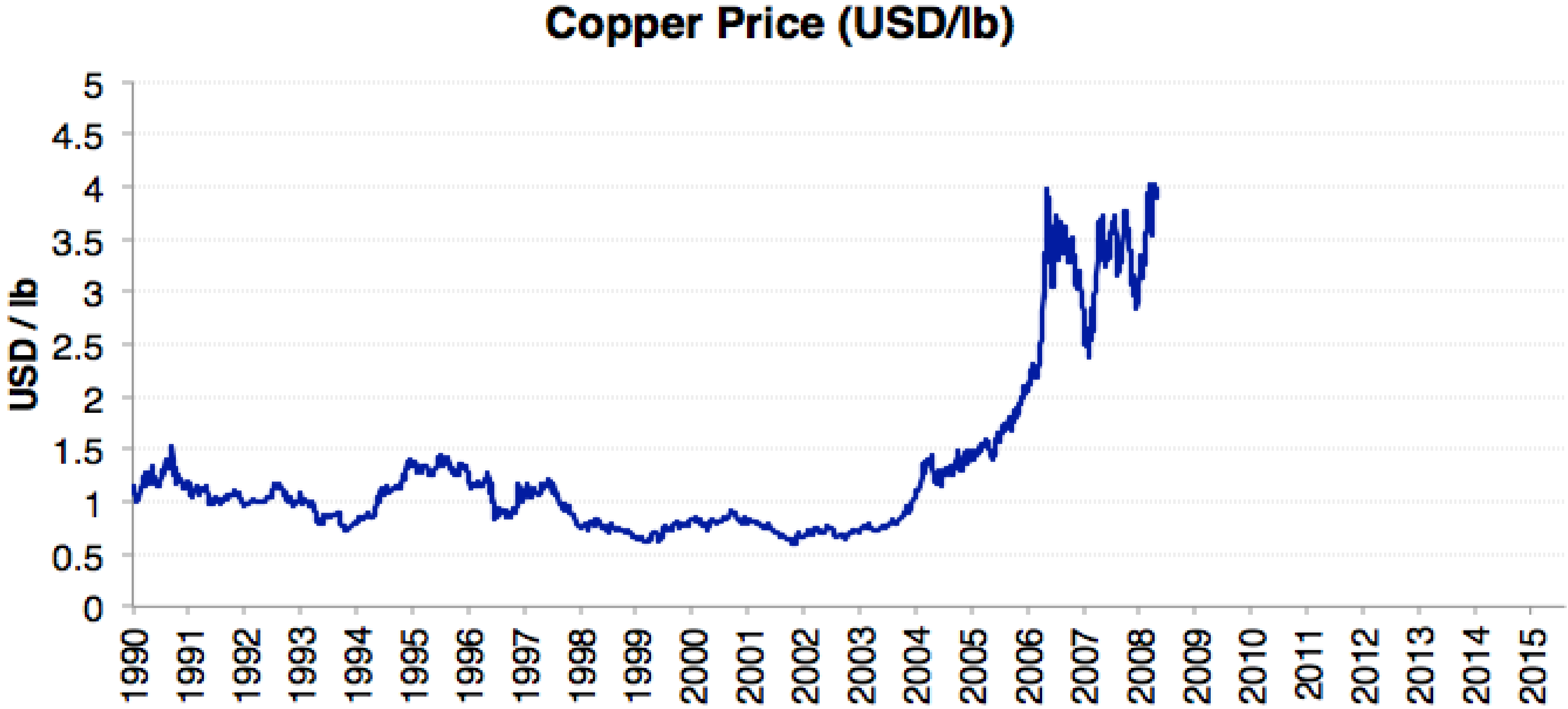
SOME OF THE HOUSES IN BWITI

Characteristics of Resource Revenues- why we should manage the same sustainably..

Volatility

Dutch Disease and Absorptive Capacity

Copper revenue volatility: Case of Chile



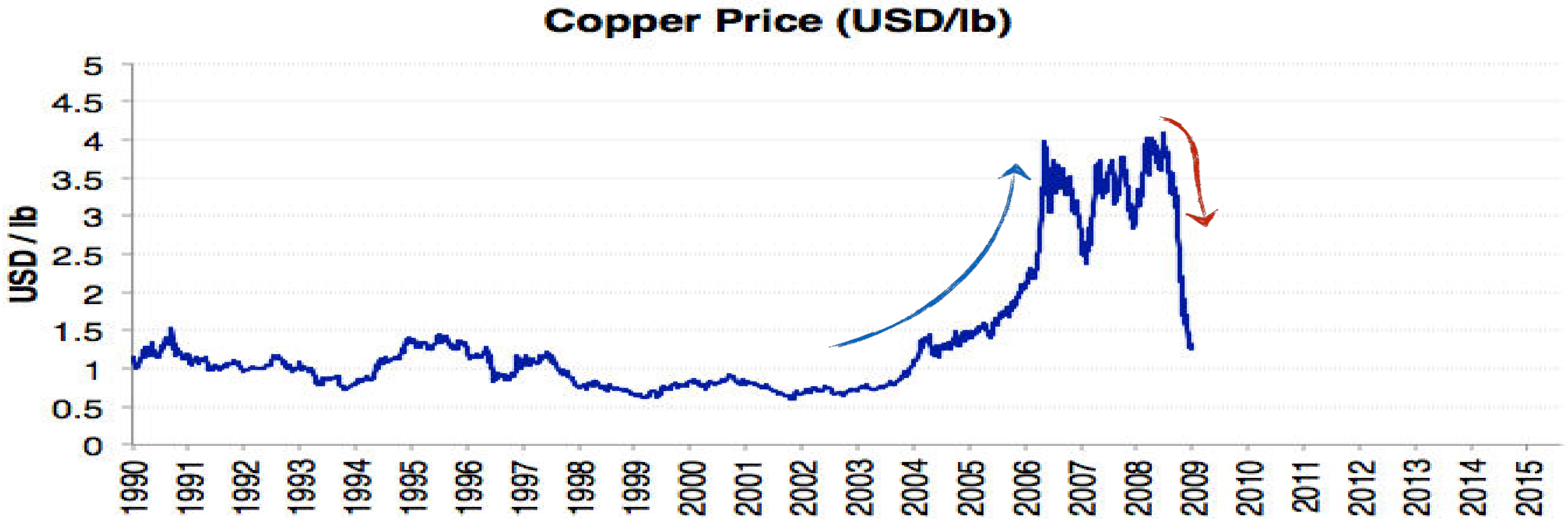
Questions

How would you have planned government spending in 2012?

What fiscal policies should government put in place today to manage spending in future years?

Copper Revenue Volatility

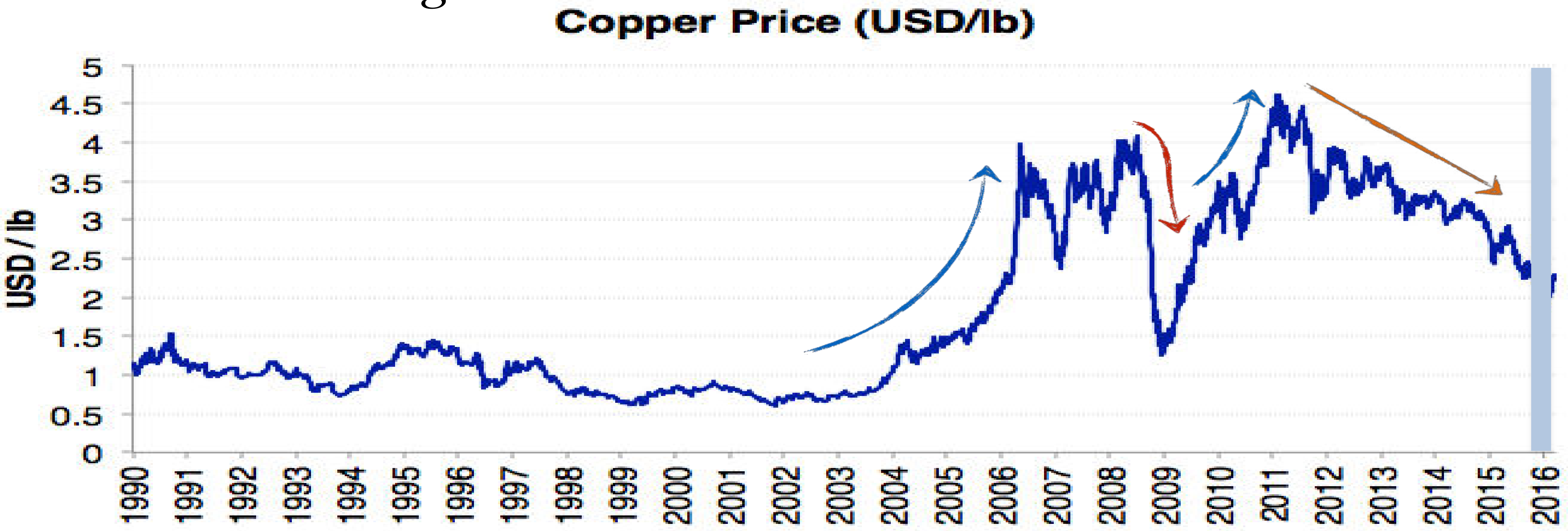
Copper revenue volatility



Copper Revenue Volatility

Copper revenue volatility

3) The 2009 rebound took the price to higher highs, but the trend didn't last for long.



Choices for managing a shortfall

Cut spending

- Increase taxes
- Borrow (foreign or domestic?)
- Ask for IFI or bilateral aid
- Draw down on government savings

Consequences of volatility (resource revenues increasing)

14 lane road in Myanmar

VS

Investing in education in Chile

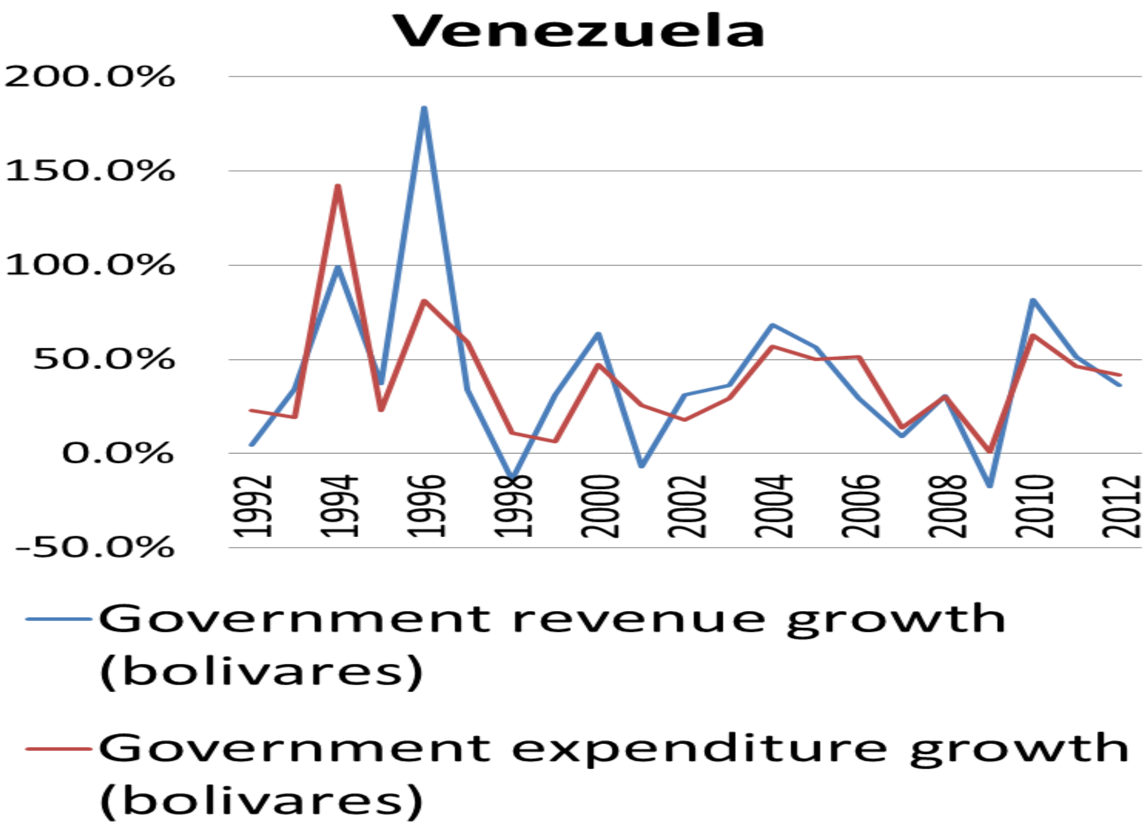
Consequences of volatility (resource revenues decreasing)

Protests in Venezuela

Calm in Chile education investments

Volatility

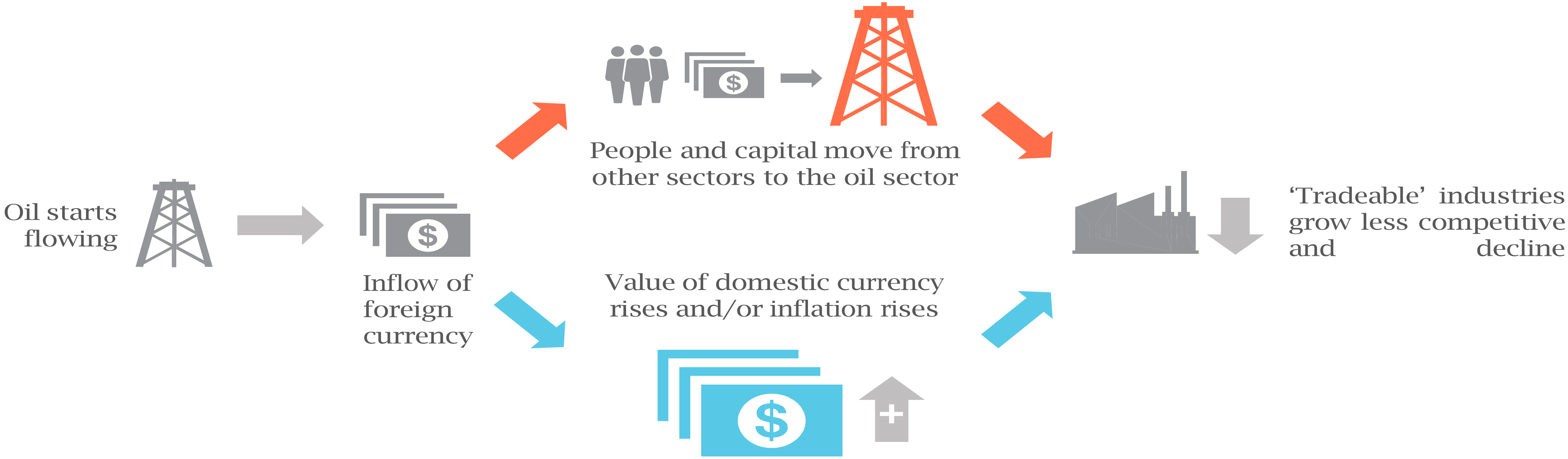
Chile
40.0%
30.0%
20.0%
10.0%
0.0%
-10.0%
-20.0%
-30.0%
1997
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
Government revenue growth (pesos)
Government expenditure growth (pesos)



Venezuela
200.0%
150.0%
100.0%
50.0%
0.0%
-50.0%
1992
1994
1996
1998
2000
2002
2004
2006
2008
2010
2012
Government revenue growth (bolivares)
Government expenditure growth (bolivares)

Dutch disease

Dutch disease



Contribution of Royalties to Govt by BT

2018- 1.3 Billion

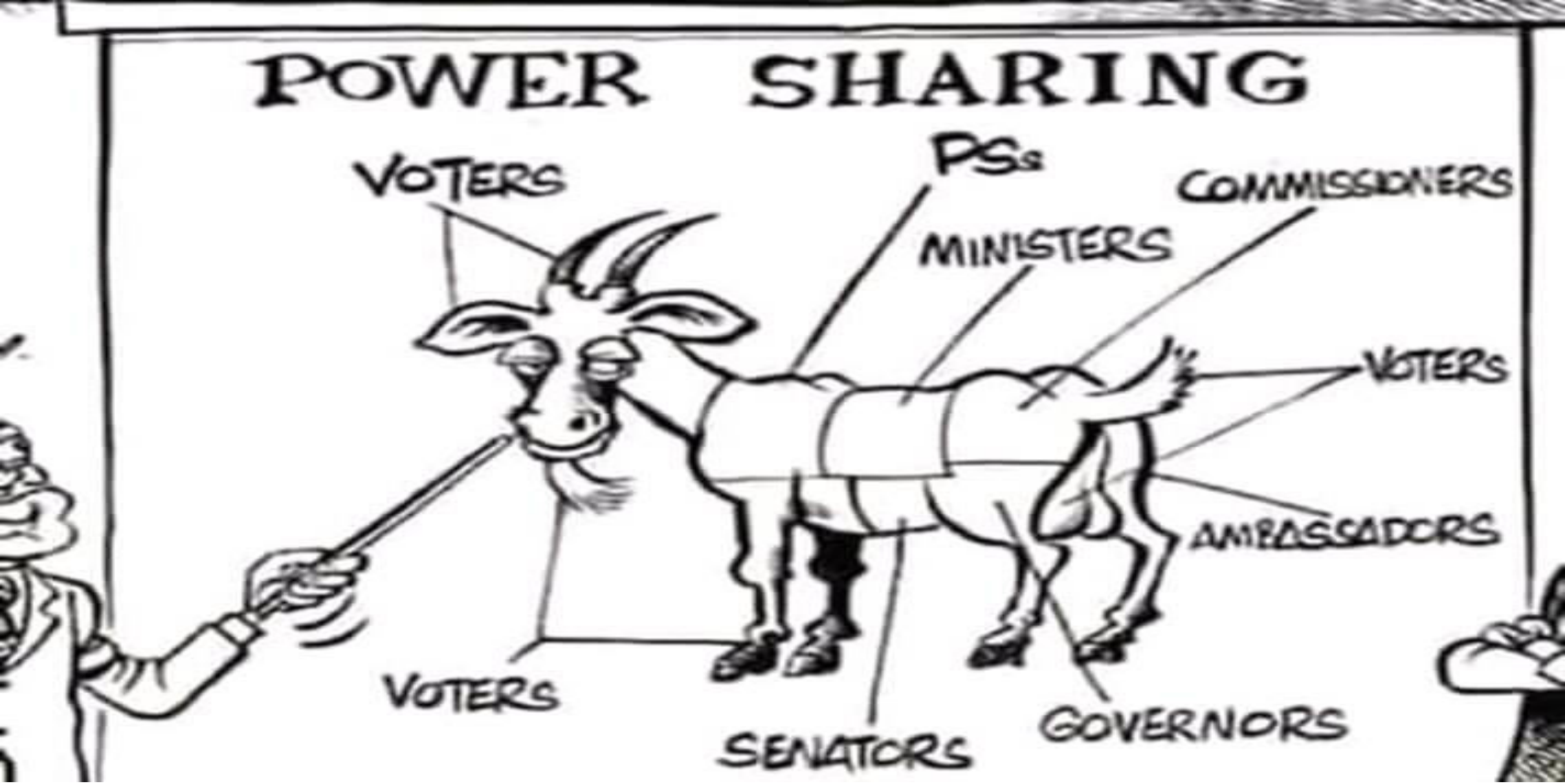
2017- 1.1 Billion

Where are these monies held? No indication of a holding account to date

Need for transparency and accountability in revenue spending and management

Need for Auditor General to audit books of account on use of the revenue streams this far

Kwale County has received a total of **Ksh. 32 billion** from 2013/2014 to 2017/2018 from the aforementioned sources. However, an interaction with some of the mining host communities revealed otherwise. Villages such as Kibwaga, Vumbu and Vidungeni have never been allocated even a single project since devolution started.


POWER SHARING
VOTERS
PSs
COMMISSIONERS
MINISTERS
VOTERS
AMBASSADORS
VOTERS
SENATORS
GOVERNORS

THANK YOU

Contact: pauline@hakijamii.com