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Back to the drawing board on mining law

South Africa has $2.5 trillion in mineral resources, putting it way ahead of all other countries, including Australia and Russia with $1.6 trillion each. But South Africa's mining industry shrank even during the global commodities boom of the early 2000s, which the National Development Plan (NDP) recognised as 'an opportunity lost'. The NDP acknowledged that much of the fault lies with South Africa's mining law, and urged that this be amended to bring it into line with international best practice.

Thus far, however, the government's proposed changes to mining law continue to chase in the wrong policy direction. It's now time to go back to the drawing board, and embrace the real reforms so urgently required. These could profitably be based on Botswana's mining law, which has served it very well.

Botswana came to independence in September 1966, almost exactly 50 years ago, with annual average GDP per capita of roughly $80, almost no infrastructure, low literacy rates, a tiny industrial sector, and an economy heavily dependent on subsistence farming and government employment. Since then, it has successfully used its mineral wealth to become an upper-middle income country with average GDP per capita of $7 240 in 2014. By contrast, South Africa's GDP per capita that year was some $6 800, or roughly 5% less.

If South Africa is to make the most of its mineral wealth, it must follow the NDP's advice and make its mining law, like the Mines and Minerals Act in Botswana, 'predictable, competitive, and stable'.

The mining industry is the bedrock on which modern South Africa was built. It still remains vital to the country's economic success, providing some 400 000 direct

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jobs and many more in the wider economy. It also brings in foreign investment, generates tax revenues, and bolsters export earnings. South Africa also has virtually unparallelled mineral riches, a Citibank survey in 2010 estimating the value of its mineral resources at $2.5 trillion. This puts the country far ahead of both Australia and Russia, whose resources are estimated at $1.6 trillion each.

Despite South Africa's extraordinary mineral wealth, its mining industry has performed well below its potential for the past 15 years. Even during the global commodities boom from 2001 to 2008, the country's mining industry shrank by 1% a year, while mining sectors in other states expanded by 5% a year on average.

Despite South Africa's extraordinary mineral wealth, its mining industry has performed well below its potential for the past 15 years.

The National Development Plan (NDP), endorsed by the ruling party as the country's overarching policy blueprint in December 2012, recognises this poor performance as 'an opportunity lost'. The NDP acknowledges that much of the fault lies with the vague and uncertain terms of the Mineral and Petroleum Resources Development Act (MPRDA) of 2002 and its accompanying mining charter, both of which came into effect in May 2004. It thus urges that the MPRDA be amended to 'ensure a predictable, competitive and stable regulatory framework'.

Thus far, however, little has been done to implement this recommendation and give the mining industry the advantages of a world-class regulatory regime. If South Africa is to benefit more fully from its enormous mineral wealth, the African National Congress (ANC) must stop chasing in the wrong policy direction. It must also recognise that mineral deposits in the ground have real-world value only to the extent that they can be mined and brought to market on a profitable basis. In heeding the NDP's advice – and seeking to bring South Africa's mining law into line with international best practice – the ANC must also recognise the many factors unique to mining that make it so vital to ensure the right policy mix.

Key factors impacting on mining policy

Mining is costly and has long lead times: Mining generally requires time-consuming and costly preliminary exploration to identify the location, depth, and potential market value of mineral deposits. It also often requires enormous upfront expenditure on acquiring machinery, sinking shafts, developing and shoring up tunnels, dealing with underground water, holding down dust levels, storing mining waste, and hiring and training mine workers. Often, it takes years before a new mine or shaft assumes production and begins to generate revenue to offset these heavy costs.

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This situation makes mining companies particularly vulnerable to *obsolescing bargain* risks. In other words, the more an investor spends on establishing or expanding a mine – which, by definition, cannot be moved elsewhere – the more that investor becomes a captive of the host government. That government may then be tempted to change relevant tax and other rules, especially if mineral prices have risen sharply in the interim, or particularly valuable mineral deposits have been found. The investor thus needs confidence that the government

will refrain from changing the policies that applied when the decision to invest was made.

The quid pro quo or essential bargain: The government provides the investor with secure mineral rights in a certain and stable policy environment. In exchange, the investor undertakes to explore and exploit the relevant mineral resources in an efficient and productive way. The investor also undertakes to make a full disclosure of the resources being mined, pay all taxes due, and fulfil appropriate health, safety, and environmental obligations.

The investor needs confidence that the government will refrain from changing the policies that applied when the decision to invest was made.

The volatility of mining profits: As Zimbabwean economist Tony Hawkins has pointed out, for the 25 years before the commodity price boom of 2002 to 2008, mining operations for base metals offered very limited returns. Profits were generally slightly below the yield on US government bonds – which meant investors would have done better by closing their mines and investing the proceeds in these bonds instead.

Enormous growth in China's demand for minerals during the 2000s changed the situation dramatically. But the global financial crisis in 2008 put a halt on surging demand, while China's decision to re-orient its economy towards increased domestic consumption has brought about a dramatic fall in most commodity prices since 2011. Over the past five years, the price of iron ore has dropped by more than 70%, while the gold price (despite recent rallies) has decreased by some 30% and the platinum price by around 50%.

Profits from mining are widely seen as 'rents': Because minerals are natural resources that do not have to be made or produced, returns on investment in mining tend to be seen as 'windfall' profits or 'rents'. However, this overlooks the major expenditure, effort, and risk-taking entrepreneurship generally needed to find and exploit mineral deposits. These deposits also have little value as long as they remain underground. It is only the often difficult and costly process of digging them out, bringing them to the surface, and (in many cases) separating them from surrounding rock that gives commercial value to mineral deposits. Moreover, if the costs of their extraction exceed the price at which mineral products can be sold, then below-ground mineral resources have little value in the real world. Yet this fact is often overlooked by governments, which adds to the obsolescing bargain risk.

Because minerals are natural resources that do not have to be made, returns on investment in mining tend to be seen as 'windfall' profits.

Mineral wealth is often poorly managed by governments: One of the key risks is the resource curse, characterised by the ramping up of state consumption expenditure in mining's boom times. Often, this level of spending cannot be sustained when commodity prices fall, leading either to painful adjustments or to unsustainable government debt. Also relevant is Dutch disease, for major mining export earnings may so boost the exchange rate as to make the exports of other sectors (agriculture and manufacturing) less internationally competitive. This in turn may make it more difficult to diversify the economy away from the extraction of finite mineral reserves, even though this shift is vital for long-term prosperity.

Resource nationalism is a perennial problem: When mineral prices rise, governments want a bigger take of what they commonly depict as mineral 'windfalls'. Often, however, these

increased profits are needed to counter-balance mining's long lead times, or to compensate mining companies for periods when mineral prices are low. Investors thus need stable and predictable fiscal and mining regimes to protect them from 'windfall' taxes and other damaging policy shifts.

Often the key problem is a self-serving elite, which sets up a policy system intended to favour the select few, or give preference to one ethnic or racial group over another. Local procurement policies may also open the door to corruption for the benefit of the ruling party or its key leaders. Sometimes mineral revenues are never properly reported by government agencies, allowing significant proportions of the taxes paid to 'disappear' into the pockets of the governing elite, without ever being disclosed or accounted for.

In a globalised world, countries must compete for mining investment. Mining companies are acutely aware of the obsolescing bargain risk.

Mineral resources are finite, while their extraction generally raises important ***health, safety and environmental considerations:*** Since mineral resources are depleted through mining, governments generally want to exploit mining revenues to the full – ideally, by making investments in infrastructure and human capital that in time will provide new sources of economic growth. At the same time, mining is often intrinsically dangerous, requiring appropriate protection for the health and safety of mineworkers. It also raises major environmental concerns, for land dug up for mining purposes cannot easily be rehabilitated. In addition, the mining process often generates noxious solid, liquid, and airborne waste, and can leave land so honeycombed with underground workings that it cannot easily be used for other purposes.

In a globalised world, countries must also ***compete for mining investment:*** Mining companies across the world are acutely aware of mining policy and the obsolescing bargain risk. This is clear, for instance, from an annual survey of the attractiveness of different mining countries conducted since 1997 by the Fraser Institute, a think tank based in Canada. As the Fraser Institute reports, decisions on where to undertake mining exploration are guided 60% by geological attractiveness (the likelihood of finding commercially viable mineral deposits) and 40% by the content of mining policies. Mining companies are also well aware of policy differences between countries and tend thus (as the Fraser Institute reports) to 'shift...exploration investment away from jurisdictions with unattractive policies'.

Decisions on where to undertake mining exploration are guided 60% by geological attractiveness and 40% by the content of mining policies.

Key international comparisons

Since the MPRDA came into force in 2004, South Africa has steadily lost ground on the Fraser mining survey. In the 2002/03 Fraser survey, before the MPRDA came into effect, South Africa ranked 27th out of 47 countries. In the 2015 survey, by comparison, it ranked 66th out of 109 countries. This put it behind most African countries, including Burkina Faso, Ghana, Namibia, Botswana, Eritrea, Ivory Coast, Ethiopia, and even the strife-torn Democratic Republic of the Congo.

In probing investor views on policy issues, the Fraser survey covers 15 factors. Among

these are the following:

1 'uncertainty... in the enforcement of existing regulations';
2 uncertainty about environmental regulations (whether these are stable, consistent, tardy, and 'not based on science');
3 the legal system (whether relevant legal process are 'fair, transparent, non-corrupt, timely, and efficiently administered');
4 the merits of the taxation system (levels of 'personal, corporate, payroll, capital, and other taxes', along with 'the complexity of tax compliance');

At least 12 factors are important to mining investors. These include the extent of 'uncertainty… in the enforcement of existing regulations'.

5 socio-economic obligations (the extent to which mining companies are expected to comply with local purchasing and beneficiation requirements, or 'supply social infrastructure such as schools or hospitals');
6 trade barriers (the impact of tariff and non-tariff barriers, plus constraints on the repatriation of capital);
7 labour regulations (including employment agreements and labour militancy or work disruptions);
8 uncertainty about disputed land claims;
9 political stability;
10 the availability of labour and skills;
11 the level of security (including physical security and the risk of attack by criminals, guerrilla groups, and so on); and
12 access to infrastructure (including access to roads, electricity, and the like).

(These last four matters extend beyond mining policy, but are nevertheless included because they are profoundly affected by good or bad policies and have a major impact on the mining environment.)

The Fraser survey probes the extent to which regulations, taxation, socio-economic obligations, political risk, or labour militancy affect investment decisions.

The Fraser survey also assesses how attractive different countries would be to investors if their mining policies were based on 'best practices': in order words, if they had (in the Fraser survey's words) 'a world-class regulatory environment', marked by 'highly competitive taxation, no political risk or uncertainty, and a fully stable mining regime'. By effectively stripping out policy issues in this way, this element in the survey helps identify a country's 'pure' mineral potential.

The survey also probes the extent to which the 'current practices' of different countries encourage or discourage exploration. Instead of assuming that 'best practices' apply, this aspect of the survey probes the extent to which actual regulations, taxation, socio-economic obligations, political risk, or labour militancy affect investment decisions. The survey then compares 'best practice' responses with 'current practice' ones, as this helps to demonstrate to governments how much room they have to reform their mining policies.

South Africa and Botswana

South Africa has enormous mineral wealth, well-developed capital markets, established mining expertise, and a level of infrastructure unmatched on the African continent. It neverthe-

less fares poorly on the 2015 Fraser survey compared to ten other African countries. It also does badly in comparison with its Botswana neighbour. The differences here are particularly telling, for both countries embarked on major changes to their mining laws in the late 1990s. Botswana opted to reform its 1977 mining legislation so as to bring it into line with international best practice. The new mining law Botswana adopted in 1999 is thus predictable and clear. The mining minister and his officials have little or no administrative discretion, making the licensing process transparent and predictable. The obligations imposed on the holders of mining licences are reasonable, certain, and stable, having remained effectively the same since the statute was adopted. Time frames for decision-making are brief: 60 days for prospecting licences, for instance, and 20 days for large-scale mining licences.

Botswana has reaped substantial benefit from its 1999 reforms, becoming one of the most attractive mining countries in the world in many ways.

Botswana has reaped substantial benefit from its 1999 reforms, becoming one of the most attractive mining countries in the world on various elements in the Fraser survey. South Africa could have followed its neighbour's example and ensured that its new mining regime complied with international best practice. Instead, South Africa chose to move in the opposite direction.

The consequences of this policy choice are evident in the rankings accorded the two countries in the 2015 Fraser mining survey. South Africa ranked 66th out of 109 countries on its overall attractiveness to investors, based on both geological factors and policy ones. Botswana ranked 39th out of 109. Since South Africa's mineral wealth far exceeds that of Botswana – and that of almost all other mining countries too – the gap between the two shows how greatly Pretoria's policies are harming South Africa's mining sector.

The comparative scores of South Africa and Botswana on the 12 policy issues particularly relevant to investors are set out in *Table 1* below:

Table 1: Fraser Institute Mining Survey 2015 (South Africa and Botswana)

	Element in mining survey	*South Africa*	*Botswana*
1	On uncertainty wth regard to mining regulations	84th	2nd
2	On environmental regulations	44th	5th
3	On legal system (for mining)	70th	20th
4	On tax regime (for mining)	69th	2nd
5	On socio-economic obligations	91st	35th
6	On trade barriers	81st	43rd
7	On labour regulations	105th	46th
8	On uncertainty about land claims	62nd	4th
9	On political stability	76th	19th
10	On the availability of skills and labour	58th	78th
11	On the level of security	25th	89th
12	On Infrastructure	56th	46th

Also relevant are those aspects of the Fraser survey that sum up the cumulative impact of policy issues, as shown in *Table 2* below:

Table 2: Fraser Institute rankings showing cumulative impact of policy issues

	Rank (out of 109 countries)	*South Africa*	*Botswana*
i	Overall policy perceptions index	78th	14th
ii	Best practices' mineral potential	50th	71st
iii	Current practices' mineral potential	85th	30th
iv	Difference between best and current: room for improvement	16th	102nd

South Africa lags far behind Botswana on almost all elements of the Fraser survey. South Africa also does badly on the 'room for improvement' test.

As these two tables show, South Africa lags far behind Botswana on almost all elements of the Fraser survey. Only on the availability of labour and skills (element 10 above) and on the extent of its infrastructure (element 12 above) does South Africa rank higher than its neighbour. This is also not surprising, for Botswana came to independence in 1966 with annual average GDP per capita of roughly $80, almost no infrastructure, low literacy rates, a tiny industrial sector, and an economy heavily dependent on subsistence farming, government employment, and remittances from Batswana working on South African mines and farms. South Africa's economy at this time was already far larger, and its skills and infrastructure significantly better developed.

The widely divergent rankings of the two countries on the 'room for improvement' element (element iv above) are particularly telling. South Africa has one of the highest rankings in the world in this regard, showing how much it needs to improve its current policies. Botswana, by contrast, comes 102nd out of 109 countries (eighth lowest in the world), confirming how little 'room for improvement' it has – and how closely its current practices already match world-class standards of regulation.

'In South Africa, the entire process of the administration of exploration rights is protracted, corrupt, arbitrary, inconsistent, and a nightmare'.

Comments by mining executives canvassed during Fraser surveys in recent years further underscore the differences between the two countries. Regarding South Africa, these executives said:

- 'In South Africa, the entire process of the administration of, and applying for, and awarding of, exploration rights is protracted, corrupt, arbitrary, inconsistent, and a nightmare' (2011);
- 'There is a strong grassroots movement to nationalise industry popularised by youth leaders as a cure for poverty/social/health problems' (2011);
- 'Both South Africa and Zimbabwe are driving social experiments not driven by logic and economy, but by ideology. In the absence of reason, primary industries have become the cash cows to fund the unfundable' (2012);
- 'Changing environmental and regulatory acts/laws have resulted in extended delays and various other issues. Lengthy red tape and multitude of departments overseeing permits, etc' (2013);

- 'Highly political unionised workforce that perpetually demands more and more in return for less and less productivity' (2014); and
- 'Government has suggested restrictions on exports of commodities and an imposed price structure' (2015).

Regarding Botswana, by contrast, mining executives said:

- 'Botswana is pro-mining and has efficient bureaucrats, no corruption, reasonable and consistent regulations, and reasonable taxation. It has also remained constant as other traditional mining-friendly areas have moved away from supporting mining' (2010);
- Botswana encourages and assists project development; it is the jurisdiction other African countries should strive to copy' (2011);
- Botswana's mining policies are 'clearly defined and obtaining all required mining permits is relatively quick and straightforward compared to most countries worldwide' (2011);
- 'Reasonably quick decision-making and access to decision makers – no corruption at all' (2014); and
- 'Improving the fiscal regime in a period of depressed commodity prices rather than increases taxes/royalties in order to try and maintain government revenues was a positive' (2015).

'Botswana encourages and assists project development; it is the jurisdiction other African countries should strive to copy'.

Botswana has also largely avoided the resource curse. Though further diversification of its economy is still needed, it has successfully used its mineral wealth to promote growth and prosperity over the past 50 years. Between 1966 and 1999, Botswana recorded an average annual growth rate of 9% of GDP, making it one of the fastest growing countries in the world. In the past decade, despite the global commodities slump, its growth rate has averaged 5% of GDP. It has risen up the World Bank's ratings to attain the status of an upper-middle income country, and had average GDP per capita of some $7 240 in 2014. By contrast, South Africa's GDP per capita that year was some $6 800, which is roughly 5% below that of Botswana. In addition, South Africa's economic growth rate over the past ten years has averaged only 2.6% of GDP a year, again well below that of its neighbour.

A key reason for Botswana's success lies in its mining regime and the extent to which this complies with international best practice. If South Africa is to make the most of its mineral wealth, it must follow the NDP's advice and bring the MPRDA into line with what best practice requires. In doing so, it would be well advised to follow the example of Botswana's Mines and Minerals Act of 1999, which has served it very well.

If South Africa is to make the most of its enormous mineral wealth, it would be well advised to follow the example of Botswana's Mines and Minerals Act of 1999.

Reforms are needed in a host of spheres. These include the granting of mining rights, the grounds on which they can be cancelled, beneficiation requirements, and the risks of nationalisation, expropriation, or other forms of state control, all of which are canvassed below. Also vital in South Africa is the question of how the disadvantaged can most effectively be

empowered, and this will be analysed in a subsequent issue of *@Liberty*. Equally important are environmental, health, safety, and labour policies, along with the fiscal regime and dispute resolution mechanisms – all of which will be dealt with in due course.

The granting of mining rights

International best practice requires equality before the law in the granting of mining rights. It also seeks certain and unambiguous rules that promote transparency and give officials minimal scope for bias, corruption, or other abuses of power.

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Botswana

Under the Botswana Mines and Minerals Act of 1999, the key criteria for the granting of a mining licence (the equivalent of a mining right under the MPRDA) are:

- a proposed mining programme that will 'ensure the most efficient and beneficial use of the mineral resources in the proposed mining area';
- 'access to adequate financial resources, technical competence, and experience to carry on effective mining operations';
- a proposed financing plan that is 'in accordance with good financial practice, and provides for a debt:equity ratio of not more than 3:1, unless the mining minister otherwise agrees';
- a proposed mining area which does not duplicate or overlap with an existing mining area; and
- confirmation that the applicant (if a company) is registered in Botswana and 'plans to carry on the sole business of mining under the mining licence applied for'.

The minister must grant the mining licence if these conditions are met. In general, an applicant for a mining licence must already have a prospecting licence for the relevant mineral and area. Where no prior prospecting licence has been issued and competing applications are lodged, the licence will go to the applicant whose proposed mining programme 'will make the more beneficial use of the mineral resources of the area'. A licence lasts for whatever period is needed to exploit the mineral, up to a maximum of 25 years, and can be renewed for another 25 years.

There are no onerous black economic empowerment, housing, or social obligations in Botswana's mining legislation.

There are no black economic empowerment (BEE), housing, or social obligations in Botswana's mining legislation, but only a limited 'local preference' requirement. The holder of a mining licence must thus give preference, 'to the maximum extent possible consistent with safety, efficiency and economy', to buying 'materials and products' made in Botswana, using service agencies located in Botswana, and employing Botswana citizens.

The strength of the Botswana approach is that it identifies and seeks to leverage the benefits of mining investment without requiring miners to take on a range of onerous BEE, housing, and other social obligations. The legislation shows a clear understanding that the sub-

stantial investment required to develop a mine and carry out mining operations is itself a major economic and social good. In this process, capital is committed and jobs are created, while household living standards and expenditure levels rise. At the same time, tax revenues and export earnings are generated for the benefit of the society as a whole.

South Africa

By contrast, the granting of mining rights under the MPRDA depends only partially on applicants having the necessary financial resources and the technical ability to carry out their proposed mining operations. In addition, applicants must show that the granting of the rights they seek will:

The investment required to develop a mine and carry out mining operations is itself a major economic and social good, helping to generate jobs, tax revenues and export earnings.

- 'substantially and meaningfully expand opportunities' for black people to enter the mining industry, and
- 'advance the social and economic welfare' of all South Africans,

'in accordance with the mining charter and the prescribed social and labour plan'. These provisions are inherently ambiguous. They also impose costly and demanding BEE and other socio-economic obligations on applicants, under both the shifting terms of the mining charter and the often unrealistic requirements of social and labour plans. In addition, some of the supposedly clear rules in the MPRDA – the first-in, first-assessed rule for competing applications, and the preference to be shown towards applicants who already hold prospecting rights – have been abused at times.

BEE requirements in the *mining charter* are particularly problematic. The 26% BEE ownership requirement (which had to be met by 2014) has made it possible in practice for DMR officials to choose the 'correct' BEE investors for mining companies to partner with by signalling that an application for a mining right is unlikely to succeed unless a specific BEE partner is brought in. As BEE consultant Jenny Cargill writes in her book *Trick or Treat*, 'this has enabled officials to dispense state patronage to the emerging black elite and in particular to those with political standing'. Mining houses are aware of such abuses, but are reluctant to complain for fear that officials may retaliate by denying them mining rights.

The 26% BEE ownership requirement has 'enabled officials to dispense state patronage to the emerging black elite'.

Undue influence of this kind was arguably evident in 2010, when Gold Fields urgently needed a fresh BEE ownership deal (after its earlier empowerment partner had sold out), so as to maintain its compliance with the charter and acquire a mining right for its new South Deep mine at Carletonville (west Rand). For the purposes of this new BEE deal, worth around some R2.1 billion, a consortium called Invictus Gold was established, in which various individuals with strong links to the ruling party were given stakes. But Gold Fields was then reportedly told that the mining right was unlikely to be granted unless ANC chairwoman Baleka Mbete was brought into the consortium and given a stake substantially greater than the R2.2 million the company had first proposed. 'And so it came to pass that Mbete walked away with a lot more: an empowerment stake worth R28.6 million', as the *Mail & Guardian* newspaper was later to report.

No clear evidence of undue influence has ever come to light. Gold Fields was nevertheless widely seen (as journalist Carol Paton wrote in *Business Day*) as having had little choice but to comply with 'the unwritten rule book' of BEE transactions. Added Ms Paton: 'No beneficiary or executive...has yet been persuaded to speak on the record about how the deals happen. Off the record, they explain that the process of putting together a BEE consortium...entails not just the normal things – like getting funders on board – but also getting the right people who will meet with political approval. Says one BEE businessman: "Core people are put forward by government and by Luthuli House and you are told that whoever else you want to include...is fine. But [including] certain people is non-negotiable. You have to be mad or naive not to realise...that this is how it works."'

The black management target is not easy to fulfil, as more than half of black South Africans are under the age of 25, and only 5% have tertiary education.

Other BEE elements in the charter were initially less problematic, as they simply required mining companies to 'aspire' to meet various BEE goals. But that changed in 2010, when the DMR insisted on the introduction of hard numerical targets in several spheres. On employment equity, for example, the 2002 charter said that mining companies should 'aspire to a baseline' of 40% black participation in management within five years. However, the revised charter of 2010 states that mining companies must 'attain a minimum of 40% black representation at board and management levels'. This target is not easy to fulfil, as more than half of black South Africans are under the age of 25 and lack the experience needed for management posts, while only 5% of them have the tertiary education often necessary or advisable for such positions.

Similar shifts were made on preferential procurement. The 2002 charter said that mining companies must 'increase procurement from black companies' and 'encourage their existing suppliers to partner with black firms'. By contrast, the revised charter of 2010 states that mining companies must increase annual procurement from black-empowered suppliers to 40% for capital goods, 50% for consumer goods, and 70% for services. These targets are also not easy to fulfil, given the limited number of experienced black firms with the capacity, in particular, to supply capital goods, which range from drilling and hoisting equipment to crushing mills and furnaces.

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The mining charter's obligations have thus become increasingly difficult for applicants to meet. The changes imposed have also undermined the certainty of mining rules and increased the obsolescing bargain risk within the country.

The MPRDA's requirements regarding *social and labour plans* – which are supposed to contribute to the socio-economic development of mining communities and labour sending areas – have also generated a host of practical problems. Applicants must develop plans that are acceptable to DMR officials; and show that they have provided, financially and otherwise, for the implementation of these proposals. In practice, social and labour plans commonly include undertakings by companies to improve living conditions and human capital in min-

ing areas, but the MPRDA provides little guidance as to what they should incorporate. Uncertainty about these requirements has made it easy for DMR officials to approve or disapprove social and labour plans on arbitrary, and often spurious, grounds. It has also allowed officials to require repeated revisions of social and labour plans, contributing to long delays in the approval of applications. Says Manus Booysen, a partner at Webber Wentzel: 'Delays commonly run to 18 months and when we tell foreign investors [this], they often decide to pack their bags and invest elsewhere.'

Vague provisions and uncertainty have made it easy for DMR officials to approve or disapprove social and labour plans on arbitrary grounds.

The MPRDA also includes a *'first-in, first-assessed'* rule, in terms of which competing applications are supposed to be granted in the order in which they are received by the DMR. If two applications for the same mineral and area are received on the same day, the minister must give preference to the application coming from black South Africans. However, even these seemingly clear rules have been abused in practice.

For many years, the DMR publicised applications for mining rights by physically pinning up notices on public notice boards from which, of course, they could easily be removed. Writes Ms Cargill: 'This had enormous significance, as applications were supposed to be processed on a first-come, first-served basis. If a notice went "missing", where was the proof of who applied first?' This lack of transparency made it easy for DMR officials to provide inside information to favoured BEE applicants, or help them get ahead in the queue.'

Further abuses of the first-in, first-assessed principle are evident in the Kumba story. This began in April 2009, the month that marked the deadline for the conversion of 'old-order' mining rights into the 'new-order' ones created by the MPRDA. Kumba Iron Ore owned 79% of the old-order mining rights to the iron ore it had long been producing at its Sishen mine (near Kathu in the Northern Cape). ArcelorMittal South Africa (AmSA) held the remaining 21%. Kumba successfully converted its old-order rights to new-order ones before the deadline, but AmSA forgot to apply. It thus became apparent that the old-order right held by AmSA would 'cease to exist', under the relevant provisions of the MPRDA, at midnight on 30th April 2009.

When Kumba realised this, it decided to apply for a new-order mining right over the remaining 21% of its Sishen mine. Kumba submitted its application on 30th April 2009, shortly before AmSA's old-order right was due to expire, and before any other contender could do so. This should have guaranteed it success under the first-in, first-assessed rule.

Kumba submitted its application before any other contender could do so, which should have guaranteed it success, under the first-in, first-assessed rule.

However, when DMR offices re-opened on 4th May (after an intervening long weekend), a BEE entity called Imperial Crown Trading (ICT) lodged a competing application for a prospecting right over the whole of Kumba's established Sishen mine. ICT was a shelf company with no mining experience, but good political connections. Its application was signed only on 5th May, while its detailed proposals were dated 8th or 9th May, which meant that it should never have entered into competition

with Kumba's earlier one. Worse still, there was evidence to suggest that ICT had copied key supporting documents from the Kumba application, which could only have been done with the help of DMR officials. Despite these flaws, the DMR granted ICT a prospecting right over the 21% share that AmSA had previously held.

Kumba urged the then mining minister, Susan Shabangu, to set aside the award to ICT, but she refused to accept that the process had been irregular. Kumba then applied to the Pretoria High Court, which granted it the relief it sought in 2011. This decision has since been upheld by both the Supreme Court of Appeal and the Constitutional Court. The Constitutional Court ruling, handed down in 2013, also made it clear that Kumba was the only entity to which AmSA's earlier mining right could be granted.

Despite having won three court cases, Kumba still does not have the mining right which the first-in, first-assessed rule should have secured for it more than seven years ago.

However, Kumba still does not have this mining right. Despite the absence of any clear MPRDA authority for this, the Constitutional Court also ruled that the minister could lay down 'whatever conditions she might deem appropriate' to counter the possible detrimental effect of a Sishen 'monopoly' on the local steel industry. Thus far, the conditions proposed by the minister have been unacceptable to Kumba, which is still trying to negotiate an appropriate outcome. As a result, Kumba still does not have the mining right which the first-in, first-assessed rule should have secured for it more than seven years ago.

The MPRDA also gives the *holders of prospecting rights* 'exclusive' capacity to apply for and obtain mining rights to the minerals they have discovered. Yet this apparently clear rule has also been ignored at times. In 2006 for instance, Aquila Resources, an Australian mining company, was granted a prospecting right for manganese and iron ore near Kuruman (Northern Cape). Having spent some R150m on exploring the area and developing a potentially world-class manganese project, Aquila applied in 2010 for the relevant mining right under the MPRDA rule giving it an exclusive capacity to do so. But instead of granting Aquila its mining right, the DMR in 2011 awarded a second prospecting right over the same area to the Pan-African Mineral Development Company (Pamdc).

Aquila should have been awarded a mining right, but the DMR instead awarded a second prospecting right over the same area to the Pan-African Mineral Development Company.

Pamdc is jointly owned by the governments of Zimbabwe, Zambia, and South Africa. It was registered only in 2007, which means the grant of its prospecting right was also in breach of the first-in, first-assessed rule. The DMR then delayed for four years in dealing with Aquila's internal appeal, after which the company finally brought legal proceedings in 2015 to have the award to Pamdc set aside.

Commented *Business Day* in an editorial: 'This is not the first time – and neither will it be the last – that the department has granted a prospecting right [when it should not have]. Its modus operandi seems to be to provoke a dispute which is then "resolved" by its intervening between the "prospector" and the pre-existing miner to look for a "solution". We will wager that Aquila is offered an opportunity to form a joint venture with the so-called prospectors.

Thus is another nail driven into South Africa's reputation as a safe investment destination.'

Recommended reform

South Africa should follow the example of Botswana's mining law. The award of mining rights should depend solely, as in Botswana, on applicants having 'adequate financial resources, technical competence, and experience to carry on effective mining operations'. The first-in, first-assessed rule should generally apply. However, if two applications are received on the same day, the mining right should be granted, as in Botswana, to the one 'whose proposed mining programme will make more beneficial use of the mineral resources of the area'. In addition, where the holder of a prospecting right has discovered a mineral resource it now wishes to mine, it should always have preference over other contenders, rather than see the benefits of its discoveries usurped by others.

Mining companies should not have to take on onerous BEE obligations of the kind set out in the mining charter.

Mining companies should not have to take on onerous BEE obligations of the kind set out in the mining charter. Nor should they have to take on responsibility for costly 'social and labour plans'. At most, mining companies should be asked voluntarily to comply with a different scorecard forming part of a new empowerment initiative, to be called 'economic empowerment for the disadvantaged' or 'EED'. The EED concept has been outlined in an earlier issue of *@Liberty* (see 'Re-imagining the mining industry', *@Liberty*, No 26, August 2016) and will be further described in a subsequent issue.

Cancellation of mining rights

Because mining is so costly and the period required for the proper exploitation of a mineral deposit is often so long, mining companies need to be confident that the mining rights they are granted will not be prematurely cancelled without sound reason. In particular, they need to be confident that the relevant rules will not be changed so as to make them vulnerable to cancellation on the basis of requirements that did not apply when they decided to invest.

Botswana

Botswana's Mines and Minerals Act requires mining companies to meet a number of clear and reasonable obligations, failing which their mining licences may be cancelled. The basis on which cancellation may be ordered has remained effectively unchanged since the statute's adoption in 1999.

In Botswana, mining licences may be cancelled only for failure to meet a number of clear and reasonable obligations, which have remained effectively unchanged since 1999.

Under the Botswana legislation, a company granted a mining licence must commence production on the date specified in its mining programme; 'develop and mine the mineral...in accordance with good mining and environmental practice'; maintain complete and accurate technical records of all mining operations; provide accurate financial records; submit such information and reports as the minister may reasonably require; and timeously furnish a copy of its annual audited financial statements.

The statute empowers the minister to cancel (or suspend) a mining licence if the mining company:

- fails to pay its annual fee or make other required payments;
- contravenes the provisions of the 1999 Act;
- fails to comply with the terms on which its mining licence has been granted (for example, by failing to adhere to its mining programme);
- knowingly makes a false statement in the information it is obliged to provide; or
- fails to remain registered as a Botswana company.

Before cancelling a mining licence, the minister must give notice to the mining company and give it the opportunity to rectify the matter within a specified period of not less than 30 days. If remedial action is not taken in this period, the minister may then cancel the mining licence.

In South Africa, recent amendments to NEMA have also increased the likelihood of mining rights being cancelled on environmental grounds.

South Africa

At first glance, the MPRDA seems similar (albeit broader), for it empowers the mining minister to cancel (or suspend) a mining right if a mining company:

- is conducting a mining operation in contravention of its terms;
- breaches any material term or condition of the mining right;
- contravenes any condition in its environmental authorisation; or
- submits information which is 'inaccurate, false, fraudulent, incorrect, or misleading'.

Before cancelling a mining right, the minister must give written notice to the company and allow it 'a reasonable opportunity' to make representations. The minister must also direct the mining company to take specified measures to remedy any contravention. If the company fails to do so, the minister must give it a reasonable opportunity to make representations before proceeding with a cancellation.

As this list shows, mining rights can be cancelled if a company contravenes 'any condition' in its environmental authorisation. Under recent amendments to the National Environmental Management Act of 1998, which took effect in November 2015, the environmental obligations of mining companies have become very much more complex and more costly. Though this shift has increased the likelihood of cancellation on environmental grounds, the new rules are so complicated that they require separate consideration in a subsequent policy paper.

The main risk of premature cancellation comes from the vague and shifting rules of the mining charter, and from the 'prescribed social and labour plan'.

For present purposes, the main risk of premature cancellation lies in the obligation to promote the active participation of black South Africans in the mining industry 'in accordance with the mining charter and the prescribed social and labour plan'. Mining companies that fail to comply either with the charter or their social and labour plan may thus be vulnerable to the cancellation of their mining rights.

Social and labour plan contraventions

The threat to mining titles in this sphere was made clear in 2011, when the then mining min-

ister, Susan Shabangu, announced the cancellation of a mining right earlier granted to gold mining company Central Rand Gold (CRG), for failure to fulfil its social and labour plan. CRG's chief executive, Johan du Toit, acknowledged that the company had been unable to spend the R33 million it had promised for social and labour projects because rising acid water had dramatically depleted its recoverable reserves. Despite its financial problems, it had nevertheless spent no less than R19 million on implementing its social and labour plan. In addition, the company had been compelled to spend a further R35 million on pumps to keep rising acid water at bay. Since this expenditure benefited not only itself but also the wider mining community, this sum should have counted as part of its 'social and labour' contribution. On this basis, said Mr du Toit, CRG had in fact exceeded the R33 million target set.

Susan Shabangu announced the cancellation of a mining right earlier granted to gold mining company Central Rand Gold, for failure to fulfil its social and labour plan.

Mr du Toit added that CRG had drawn up its social and labour plan on the basis of assumptions about future profits that subsequent events had made impossible to attain. The minister had nevertheless declined to enter into discussions on what the company could feasibly achieve. Instead, she had cancelled CRG's mining right in a blaze of publicity and with immediate effect – and without giving the company notice or the opportunity to make representations or take remedial action. When CRG applied for judicial review of the decision, the minister backed down and quietly restored its mining right. But the saga nevertheless demonstrated how easily mining rights could be terminated, without good reason, for alleged social and labour plan contraventions.

Mining charter contraventions

The mining charter, as drawn up in 2002, required mining companies to attain 26% BEE ownership by 2014. It also said that 'the continuing consequences of all previous deals' should be taken into account, even if those transactions came to an end because BEE investors had chosen to sell out. However, in 2010, as earlier described, the DMR unilaterally changed the charter in various ways. The 26% ownership target remained the same, but the revised charter now required specified levels of community and employee participation in all BEE deals. It also limited the 'once-empowered, always-empowered rule' to ownership deals concluded before 2002.

In 2015 the DMR used the charter's revised rules to claim that only 20% of mining companies had met the BEE ownership obligation.

In 2015, at the end of the ten-year charter period, the DMR used these revised rules to claim that only 20% of mining companies had met the BEE ownership obligation. The Chamber of Mines disagreed, saying all its members had at least 26% black ownership and that the average attained stood at 38%. In addition, BEE transactions had created a net value of R159bn, which was equivalent to 26% of the value of the entire mining industry in December 2014. These differing assessments stemmed mainly from conflicting views as to whether the changes introduced by the 2010 revised charter should have retrospective effect.

If the original targets in the 2002 charter were applied, the DMR agreed that 90% of mines had not only met the 26% target, but in fact exceeded it by bringing black ownership up to

some 33% on average. However, the 2010 charter had introduced a new rule saying that BEE deals must include employees and communities, and most ownership deals lacked the correct beneficiary mix. In addition, the DMR had not counted post-2002 ownership deals from which BEE partners had sold out, or which had otherwise come to an end.

As regards employment equity and preferential procurement requirements, the 2010 charter (as earlier noted) replaced aspirational objectives with hard numerical targets. These new targets were difficult to fulfil, given the acute shortage of experienced black managers and established black firms within the country. Yet the revised charter also expressly stated that 'non-compliance with its provisions' would 'render the mining company in breach' of the MPRDA and vulnerable to the cancellation of mining rights. Commented journalist Tim Cohen in *Business Day*: 'Suddenly, all the soft targets of the charter have been turned into black letter law. Suddenly, not achieving procurement targets means your competitors can insist your licence is revoked.'

'Suddenly, not achieving procurement targets means your competitors can insist your licence is revoked.'

In assessing compliance with these elements of the revised mining charter, the DMR's 2015 report found that most companies had met, if not exceeded, the 40% black management target. As for preferential procurement, the DMR report showed that some 82% of companies had met the 40% target for capital goods, while 65% had met the 50% target for consumer goods, and 83% had met the 70% target for services. Mining companies had mostly met their skills development targets, the DMR added, but their progress on hostel conversion had been limited. (However, the Chamber of Mines rejected the department's view on hostel upgrading, saying most of their members had complied fully with this requirement.)

Despite the high levels of compliance evident, the then mining minister, Ngoako Ramatlhodi, stressed that 'only about 70% of mining rights holders had done everything the charter required for meaningful economic participation'. The DMR, he went on, was now talking to companies which had not met the charter requirements and 'would have to take steps to cancel mining licences under Section 47 of the MPRDA'.

This was a major threat to the security of mining titles. In response, the president of the chamber, Mike Teke, said that the DMR was not 'fairly reflecting' all the work the mines had done. He also stressed the difficulties confronting the industry, which was faced with 'depressed commodity prices, rapidly escalating costs, electricity supply challenges, and continued uncertainty regarding some parts of South Africa's mining and transformation laws'. The CEO of Harmony Gold, Graham Briggs, added that the threat to revoke mining rights was a threat to the very existence of many companies and put 'a dark cloud' over the industry.

The CEO of Harmony Gold said that the threat to revoke mining rights was a threat to the very existence of many companies.

That threat has since increased still further with the publication of the draft 'reviewed' mining charter in April 2016. Under this draft, which the DMR wants to finalise in October this year, mining companies will have to remain 100% compliant with the 26% BEE ownership requirement throughout the 30-year life of a mining right, even if BEE investors choose to sell out.

Yet having to do ever more ownership deals over this prolonged period will be enormously costly. It will damage confidence, inhibit mine development, and dilute the shareholdings of all existing investors, many of which are pension funds seeking to meet the retirement needs of millions of ordinary South Africans, both black and white.

Under the draft, mining companies will also have to maintain 100% scores, again for 30 years or more, on costly skills development and housing targets. Again, these targets will not be easy to fulfil – and especially not when input costs are rising rapidly and mineral prices are depressed. Mining companies that fail to maintain 100% scores on these three 'ring-fenced' elements will nevertheless be vulnerable to the cancellation of their mining rights, for the draft charter states: 'Mining rights holders who have not complied with the ownership, housing...and human resource development elements...will be regarded as non-compliant with the provisions of the Charter, and the MPRDA shall render the mining right holder in breach of the MPRDA and subject to the sanctions provided for in the Act.' These sanctions, of course, include the cancellation of mining rights.

Having to do ever more ownership deals over this period will be enormously costly. It will also damage confidence and inhibit mine development.

BEE obligations under the mining charter are thus being steadily tightened up, while the new rules are also being applied retrospectively. The obsolescing bargain risk in South Africa is becoming increasingly apparent, providing a significant barrier to new investment in mining.

Reforms required

South Africa should follow the approach used in Botswana. Mining rights should be subject to cancellation only for material breaches of reasonable, certain, and stable requirements. Hence, the risk of cancellation should apply only where a mining company fails to maintain accurate records, or knowingly makes false statements in its reports, or omits to develop and mine the minerals in issue. In short, cancellation should be limited to material and persistent failures to uphold the essential bargain between the mining company and the South African government. (An effective dispute resolution process is also needed, but this issue will be canvassed in a subsequent policy paper.)

South Africa should follow the approach used in Botswana. Mining rights should be subject to cancellation only for material breaches of reasonable, certain, and stable requirements.

Beneficiation requirements

Partly because mineral resources are finite, governments often want mining companies to beneficiate them locally, so as to boost domestic employment, promote growth, and enhance the value of mineral products before they are exported. However, beneficiation requirements cannot realistically be met when essential inputs (electricity and skills, for instance) are lacking, or high production costs make manufactured goods internationally uncompetitive. Beneficiation also goes beyond the core competencies of mining companies, which should not be expected to contribute to downstream manufacturing. In the words of a former governor of the South African Reserve Bank, Gill Marcus: 'The idea that mines

should ensure beneficiation is akin to making families who own cattle manufacture leather handbags'.

Botswana

Botswana's Mines and Minerals Act imposes no beneficiation obligations on mining companies. All that it requires is that the holder of a mining licence should be able to run mining operations that make 'the most efficient and beneficial use of the mineral resources' in the relevant mining area. It also allows mining companies to 'dispose of any mineral products recovered', without any price or export controls aimed at boosting local beneficiation.

'The idea that mines should ensure beneficiation is akin to making families who own cattle manufacture leather handbags'.

South Africa

Beneficiation requirements under the MPRDA are being ratcheted up to a significant extent, in a further example of the obsolescing bargain hazard. At the same time, the DMR's demands ignore the extent of the local beneficiation that is already being achieved. They also overlook the fact that beneficiation cannot realistically be expanded in the light of practical constraints that are largely of the government's own making.

The DMR declines to acknowledge that the mining process is itself an important form of beneficiation. What mining achieves, in essence, is to convert mineral deposits beneath the surface into mineral products with a realisable market value. This in itself adds enormous value to the country's mineral resources, which would have no commercial value at all if they remained untapped within the ground. Mining companies should thus be given full credit for this vital form of local beneficiation.

Instead, they are increasingly being pressurised to contribute to the downstream industrial processing of mineral products. Yet the country lacks both the electricity supply and the skills required for the various stages of beneficiation, as the NDP itself has warned. Other obstacles to success include high input costs and the excessive volatility of the rand. In the face of these challenges, the Industrial Development Corporation (IDC), a state-owned enterprise that already has a mandate to promote local beneficiation, has long been battling to achieve this objective. In addition, new enterprises cannot easily be established when profit margins in manufacturing have shrunk from 7% in 2011 to 4.4% in 2014, some 246 000 jobs have been lost over this period, and South Africa's growth rate is likely to be less than 1% of GDP in 2016.

The DMR declines to acknowledge that the mining process is itself an important form of beneficiation. It also overlooks the many obstacles to the industrial processing of minerals.

Despite these binding constraints (many of them the product of the government's own policies), the DMR remains determined that the mining industry must do more to promote local beneficiation. Beneficiation obligations have already been increased – and will become yet more onerous if proposed amendments to the MPRDA are adopted in their current form.

As first enacted in 2002, the MPRDA had relatively little to say about beneficiation. It identified a commitment to local beneficiation as a factor that 'might' be taken into consideration in the granting of mining rights. It empowered the mining minister to 'promote' beneficiation

in various ways, and stated that companies wanting to beneficiate South African minerals outside the country would have to do so 'in consultation' with the minister.

However, under an amendment introduced in 2008, the minister was empowered, in promoting beneficiation, to 'prescribe the levels required for beneficiation'. This wording is ambiguous, but the DMR's intentions have since been clarified under the MPRDA Amendment Bill of 2013. (This Bill was adopted by Parliament in March 2014 but has yet to be signed into law, as President Jacob Zuma sent it back to the legislature in January 2015, citing concerns about its constitutionality. However, Parliament's mineral resources portfolio committee has recently rejected his concerns as unfounded, which could pave the way for the Bill's enactment in the near future.)

The minister may 'designate' minerals for local beneficiation and stipulate 'the prescribed quantities, qualities, and timelines' in which they must be provided.

Under the Bill, the mining minister 'must...regulate the mining industry to meet national development imperatives'. To this end, he must 'initiate or promote' beneficiation, and may 'designate' various minerals as needed for this purpose. He may also stipulate 'the prescribed quantities, qualities and timelines' in which these minerals must be provided. Prices must be either 'mine-gate' or 'agreed', while no designated mineral may be exported without the minister's consent until the stipulated percentages have been locally supplied. Though the Bill lacks detail on this point, both price and export controls are also likely to be imposed on all minerals identified by the minister as 'strategic'.

Such price and export controls will greatly restrict the operational autonomy of mining companies. They could also erode their profitability. Already, the possibility of price and export controls on coal is stalling investment in the new coal mines needed for power generation in the future. By 2022, Eskom will require an additional 76 million metric tonnes of coal for its power stations, while some R600bn needs to be invested in new coal mines to meet this demand. But mining companies have little wish to risk this outlay when the mining minister can decide to whom, and at what price, coal is to be sold. Hence, far from helping to guarantee coal supplies, the proposed provisions (in the words of Mike Rossouw, chairman of the Intensive Energy Users Group) are already 'choking off new investment and decreasing supply, which is the opposite of what the government wants and is needed'.

These proposed price and export controls are already 'choking off new investment in coal mines and decreasing supply'.

Reforms required

South Africa should scrap the beneficiation requirements in the MPRDA and follow the Botswana statute in allowing mining companies to dispose of mineral products on such terms as they think fit. The government should instead focus (through labour, education, and other reforms extending beyond the mining sector) on improving South Africa's global competitiveness and bringing down current barriers to successful local manufacturing.

In addition, the DMR should recognise that the mining process is itself a vital form of local beneficiation; that it is not part of the essential bargain for mining companies to promote local manufacturing; and that South Africa's sophisticated private sector is already well equipped

to identify opportunities for local value-addition where these make commercial sense.

Expropriation, nationalisation, and other forms of state control

The mining sector is particularly vulnerable to expropriation, nationalisation, and other forms of state control. The underlying reasons range from resource nationalism to the captive nature of mining investments and the major profits to be made from mining in boom times. International best practice thus requires appropriate safeguards for mining companies against expropriation, nationalisation, and other forms of state control.

The Botswana government has no right to a 'free' interest in a new mine. Its possible stake is also limited to 15%.

Botswana

The Mines and Minerals Act of 1999 echoes its 1977 predecessor in vesting 'all rights of ownership in minerals' in the Botswana government. It also gives the government, when it issues a mining licence, 'the option of acquiring up to 15% working interest participation in the proposed mine'. This working interest allows the government to appoint two of the company's directors and receive dividends proportional to its stake. But the statute also obliges the government to pay for its working interest by contributing, again on a proportional basis, to the expenditure incurred in obtaining the mining licence and developing the mine. The Botswana government thus has no right to a 'free' interest in a new mine. In addition, its maximum 15% stake is not big enough to give it control of a mining operation in which it chooses to participate.

Botswana has done little to change the relevant rules since 1999, when its new mining law was enacted. Nor has it threatened mining companies with the expropriation or nationalisation of their mining enterprises under other laws. It has also avoided 'indigenisation' rules of the kind adopted in Zimbabwe, which require all mining companies to have 51% local ownership. These factors have promoted investor confidence and help to boost Botswana's rankings on the Fraser mining survey.

Botswana has not threatened mining companies with nationalisation. It has also avoided 'indigenisation' rules of the kind adopted in Zimbabwe.

South Africa

In South Africa, by contrast, two thirds of the country's mineral resources were privately owned before the MPRDA came into force in May 2004. These ownership rights were real rights which, if properly registered, were enforceable against the world, had unlimited duration, and could freely be sold or otherwise disposed of. Under the MPRDA, however, the 'custodianship' of all mineral resources was vested in the state. Though mining companies already engaged in mining operations could apply for the conversion of their 'old-order' rights into 'new-order' rights, the new rights are clearly inferior to the old. In particular, the granting of new-order mining rights is dependent on complex BEE and socio-economic obligations, while the new rights last for a maximum of 30 years (unless the DMR agrees to renew them). They can also be cancelled in wide-ranging circumstances, as earlier outlined.

When the MPRDA was being drawn up, the Chamber of Mines stressed that it would be unfair and unwise to transfer private ownership rights to the state without compensation –

especially given the vast sums that many mining houses had already invested in the industry. But the government denied that any expropriation would occur, saying mining companies would be able to convert their existing rights and continue with their operations in much the same way as before. A compromise provision was thus included (as part of the MPRDA's 'transitional arrangements'), under which compensation is available to those who can prove the expropriation of their property under the statute.

The Pretoria high court ruled that expropriation had occurred, as it did not matter that the state's powers were termed 'custodianship' rather than ownership.

Since the mining industry's value had been put at R750bn in 2002, substantial claims might have been anticipated under this clause. Thus far, however, only one expropriation case has been brought before the South African courts. The *Agri SA* case, as it is known, began in 2010 when a company called Sebenza (Pty) Ltd bought an unused coal mining right for R1m. When the MPRDA came into effect in 2004, Sebenza had one year to convert this old-order right into a new-order one. However, the company could not afford the R1.5m application fee, which meant its old-order right 'ceased to exist' a year later. Sebenza sued for compensation and Agri SA – a lobby group for commercial farmers, many of whom previously owned the mineral resources beneath their land – took over Sebenza's claim and brought it before the North Gauteng High Court as a test case on the consequences of the MPRDA.

Handing down judgment in 2011, the Pretoria high court found that Sebenza's ownership rights had been 'legislated out of existence' under the MPRDA. Sebenza had lost all the competencies of ownership it had previously enjoyed, while the statute had given the minister substantially similar rights. The state had thus acquired 'the substance of the property rights of the erstwhile holder'; and it made no difference that the state's competencies were termed 'custodianship' rather than ownership. Expropriation had occurred, for which the former owner was entitled to R750 000 in compensation.

On appeal, Chief Justice Mogoeng ruled that 'the assumption of custodianship' by the state did not amount to expropriation, so no compensation was payable.

This ruling, however, was set aside by the Constitutional Court in April 2013. Handing down the majority judgment, Chief Justice Mogoeng Mogoeng agreed that Sebenza had suffered a 'compulsory deprivation' of its mining right and that the 'custodianship' of this resource was now vested in the state. However, said Chief Justice Mogoeng, 'the assumption of custodianship' did not amount to expropriation because it did not make the state the owner of the right in issue. Added the chief justice: 'Whatever "custodian" might mean, it does not mean that the State has acquired and thus become the owner of the rights concerned.' This in turn meant that no expropriation had occurred and no compensation was payable.

The main judgment seems to lay down a new legal principle: that the assumption of custodianship by the state does not amount to expropriation. However, the chief justice also took pains to emphasise that he was dealing solely with the facts before him, rather than 'deciding definitively that expropriation is...incapable of ever being established' under the MPRDA. Two separate minority judgments further stressed (in the words of Justice Edwin Cameron) that it

was 'inadvisable to extrapolate an inflexible general rule of state acquisition as a requirement [for expropriation] in all cases'. One of these minority judgments also warned against the chief justice's approach, saying it could lead to 'the abolition of the private ownership of all property' without compensation. 'Any legislative transfer of property from existing property holders' would no longer be 'recognised as expropriation' if it was 'done by the state as custodian of the country's resources', it cautioned.

Despite these warnings, the government now seems intent on turning Chief Justice Mogoeng's majority ruling into a general principle of law. This is evident, in particular, in the definition of expropriation that was belatedly inserted into the Expropriation Bill of 2015 in the final stages of the Bill's adoption by the National Assembly. (Since then, the Bill has been endorsed by both houses of parliament, but Mr Zuma has not yet signed it into law. This is largely because the legislative process in the National Council of Provinces was clearly flawed and has been queried by the president, putting the Bill's enactment on hold.)

Despite these warnings, the government now seems intent on turning Chief Justice Mogoeng's majority ruling into a general principle of law.

The Bill defines expropriation as the 'compulsory acquisition of property by...an organ of state'. Though this wording may seem innocuous, it will effectively preclude the payment of any compensation for 'indirect' or 'regulatory' expropriations. Regulatory expropriations occur when the government does not itself take ownership of property, but its regulations deprive owners of many of the powers and benefits of ownership they would normally enjoy. Hence, if significant price and export controls are imposed on 'designated' and 'strategic' minerals under the MPRDA Amendment Bill of 2013, as earlier described (see *Beneficiation requirements*, above), this will give rise to regulatory expropriations. The mining companies which have extracted the relevant minerals will not lose ownership to the government, but could be compelled to sell their minerals at 'developmental' prices set by the state, rather than at market prices. But mining companies will not be able to obtain compensation for any resulting losses, as these regulatory interventions will fall outside the definition of expropriation in the Bill.

If the Expropriation Bill is signed into law in its current form, regulatory expropriations of this kind are thus likely to proceed. The government could also expropriate mining land, mining rights, and other mining assets in return for compensation well below their market value – as this is what the Expropriation Bill explicitly allows. In addition, the DMR could effectively nationalise mining land and mining rights by taking 'custodianship' of them and then refusing to pay any compensation – as the majority judgment in the *Agri SA* case arguably permits.

Under the Expropriation Bill, the government could also expropriate mining land, mining rights, and other mining assets in return for compensation well below their market value.

Whether the ANC plans to nationalise the mines in these or other ways remains uncertain. However, its junior wing, the ANC Youth League, has long been pushing for mine nationalisation. So too have the Economic Freedom Fighters (EFF), led by Julius Malema, a former Youth

League president. The government has also seemingly prepared the way for the implementation of the Youth League's demands by:

- terminating its bilateral investment treaties (BITs) with the United Kingdom and 12 European countries, so putting an end to treaty provisions with these nations that barred nationalisation and expropriation, whether direct or regulatory, without 'prompt, adequate and effective compensation';
- adopting the Protection of Investment Act of 2015 (which was signed into law in December 2015, but has yet to be made operative), which was supposed to 'codify' the standard provisions in these BITs but in fact includes no meaningful protections for investors at all; and
- putting forward a draft bill aimed at establishing the state mining company, the African Exploration Mining and Finance Corporation, as a separate legal entity with new powers (rather than as an off-shoot of the state-owned Central Energy Fund, as now).

The Youth League demands mine nationalisation to comply with the Freedom Charter of 1955 and give black South Africans 'economic freedom' from white domination.

The Youth League's demands for mine nationalisation go back to the start of the Zuma administration in 2009. The league insisted that nationalisation of the mines was required not only by the Freedom Charter of 1955 (the ANC's self-proclaimed policy 'lodestar'), but also so as to give black South Africans 'economic freedom' from white domination. The league thus called for the establishment of a state mining company that would own at least 60% of all new mining investments. In existing mines, said the league, the state should own a 30% stake, which would rise to 60% as mining rights came up for renewal. No compensation would be paid for unprofitable or highly indebted mines, or for those where major labour retrenchments had taken place, it stressed.

In 2010, largely at the Youth League's insistence, the ANC agreed to investigate the merits of mine nationalisation so that informed decisions could be made at its pending policy and national conferences (to be held in June and December 2012, respectively). This investigation culminated in March 2012 in the publication of a policy discussion document entitled 'State Intervention in the Mining Sector (SIMS)'. This document advised against nationalisation, as compensation payments could easily amount to an unaffordable R1 trillion under South Africa's BITs with mainly European countries. (Since then, of course, these BITs have all been terminated, but existing investments nevertheless remain protected by the 'sunset' clauses in these treaties for periods ranging from ten to 20 years.) Instead, the SIMS document recommended an increased role for a state mining company, a renewed focus on beneficiation, and a new 50% tax on 'windfall' profits.

The SIMS document recommended an increased role for a state mining company, a renewed focus on beneficiation, and a new 50% tax on 'windfall' profits.

The ANC's policy conference in June 2012 endorsed most of the recommendations in the SIMS report. It rejected wholesale nationalisation as a policy option but decided in favour of 'strategic nationalisation on the balance of evidence'. (One delegate said this meant that

only the profit-making mines would be nationalised, not the loss-making ones.) The conference also urged a bigger role for the state mining company and increased state control over 'strategic' minerals, such as coal and iron ore, to ensure their supply at developmental prices to state-owned enterprises and downstream industries. Two other possibilities were also mooted: first, that the BEE ownership requirement should be raised from 26% to 30% and, second, that the government should be given its own 30% stake in mines. This approach, if implemented, would bring combined BEE and state ownership to 60%.

At its national conference at Mangaung in December 2012, the ANC skirted around the issue of mine nationalisation, instead endorsing many of the proposals in the SIMS document. The conference stressed that 'state intervention with a focus on beneficiation for industrialisation' was urgently required. To this end, the 'targeted management' of minerals exports was needed. The state mining company would also need to be strengthened significantly, while the state would take steps to 'capture an equitable share of mineral resource rents via the tax system'. Included within the resolutions adopted was a long list of the minerals the ANC regarded as 'strategic and important assets', suggesting that future state controls were likely to be extensive.

The 2013 Bill obliges the minister to 'regulate the mining industry to meet national development imperatives' and promote beneficiation.

Ten days later, an amendment bill along these lines was tabled for public comment. Though various changes to the text have since been made, the current MPRDA Amendment Bill of 2013 remains much the same in many ways. In keeping with the Mangaung resolutions (and as earlier described), the Bill obliges the minister to 'regulate the mining industry to meet national development imperatives'. It also empowers him to impose price and export controls on minerals identified by him as 'designated' or 'strategic'.

Since Mangaung, many of the steps needed to implement the SIMS document – or to embark on a wider process of mine expropriation or nationalisation – have quietly been taken. Overt demands for nationalisation have seldom been voiced, but the issue has by no means gone away. The demand for mine nationalisation has also resurfaced in 2016, with student activists demanding 'nationalisation for free education' in February this year and former Cosatu president Zwelinzima Vavi adding in September: 'We should by now have nationalised all these mines and put them under the democratic control of the working people of this country, so that they can be used to ensure that education is accessible.'

Overt demands for nationalisation are seldom voiced, but the issue has by no means gone away. Recently, the Youth League has returned to this demand.

Also in September, the Youth League returned to this theme, saying there had long been a 'strategic need for the nationalisation of mines'. It demanded to know when the bill establishing the state-mining company would be adopted by Parliament, adding: 'As soon as it is operational, [this company] must take up ownership and control of [the] greater mines in the country.' The league also urged a further amendment to the MPRDA, under which new mining rights would be issued 'with the condition that the state mining company will own 51% as custodian for the people of South Africa'. According to the league, 'select strategic mineral properties must also be reserved for the state mining company'.

The Youth League's demands tend to be dismissed by many as little more than political rhetoric. They are nevertheless consistent with many of the policy shifts the government has recently made, from the MPRDA amendments to the Expropriation Bill, the termination of the European BITs, and the Investment Act. The bill establishing the state mining company as a separate legal entity is also important here. Under that bill, the stated objects of the corporation will be to 'give effect to state participation' and 'drive the nation's developmental imperatives through mining'. To these ends, it will acquire mining rights from the DMR, undertake its own mining operations, and 'acquire shares or other interests' in companies which are already engaged in mining. Its sole shareholder will be the state, and it will operate under the control of the mining minister at all times.

The government has previously attempted to 'exempt' African Exploration from having to comply with the MPRDA, and could try to do the same again in the future.

Pending the enactment of this bill, South Africa's state mining company, the African Exploration Mining and Finance Corporation, will continue as a subsidiary of the Central Energy Fund, a state-owned enterprise. In February 2011 African Exploration launched its first mining project at the Vlakfontein coal mine near Ogies (Mpumalanga). Speaking at the launch, Mr Zuma stressed that 'the role of the state cannot be merely confined to that of a regulator' and that the company had 'a critical role to play in the state's efforts to strategically manage [the country's] mineral resources'.

Private sector objections to African Exploration have thus far been muted, though the Chamber of Mines has stressed the need for the minister to ensure 'a level playing field' as between African Exploration and its private-sector competitors. But, as mining expert Peter Leon has noted, fairness is difficult to achieve when the state mining company can rely on taxpayer revenue for funding and on a fellow state entity (the DMR) to grant it mining and prospecting rights. In addition, the government has previously attempted to 'exempt' African Exploration from having to comply with the onerous requirements of the MPRDA. In 2011 the threat of litigation forced it to withdraw a regulation to this effect, but it may attempt to reinstate this exemption once the state mining company bill has been enacted.

Reforms required

International experience shows that, where a state-owned mining company exists, it must be subject to the same rules as everyone else. It must not be given preferential access to mining rights or other permits, and must be subject to the same fiscal regime and auditing requirements as other companies. In practice, however, this is difficult to achieve, for the government (as referee) has great scope to give preference to the government (as player) – and especially so where mining legislation is ambiguous and its administration opaque.

International experience also shows that state mining companies generally fail, usually managing to produce only a fraction of what privately-owned companies do.

International experience also shows that state mining companies generally fail, usually managing to produce only a fraction of what their privately-owned predecessors or competitors are able to achieve. Key reasons for these failures are poor management and mounting

inefficiency, the weakening of competition, and difficulties in raising funds – especially where governments face many other demands on the public purse. The most important obstacle is usually a lack of good governance: such companies tend to be captured by small and privileged elites, which use them for their own gains rather than in the national interest or to help the poor. Often these elites use state mining companies to conceal mining revenues and siphon these off to individual bank accounts abroad.

Nationalisation achieved in other ways, via the uncompensated seizure of mining companies and their assets, has also generally failed to boost production, increase state revenues, help the poor, or reduce inequality. The same underlying factors are generally to blame, for nationalisation reduces efficiency, erodes competition, hampers funding, and works to the benefit of only a small elite.

Nationalisation reduces efficiency, erodes competition, hampers funding, and works to the benefit of only a small elite, as the experience of Zambia and Chile shows.

That nationalisation does not work well is demonstrated by key differences in the economic performance of Zambia and Chile. Both are important copper-producing countries, with populations and land areas of much the same size. But Zambia nationalised its copper industry in 1973, whereas Chile liberalised its mining regime at much the same time by adopting clear, certain, and stable mining rules similar to those in Botswana's Mines and Minerals Act.

In 1973 Zambia's copper mines employed some 48 000 people and produced some 720 000 tonnes of copper, amounting to 15% of the global total. But after its copper mines were nationalised that year, production showed a steady decline. By 2000, when the mines were privatised again, production had fallen to 257 000 tonnes and employment to 21 000. Real GDP per head had also dropped sharply: from $1 455 in 1976 to $892 in 2000, when the cost to the state of running the copper mines was $1m a day. As the Brenthurst Foundation reports: 'Nationalisation of the mines is calculated to have cost Zambia $45 billion in production losses, more than the total in aid received over the period. If Zambia had maintained its 1970 share of global copper production, it would now be producing 2.7 million tonnes a year.'

'Nationalisation of the mines is calculated to have cost Zambia $45 billion in production losses, more than the total in aid received over the period' from 1963 to 2000.

The privatisation of Zambia's copper mines in 2000 helped bring in fresh investment, which in turn raised employment to 65 000 in 2014 and pushed production up to some 700 000 tonnes that year. However, this tonnage was still less than the 1973 total (720 000 tonnes) and amounted to less than 4% of the global total.

Chile, by contrast, embarked in the 1970s on free market reforms aimed at reducing state control and attracting private investment. Though it still has a state copper mining company (Codelco), the country's mining law reforms have helped promote an upsurge in investment in the copper sector.

In this new policy environment, Codelco's production has doubled from what it was 20 years ago. But Codelco's achievements are far outstripped by those of private mining companies, which have helped bring overall copper production up to 6 million tonnes. Of this total,

two thirds is produced by the private sector. Writes the Brenthurst Foundation: 'In 1970 Chile produced the same amount of copper as Zambia; four decades later it produced eight times more.'

Mine nationalisation has helped to keep Zambia mired in poverty, while Chile has witnessed a great leap forward in economic growth and individual prosperity, as shown in *Table 3*, below:

Table 3: Similarities and differences between Zambia and Chile

Key points of similarity/difference	*Zambia*	*Chile*
Land area in sq km	752 614	755 839
Population	16.4m	17.6m
GDP (2011, USD)	$27bn	$258bn
Copper production (1970, tonnes)	684 000	686 000
Copper production (2012, tonnes)	675 000	5 370 000
Poverty (% below poverty line)	61%	15%
Extreme poverty (%)	42.3%	2.8%
Life expectancy at birth	49 years	79 years
Infant mortality (per 1000 live births)	53	8
Child malnutrition (% under-fives)	15	1

Source: The Brenthurst Foundation, *'The Zambezi Protocol: Result of a dialogue on natural resource policy in Africa'*, 22-24 April 2016, May 2016, p9

The message from these figures is clear. If the South African government wants greater prosperity, less poverty, lower infant mortality, and increased longevity for its people, it needs to follow the policy path pursued since the 1970s in Chile, not Zambia. Mine nationalisation in South Africa will not bring the benefits that Cosatu, the Youth League, and the EFF claim. On the contrary, any such step will reduce mining investment, production, employment, and tax revenues. It could also freeze investment in all sectors of the economy and push the rand into free fall. Poverty and inequality will then grow, leaving all but a small political elite worse off by far.

Mine nationalisation in South Africa will not bring the benefits that Cosatu, the Youth League, and the EFF claim, but rather leave most people worse off.

Follow Botswana's mining law for growth and prosperity

Botswana's mining regime is not without fault. It lacks clear provisions on the granting of mining licences for diamonds, which essentially depend on the agreements reached between applicants and the Botswana government. When diamonds were discovered there in the 1960s, the mining company established to exploit the country's new major source of mineral wealth, Debswana, initially had a 15% stake for the Botswana government, while the remaining 85% was held by De Beers. However, by 1974 the government's stake had been increased to 50%.

In 2012, as part of a deal struck around the renewal of the mining licences for two giant diamond mines, De Beers agreed to shift its diamond sightholder sales from London to Botswana's capital, Gaborone. This move is intended to stimulate not only the local selling of

rough diamonds but also their sorting, cutting, and polishing within Botswana. But Botswana's infant enterprise cannot easily compete with the established diamond cutting industries in Belgium, Israel, China, and India. In India, for example, the city of Surat has many years of experience, much lower costs, and nearly a million workers involved in the diamond industry, while Botswana has little comparative advantage. The costs of cutting and polishing are thus some $45 per carat in Botswana, versus $10 per carat in India. (However, Botswana is three times cheaper than South Africa, which has encouraged the relocation to it of diamond businesses that used to be based here.)

South Africa urgently needs to go back to the drawing board. It should follow the example of Botswana in bringing its mining law into line with international best practice.

At the same time, Botswana has got much of its mining law right. Its rules for the granting and cancellation of mining licences are certain, clear, and stable. It does not impose BEE, beneficiation, or onerous socio-economic conditions on mining investors. It has not threatened the mining industry with nationalisation or expropriation, whether direct or indirect. It has avoided corruption and other aspects of the resource curse, and generally used its mining revenues well to promote growth and increase prosperity. Against this background, it is not surprising that Botswana does so much better than South Africa on the Fraser mining survey, or that its mining industry is expanding, rather than largely stagnating.

The issues canvassed here – the granting and cancellation of mining rights, beneficiation requirements, and state attempts to own or control the mining industry – are not the only ones that need to be considered. However, space constraints do not allow further analysis of what should be done to empower the disadvantaged in far more effective ways than the ones now being used. They also do not allow proper consideration of other important issues, ranging from environmental, labour, and safety challenges to the optimum fiscal regime and dispute resolution mechanisms. All these issues will thus be analysed in future policy papers.

On the issues canvassed here, however, it is clear that South Africa urgently needs to go back to the drawing board on its mining regime. It would also be well advised to follow the example of its Botswana neighbour, which offers a sound way to bring its mining law into line with international best practice.

— Anthea Jeffery

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