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Greater transparency in commodity markets

Note by the UNCTAD secretariat

Summary

In this background note, issues related to transparency in commodity markets are reviewed. The need for transparency is highlighted as a precondition for accountability and good governance of the commodity sectors. Transparency can help to prevent corruption, mismanagement, loss of public revenue and illicit financial flows from commodity-dependent developing countries. In the note, it is argued that improving transparency in commodity markets requires a joint and coordinated effort between commodity-dependent developing countries and developed countries. In this regard, it is crucial that commodity-dependent developing countries, together with development partners, build the capacity that is required to ensure transparency and discourage illicit financial flows. Also, participation in international and regional initiatives, as well as application of standards and certification schemes, can help to strengthen transparency. Furthermore, promoting the availability of market information contributes to transparency. Technology can also play a role, particularly in terms of product traceability and improving the market access of smallholder farmers.

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Introduction

1. Paragraph 208 of the Accra Accord (TD/442) gives a mandate to the Trade and Development Board of the United Nations Conference on Trade and Development (UNCTAD) to establish a multi-year expert meeting on commodities and development. The mandate was reiterated in paragraph 17 of the Doha Mandate (TD/500/Add.1), extending it for the period between 2013 and 2016, and in paragraph 100 (s) of the Nairobi Maafikiano (TD/519/Add.2), adopted at the fourteenth session of the Conference, which further extended the mandate through 2020. The current meeting is the twelfth session of the Multi-year Expert Meeting on Commodities and Development.

2. The importance of transparency for good governance of commodity markets is highlighted in this background note. In this sense, the note is a response to paragraph 55 (b) of the Nairobi Maafikiano in which UNCTAD is called upon to "undertake research and analysis and provide technical assistance on the changing international trade landscape, including identifying means of stimulating economic diversification, reducing trade costs and promoting value added production, including in global value chains for goods and services, while addressing transparency, social and environmental responsibility and their potential development impacts". Furthermore, the decision of the Trade and Development Board at its sixty-fifth session to include greater transparency in commodity markets as one of the main topics of the twelfth session of the Multi-year Expert Meeting on Commodities and Development is implemented through the background note.[1]

3. The focus of the background note is on transparency as a basis for accountability and good governance. In this context, transparency is required at all stages of commodity value chains as well as for the sustainable management of commodity revenue. Furthermore, in the note, it is argued that transparency is a joint challenge of commodity-dependent developing countries and developed countries. In the note, several entry points are identified to strengthen transparency in commodity sectors, such as through regional and international initiatives and standards and certification schemes, as well as the promotion of commodity market information.

I. Transparency in commodity markets: A common challenge for developing and developed countries

A. The importance of transparency

4. While there is no generally agreed definition, transparency characterizes a situation where the public has comprehensive and timely access to information and data that are necessary to hold policymakers, institutions and enterprises accountable for their actions. In this sense, transparency is not an end in itself but rather a precondition for accountability and good governance in a broader sense. The absence of transparency enables corruption, illicit business practices and unethical behaviour.

5. Commodity markets often lack transparency, which has negative consequences particularly for developing countries that depend on the export of commodities, such as oil, minerals and agricultural goods. In many of these countries, commodity revenue is essential to fight poverty and fund development programmes. For instance, 64 per cent of developing and transition economies are classified as commodity dependent by UNCTAD.[2] In these countries, export revenues from the commodity sector represent at least 60 per cent of total merchandise export revenues. Low-income countries, 91 per cent of which are commodity-dependent developing countries, are particularly prone to commodity dependence. In many commodity-dependent developing countries, transparency needs to be strengthened to

[1] TD/B/65(2)/4, para. 82 and annex II.

[2] UNCTAD, 2019, *State of Commodity Dependence 2019* (United Nations publication, Sales No. E.19.II.D.8, Geneva).

ensure that the gains of resource exploitation are broadly shared and contribute to sustainable development.

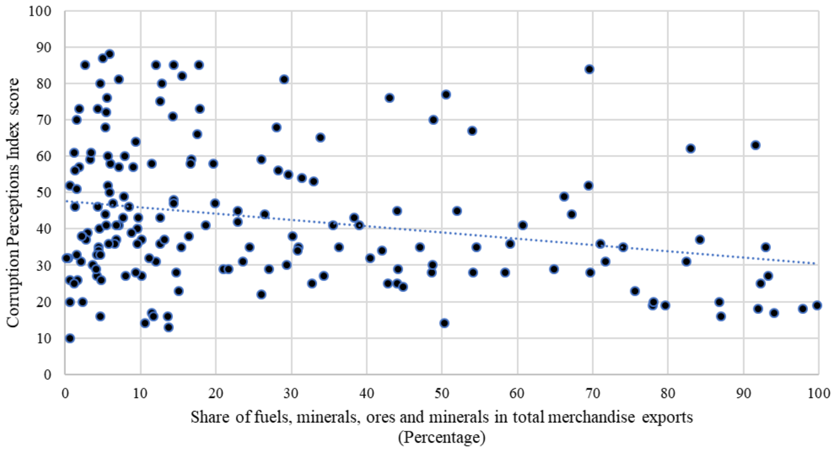
6. Transparency is an issue that concerns the entire commodity value chain, including the stages of exploration, production, processing and trading. At each stage of the value chain, transparency can help to reduce the scope for corruption and mismanagement, improve governance and result in fairer sharing of commodity revenue. In this context, strengthening transparency requires a common effort by Governments, civil society and businesses in the commodity sector.

B. Transparency along commodity value chains

7. Transparency is a key aspect of good governance for all commodity sectors. However, the extractive industries, i.e. the oil, gas and mineral sectors, are particularly prone to a lack of transparency. For instance, the oil, gas and mineral sectors often feature discretional decision-making at high levels of Government, where institutional oversight is limited. Also, mining operations are technically complex and frequently concentrated in remote areas, which renders public scrutiny difficult.

8. A lack of transparency creates an environment that favours corruption and thus constitutes an impediment to growth and development for commodity-dependent developing countries that depend on the extractive industries. According to one Organization for Economic Cooperation and Development (OECD) assessment, the oil and mining sectors accounted for the highest share (19 per cent) of foreign bribery cases that were completed between the entry into force of the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions in 1999 and 2014.[3] Also, on the Corruption Perceptions Index of Transparency International (where a high score implies a perception of low levels of corruption), the 20 United Nations Member States with the highest combined share of fuels, ores and metals in their merchandise exports in 2018 have an average score of 30.5, significantly below the average for all countries of 43.0. Figure 1 illustrates the negative relationship between the score on the Corruption Perceptions Index and the level of dependence on the extractives sector.

Figure 1
Extractive industries and perceived corruption



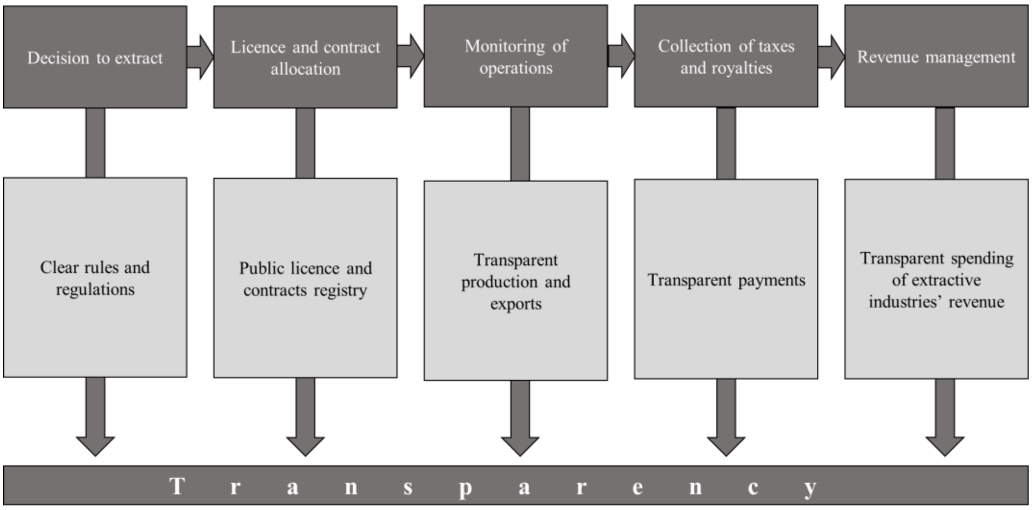
Sources: UNCTADstat database for trade data; Corruption Perceptions Index score of Transparency International (available at https://www.transparency.org/cpi2018).

Notes: Calculation based on 176 United Nations Member States that have data for 2018 in both the UNCTADstat database and the Corruption Perceptions Index. A lower score on the Corruption Perceptions Index means a perception of higher levels of corruption. Fuels, minerals, ores and metals includes Standard International Trade Classification sections 3, 27, 28, 68, 667 and 971.

[3] OECD, 2014, *OECD Foreign Bribery Report: An Analysis of the Crime of Bribery of Foreign Public Officials*, OECD Publishing, Paris.

9. The issue of transparency arises throughout the value chain for extractive industries. There are different conceptual frameworks for the analysis of oil, gas and mining value chains that either follow the chronological order of individual projects (exploration – development – production – decommissioning) or focus on associated policy areas for the sustainable management of the extractives sector (decision to extract – licensing – monitoring operations – collecting taxes and royalties – revenue management). This background note takes the latter approach since it lends itself better to the analysis of policy design and implementation, is widely used in the relevant literature and has been adopted by organizations focusing on transparency and governance in the extractive industries such as the Extractive Industries Transparency Initiative and the Natural Resource Governance Institute. Figure 2 provides a graphical representation of main policy areas of oil, gas and mining value chains.

Figure 2
Transparency and the value chain for extractive industries



Source: UNCTAD secretariat.

10. Transparency in the extractives sector begins with clear rules and regulations for decision-making, including on whether or not to extract a newly discovered resource. In this context, it is important that expected revenue and other benefits, as well as expected costs and risks, are known, carefully analysed and accounted for in decision-making. This includes an analysis of potential environmental, health and social impacts, particularly in and around the communities where extractive activities would take place. Transparency requires that both costs and benefits of potential extractive projects are subject to a broad-based public debate involving all relevant stakeholders.

11. In the mining sector, one precondition for a meaningful public discussion among stakeholders is the availability of detailed information regarding the resource. In this regard, it is crucial for Government, civil society and investors in the mining industry to have a clear picture of exploration results, including key indicators of resources or reserves such as quantities and ore grades. This allows governments to better anticipate future revenue, informs civil society of potential mining activities and reduces risk and uncertainty for potential investors. To improve transparency in exploration results, many countries have developed reporting and classification standards. At the international level, there are two main initiatives to develop common and comparable reporting standards, namely the Committee for Mineral Reserves International Reporting Standards and the United Nations Framework Classification for Fossil Energy and Mineral Reserves and Resources. The Committee for Mineral Reserves International Reporting Standards is an international advisory body that has developed a reporting template for solid mineral reserves and resources to which many national reporting regulations have been aligned. Therefore, the Committee's reporting principles are mandatory for mining companies listed on many stock

exchanges.[4] The United Nations Framework Classification for Fossil Energy and Mineral Reserves and Resources, developed by the Economic Commission for Europe, provides a classification framework that applies to reserves and resources of minerals, fossil energy, nuclear energy and renewable energy.[5] For solid mineral resources, there exists a bridging document that allows for classification of estimates based on the definitions of the Committee for Mineral Reserves International Reporting Standards, within the code system United Nations Framework Classification for Fossil Energy and Mineral Reserves and Resources.

Contract transparency

12. Transparency in licensing and contract allocation is another key element of good resource governance. This includes public information regarding rules, procedures and criteria for the award of licences, permits and contracts. In this regard, it is important to note that disclosing agreements between a Government and companies can be beneficial for both parties. In particular, contract transparency can strengthen a company's social licence to operate, i.e. the public acceptance of the company's business activities. Similarly, contract transparency can contribute to citizens' trust in the Government's good governance of the extractives sector.

13. Contract transparency in the extractive industry encompasses public disclosure of all agreements between the Government and companies in the oil, gas and mining sector. This includes licences and permits for exploration or exploitation of deposits, environmental impact assessments and agreements regarding environmental monitoring, health impact assessments, social impact assessments and any other agreements, including those on local content requirements.

14. A growing number of countries have established practices or introduced laws that promote the disclosure of contracts. For instance, a Natural Resource Governance Institute study in 2017 identified 22 countries that have a law or policy that requires some level of contract disclosure in the extractives sector.[6] A public registry of licenses and contracts for mineral exploration and production can enhance transparency and facilitate access to information for all stakeholders, including civil society groups. Several countries have launched such online registries for resource contracts, including Colombia, the Democratic Republic of the Congo, Guinea, the Philippines, Sierra Leone and Tunisia. An online repository that collects publicly available contracts from the oil, gas and mineral sectors contains more than 2,000 documents for 93 countries and 53 resources.[7] The table below shows a list of the 15 countries with the highest number of publicly available contract documents for oil, gas and mining projects. This list includes 9 countries in Africa, 4 in Latin American countries and 2 in Asia.

Publicly available contract documents for oil, gas and mining projects

Country	*Number of disclosed documents*
Tunisia	297
Peru	271
Colombia	266
Democratic Republic of the Congo	147
Mexico	136

4 Current members represent most European countries, as well as Australia, Brazil, Canada, Chile, Colombia, India, Indonesia, Kazakhstan, Mongolia, the Russian Federation, South Africa, Turkey and the United States of America.

5 The United Nations Framework Classification for Fossil Energy and Mineral Reserves and Resources has been endorsed by the 56 member States of United Nations Economic Commission for Europe.

6 Pitman R and Hubert D, 2017, *Past the Tipping Point? Contract Disclosure within EITI [Extractive Industries Transparency Initiative]*, Natural Resource Governance Institute. Available at https://resourcegovernance.org/analysis-tools/publications/past-tipping-point (accessed 18 December 2019).

7 Based on data from https://resourcecontracts.org/ (accessed on 14 November 2019).

Country	*Number of disclosed documents*
Philippines	101
Guinea	86
Iraq	84
Zambia	71
Senegal	52
Bolivia (Plurinational State of)	50
Ghana	40
Liberia	37
Congo	28
Mauritania	26

Source: Based on data from https://resourcecontracts.org/ (accessed 14 November 2019).

15. The private sector can also contribute to contract transparency in the extractives sector. For example, the Extractive Industries Transparency Initiative EITI lists 62 supporting companies on its website, including some of the world's largest oil, gas and mining enterprises.[8] A few companies make contract agreements available on their own websites. For example, the website of the oil and gas exploration and production company Kosmos Energy, based in the United States of America, shows petroleum agreements and production sharing contracts with Governments of nine African countries and one South American country.[9] Also, Tullow Oil, based in the United Kingdom of Great Britain and Northern Ireland, makes available its production sharing agreements with Ghana and Guyana on its website.[10] A significant share of companies in the extractives sector appears to support contract transparency. For instance, an Oxfam survey in 2018 showed that more than half of the supporting companies of the Extractive Industries Transparency Initiative and members of the International Council on Mining and Metals assessed supported contract disclosure in some form.[11]

16. Monitoring of operations is crucial for the transparency in the extractives sector. Good governance requires that Government monitor operations of oil, gas and mining companies with regard to production and exports, as well as health, safety and environmental practices. This includes regular verification that the terms stipulated in licences and other contractual agreements are met by companies. For instance, a Government needs to be able to verify through sampling and testing the accuracy of mining companies' statements on the value of exported minerals. In the absence of effective monitoring, there is the risk of undervaluation by mining companies and loss of government revenue.[12] In this regard, it is important that roles and responsibilities for monitoring of operations are clearly assigned to government agencies and authorities. Furthermore, for monitoring to be effective, responsible agencies have to be equipped with the necessary capacity and resources to fulfil their mandate.

Payment and revenue transparency

17. Payment and revenue transparency lie at the very core of good resource governance. In order to assess whether a country is receiving a fair share from the exploitation of its resource wealth, detailed information on payments and revenue from the resource sector needs to be available. In this regard, the public should have timely, accurate and comprehensive access to information on payments for licence fees, taxes and royalties, and dividends, as well as in-kind payments such as production shares transferred to Government

[8] See https://eiti.org/supporters/companies (accessed 14 November 2019).

[9] See https://www.kosmosenergy.com/transparency/ (accessed 14 November 2019).

[10] See https://www.tullowoil.com/sustainability/equality-and-transparency/transparency-of-tax-and-petroleum-agreements (accessed 14 November 2019).

[11] Oxfam International, 2018, Contract disclosure survey 2018, Oxfam Briefing Paper (May).

[12] Readhead A, 2018, Monitoring the value of mineral exports: Policy options for Governments, International Institute for Sustainable Development and OECD.

or a State-owned enterprise. Also, information on revenue that the government or State-owned enterprises generate from selling oil, gas or minerals to commodity trading companies should be made public, thus facilitating scrutiny and accountability. Such commodity trading represents significant shares of commodity revenue for many countries. For instance, oil sales account for more than two thirds of total government revenues in Azerbaijan, the Congo, Iraq and Nigeria.[13]

18. Furthermore, information regarding financial incentives, such as tax holidays, tax or royalty reductions, accelerated depreciation, investment allowances that are provided to extractive industries, are part of payment transparency as such incentives might be linked to significant foregone revenue for Government. For instance, 12 of 21 countries in the tax incentives database of the Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development offer tax holidays.[14] In this regard, potential behavioural responses to financial incentives, such as companies shifting production and income to tax holidays, also need to be taken into account.[15] Without transparency in incentives, civil society, parliament and other stakeholders cannot make an informed judgement on the contribution of a resource sector to the welfare and development of their country.

Illicit financial flows

19. The absence of transparency creates an environment that favours mismanagement and enables unethical business practices that can result in illicit financial flows. Illicit financial flows related to commodity sectors have received increased attention in recent years. While there is no universally agreed definition of illicit financial flows, they are often described as money that is illegally earned, transferred or used and that crosses borders.[16]

20. Illicit financial flows drain budgets of important resources and are estimated to be larger than ODA flows in some cases. For instance, the High-level Panel on Illicit Financial Flows from Africa estimated illicit financial flows from Africa at $50 billion per year.[17] The importance of illicit financial flows is also evidenced by the related target 16.4 under Sustainable Development Goal 16 to “significantly reduce illicit financial and arms flows, strengthen the recovery and return of stolen assets and combat all forms of organized crime” (A/RES/70/1). Also, the Addis Ababa Action Agenda commits countries to redouble efforts to “substantially reduce illicit financial flows by 2030, with a view to eventually eliminating them” (A/RES/69/313).

21. In the context of commodity markets, transfer mispricing is a key driver of illicit financial flows. Transfer mispricing is a practice whereby intra-firm transactions are conducted at inflated prices instead of being based on an arm’s length principle of reducing taxable profits. The aim of such transactions is to shift profits from high-tax jurisdictions to low-tax jurisdictions in order to reduce taxation. Reducing the scope for this and other methods of tax evasion and avoidance is at the heart of the OECD/Group of 20 Base Erosion and Profit Shifting project. According to the project’s estimates, tax avoidance costs Governments between $100 billion and $240 billion per year, equivalent to 4–10 per cent of global corporate tax revenues.[18]

[13] Poretti P, 2019, Transparency in the first trade, Extractive Industries Transparency Initiative. Available at https://eiti.org/document/transparency-in-first-trade (accessed 20 January 2020).

[14] Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development, 2019, Mining tax incentives database. Available at https://www.igfmining.org/tax-incentives-mining/ (accessed 20 January 2020).

[15] Readhead A, 2018, *Tax Incentives in Mining: Minimizing Risks to Revenue*, International Institute for Sustainable Development and Organization for Economic Cooperation and Development.

[16] See https://developmentfinance.un.org/illicit-financial-flows (accessed 16 December 2019).

[17] United Nations, Economic Commission for Africa, 2015, *Illicit Financial Flows: Report of the High-Level Panel on Illicit Financial Flows from Africa,* Addis Ababa.

[18] OECD, 2015, Taxing multinational enterprises: Base erosion and profit shifting, Policy Brief, October, OECD Publishing.

22. In this context, stemming transfer mispricing requires cooperation between Governments of countries where mining activities take place and Governments of countries where international mining companies are headquartered. This is particularly important since many companies active in the extractive industries in commodity-dependent developing countries are multinational enterprises based in developed countries or, to some extent, other developing countries. For instance, 717 Australian companies in the mining, oil and gas sector had projects in 106 countries, including 34 African countries in 2017.[19] Likewise, 1,364 Canadian mining companies owned $260.1 billion in mining and exploration assets abroad in 2017, including $55.0 billion in South America and $26.3 billion in Africa.[20]

23. In recent years, several laws and regulations aimed at improving transparency in natural resource sectors were introduced in developed countries. For instance, the European Union Directive 2013/50/EU requires companies whose securities are traded within the European Union and that are active in the extractive industry or in logging of primary forest to disclose, on an annual basis, payments made to Governments in the countries where they operate. In Canada, the Extractive Sector Transparency Measures Act came into force in 2015. The law requires companies that are listed on a Canadian stock exchange or do business in Canada to disclose payments made to foreign Governments due to taxes, royalties, fees, production entitlements, bonuses, dividends and infrastructure improvement in the oil, gas and minerals sectors. In the United States, section 1504 of the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 required United States-listed companies to disclose payments to foreign Governments relating to oil, gas and mineral rights. However, the rule[21] implementing this requirement issued by the United States Securities and Exchange Commission was repealed in 2017.[22]

Beneficial ownership

24. Beneficial ownership is an important element of transparency in commodity sectors. The Financial Action Task Force, an intergovernmental organization that develops policies to combat money laundering, defines a beneficial owner as "the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement".[23] Hence, a beneficial owner is the real person owning or controlling a company. In the absence of transparency of beneficial ownership, business can be conducted by anonymous shell companies, which is conducive to corruption, conflicts of interest and tax evasion.

25. In recent years, several countries including commodity-dependent developing countries have anchored requirements for transparency of beneficial ownership in their laws. For instance, Liberia has included a provision that mandates disclosure of beneficial ownership of companies applying for pre-qualification for oil contracts in its law.[24] Countries participating in the Extractive Industries Transparency Initiative are required to publish details of the beneficial owners of companies that operate in the oil, gas and mining

[19] Publish What You Pay Australia, 2017, Abundant resources, absent data: Measuring the openness of Australian listed mining, oil and gas companies on the African continent, London.

[20] Natural Resources Canada, 2019, Canadian mining assets, Information Bulletin, February. Available at https://www.nrcan.gc.ca/mining-materials/publications/19323 (accessed 15 November 2019).

[21] Rule on disclosure of payments by resource extraction issuers (document 81 FR 49359), issued by the Securities and Exchange Commission of the United States of America on 27 July 2016. Available at https://www.federalregister.gov/documents/2016/07/27/2016-15676/disclosure-of-payments-by-resource-extraction-issuers (accessed 22 January 2020).

[22] United States of America, 2017, Public Law 115-4, available at https://www.congress.gov/115/plaws/publ4/PLAW-115publ4.pdf.

[23] Financial Action Task Force, 2012–2019, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation*, Paris, available at www.fatf-gafi.org/recommendations.html (accessed 22 January 2020).

[24] Natural Resource Governance Institute, 2018, Beneficial ownership screening: Practical measures to reduce corruption risks in extractives licensing, Briefing, May.

sectors by 2020. Beneficial ownership registries can also strengthen transparency and reduce the scope for conflicts of interests in commodity sectors and beyond.

Managing commodity revenue

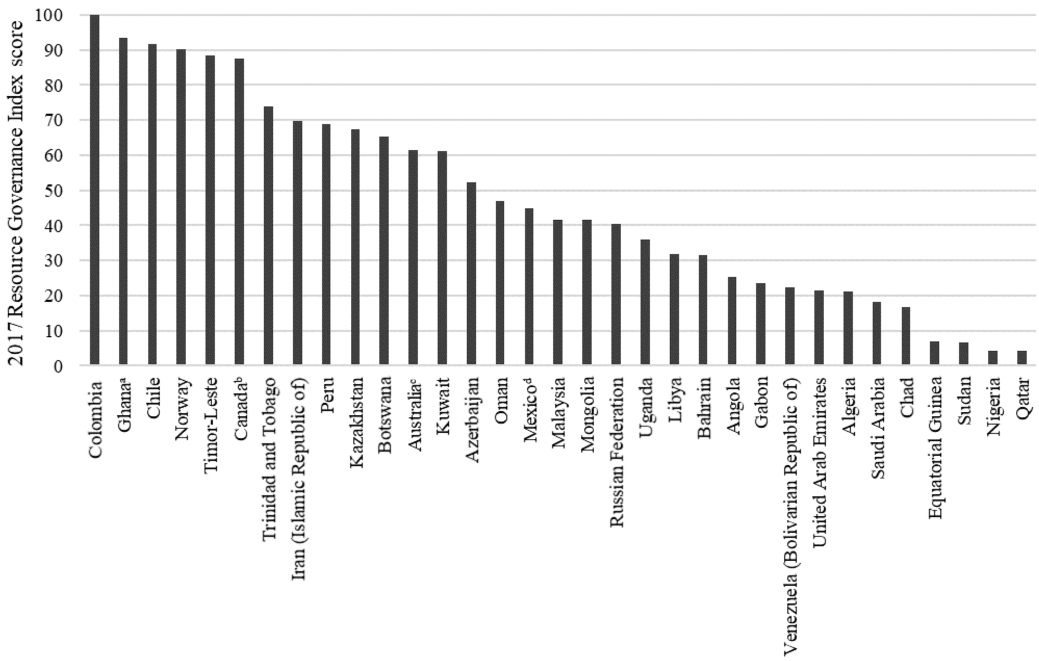
26. The management of commodity revenue is a crucial and challenging task for Governments of commodity-dependent developing countries. Commodity markets are characterized by a high level of volatility, which translates into revenue fluctuations and uncertainty about future revenue flows. In this context, the presence of a well-designed and transparent fiscal policy framework can strengthen the efficiency of public spending. This is reflected, for instance, by the 2019 edition of the International Monetary Fund's Fiscal Transparency Code, which features a new pillar on natural resource revenue management that states that "government revenues from natural resource exploration and extraction activity should be collected, managed and disbursed in an open and transparent manner".[25] In this context, transparency enables public oversight and limits the scope for inefficiency and corruption.

27. When a country draws on its stock of non-renewable resources, such as oil, gas or minerals, to generate revenue, sustainability and intergenerational fairness become important aspects of revenue management. Using part of current commodity revenue to build up other forms of capital, including human capital, physical capital and financial assets, is one way to ensure that revenue flows are sustainable and future generations receive a fair share of a country's commodity wealth.

28. Transparent commodity revenue management also extends to commodity-based sovereign wealth funds. Many resource-rich countries, including commodity-dependent developing countries, have established such funds. Examples include the Revenue Regulation Fund (oil and gas) of Algeria, the Angola Sovereign Fund (oil), the Pula Fund (diamonds) of Botswana, the Savings and Stabilization Fund (oil, gas and mining) of Colombia, the National Oil Fund of Kazakhstan and the Petroleum Fund of Timor-Leste. Commodity-based sovereign wealth funds are only effective and sustainable if they are characterized by transparency, strong governance and inflow/outflow rules that are anchored in a robust fiscal policy framework. For example, the copper revenue-based Economic and Social Stabilization Fund of Chile is generally perceived as a successful example of a commodity-based sovereign wealth fund. The Economic and Social Stabilization Fund works in conjunction with a transparent structural balance rule that shields the budget from copper price volatility but also limits withdrawals from the fund. Of the 33 sovereign wealth funds included in the 2017 Resource Governance Index on the oil, gas and mining sectors, 6 received a good score (defined as more than 75 points), of which 4 are commodity-dependent developing countries. However, all of the sovereign wealth funds rated as failing (fewer than 30 points) were also from commodity-dependent developing countries (figure 3).

[25] International Monetary Fund, 2019, The fiscal transparency code, available at https://www.imf.org/external/np/fad/trans/Code2019.pdf.

Figure 3
Resource Governance Index scores of commodity-based sovereign wealth funds



Source: Based on data from the Natural Resource Governance Institute, 2017 Resource Governance Index.
[a] Oil and gas.
[b] Alberta.
[c] Western Australia.
[d] Oil and gas.

29. Transparency is also an important issue for State-owned enterprises. State-owned enterprises are often large and take key roles in extractives sectors. For example, State-owned enterprise in the upstream oil, gas and mineral sectors control around 80 per cent of global oil reserves.[26] Therefore, corruption in State-owned enterprise can cause particularly high economic damage in addition to undermining public trust in Government. According to an OECD study, State-owned enterprises were involved in 20 per cent of the 131 reported corruption cases in the extractives sector and have elevated corruption risks, as compared to other sectors of the economy.[27] Furthermore, only 9 of 81 State-owned enterprise included in the 2017 Resource Governance Index achieved a good standard of transparency and accountable governance.[28]

C. How to improve transparency in commodity markets

30. Commodity-dependent developing countries can strengthen transparency in commodity sectors through international standards and initiatives. For commodity-dependent developing countries with significant oil, gas and mining resources, the Extractive Industries Transparency Initiative can contribute to improving governance of these sectors. The Extractive Industries Transparency Initiative is a multi-stakeholder initiative launched in September 2002 at the World Summit on Sustainable Development in Johannesburg (South Africa). It provides a standard for transparency and good governance of oil, gas and mineral sectors. Countries implementing the Extractive Industries

[26] International Monetary Fund, 2012, Fiscal regimes for extractive industries: Design and implementation, Policy Paper.
[27] OECD, 2016, *Corruption in the Extractive Value Chain: Typology of Risks, Mitigation Measures and Incentives*, OECD Publishing, Paris.
[28] Natural Resource Governance Institute, 2018, Guide to extractive sector State-owned enterprise disclosures. Available at https://resourcegovernance.org/analysis-tools/publications/guide-to-extractive-sector-state-owned-enterprise-disclosures (accessed 21 January 2020).

Transparency Initiative must fulfil a range of requirements that cover the entire extractives value chain, as well as public revenue management. As of November 2019, there were 52 countries, including 37 commodity-dependent developing countries, implementing the Extractive Industries Transparency Initiative. Among commodity-dependent developing countries, 5 were assessed to have made satisfactory progress and 25 meaningful progress, while 3 were suspended or had made inadequate progress. Furthermore, four commodity-dependent developing countries participating in the Extractive Industries Transparency Initiative had not yet been assessed against the Initiative's 2016 standard.[29]

31. Implementing regional standards and principles such as those of the Africa Mining Vision can also contribute to improving transparency in commodity sectors. The Africa Mining Vision was adopted by African Heads of States at the African Union Summit in 2009. The Africa Mining Vision, complemented by its Action Plan and the African Minerals Governance Framework, aims at transparent, equitable and optimal exploitation of mineral resources to achieve sustainable development in the region.[30] Through country mining visions, the Africa Mining Vision can be adapted and implemented at the national level.

32. For commodity-dependent developing countries that have commodity-based sovereign wealth funds, the so-called Santiago Principles provide 24 voluntary best practice guidelines.[31] One of the key objectives of the principles is to ensure that sovereign wealth funds have in place a transparent and sound governance structure that provides adequate operational controls, risk management and accountability. Commodity-based sovereign wealth funds that have endorsed the Santiago Principles include the Abu Dhabi Investment Authority, the Angola Sovereign Fund, the State Oil Fund of Azerbaijan, the Kuwait Investment Authority, the Libyan Investment Authority, the Pula Fund of Botswana, the Qatar Investment Authority and the Timor-Leste Petroleum Fund.[32]

33. Curbing illicit financial flows related to the commodity sector is an important aspect of promoting domestic resource mobilization in line with the Addis Ababa Action Agenda, as they reduce the public resources available to fund the Sustainable Development Goals. Since opaqueness favours illicit financial flows, strengthening transparency is an important aspect of combating illicit financial flows. Reliable evidence is needed as a starting point for addressing illicit financial flows, which means that methods for measuring illicit financial flows need to be strengthened. Furthermore, coherence and coordination between agencies that combat illicit financial flows need to be improved. Finally, it is crucial that the institutions fighting illicit financial flows at the national level, such as tax authorities, have the means and capacity to do so effectively. For instance, through access to training activities and peer learning, tax investigators can build and strengthen their capacity to assess whether the arm's length principle has been adhered to in transfer pricing of multinational enterprises.

34. Certification schemes to verify the origin of minerals can be an effective way of enhancing transparency in the extractives sector. In particular, traceability is an important aspect of sustainable minerals development in the context of conflict-affected countries. A number of certification standards have been developed for different minerals, regions and mining processes. The Kimberley Process Certification Scheme, established in 2003, was the first certification scheme for the ethical sourcing of minerals. The Kimberley Process Certification Scheme that grew out of United Nations General Assembly resolution 55/56 and aims at preventing conflict diamonds from entering the global diamond market.

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[29] See https://eiti.org/countries (accessed 20 November 2019).

[30] African Union, 2009, Africa Mining Vision, available at https://au.int/en/documents-9 (accessed 21 January 2020).

[31] See International Working Group of Sovereign Wealth Funds, 2008, *Sovereign Wealth Funds, Generally Accepted Principles and Practices – "Santiago Principles"*.

[32] For a list of members of the International Forum of Sovereign Wealth Funds, see https://www.ifswf.org/our-members (accessed 20 January 2020).

35. The OECD Due Diligence Guidance for Responsible Mineral Supply Chains was adopted in 2011 and is based on a multi-stakeholder process, including 11 countries of the Great Lakes Region, as well as civil society, the mining industry and the Group of Experts on the Democratic Republic of the Congo established by the United Nations. The main objective of the OECD guidance is to ensure that companies do not contribute to human rights violations and conflict through their mineral purchases. Originally, the OECD guidance specified tin, tantalum, tungsten and gold as conflict minerals, but later editions have widened the scope to all minerals sourced from conflict-affected and high-risk areas.

36. Several certification schemes and due diligence regulations are based on or draw from the OECD guidance. For example, the United States Securities and Exchange Commission recognizes the OECD guidance as a basis for implementing due diligence in the framework of conflict minerals reporting under the Dodd–Frank Wall Street Reform and Consumer Protection Act (section 1502). Principles of the OECD guidance have also been integrated into the mineral certification scheme of the International Conference of the Great Lakes Region. The International Conference of the Great Lakes Region includes requirements that mines should be conflict free, not rely on child labour and not abuse human rights. The certification process includes mine site inspections, mineral tracking, export certification, minerals tracking database and third-party audits, as well as an independent mineral chain auditor. Mines that meet all criteria are certified or green flagged. Regulation (EU) 2017/821 of the European Parliament and the Council, which was adopted in May 2017 and will enter into force in January 2021, defines supply chain due diligence obligations for European Union importers of tin, tantalum and tungsten, and their ores, and gold originating from conflict-affected and high-risk areas in accordance with the OECD guidance. Various industry standards developed by private-sector associations, such as the Conflict-Free Gold Standard of the World Gold Council and the Chain of Custody Certification of the Responsible Jewellery Council, also draw on the OECD guidance.

37. The availability of market information can also help to promote transparency of commodity markets. One example is the Agricultural Market Information System, which was established by the Group of 20 ministers of agriculture in 2011 as a response to the global food price hikes in 2007/08 and 2010. The Agricultural Market Information System provides data and forecasts of market fundamentals and prices of wheat, maize, rice and soybeans and thus reduces market uncertainty and facilitates policy coordination. Other examples are the Joint Organizations Data Initiative, a platform launched by the Asia–Pacific Economic Cooperation forum, the Statistical Office of the European Communities, the Gas-Exporting Countries Forum, the International Energy Agency, the Latin American Energy Organization, the Organization of the Petroleum Exporting Countries and the United Nations Statistics Division. The Joint Organizations Data Initiative contributes to transparency within the global oil and natural gas markets by making available production, consumption, trade and stocks data in freely accessible databases.[33]

38. Commodity exchanges can be a vehicle to improve market transparency for a range of stakeholders, including smallholder farmers, traders and exporters. Commodity exchanges are regulated marketplaces that fulfil several important functions including the provision of market information by disseminating data on prices, market liquidity, and warehouse stocks. The largest and most sophisticated commodity exchanges outside of developed countries are in emerging economies. These include Brasil, Bolsa, Balcão (Brazil); the Rosario Board of Trade in Argentina; the Multi Commodity Exchange of India and the National Commodity and Derivatives Exchange (India); the Dalian Commodity Exchange, Shanghai Futures Exchange, Zhengzhou Commodity Exchange in China; Bursa Malaysia; and the South African Futures Exchange (South Africa).

[33] See https://www.jodidata.org/.

39. Beyond high-volume futures exchanges, there are several commodity exchanges based in commodity-dependent developing countries that contribute to market transparency by providing spot markets, warehouse receipt systems and other important services. For instance, the Agricultural Commodity Exchange for Africa in Malawi, established in 2006, operates several warehouses and features trade in grains, legumes and nuts. Another example is the Ethiopia Commodity Exchange, established in 2008, which has an electronic warehouse receipt system and offers a spot market for coffee, sesame seeds and other commodities. The East Africa Exchange was established in Rwanda in 2013 and has since expanded operations to Kenya and Uganda. Commodities traded on the East Africa Exchange include beans, maize, rice, soya, sorghum and wheat. The Ghana Commodity Exchange started trading operations in late 2018. Commodities currently traded on the Ghana Commodity Exchange include maize, sesame, sorghum and soybeans. Functioning commodity exchanges in commodity-dependent developing countries can contribute to greater transparency in commodity markets by making prevailing prices and traded volumes known to all market participants. However, it must be noted that certain preconditions including an appropriate regulatory and legal framework and physical infrastructure requirements need to be met for commodity exchanges to be effective and sustainable.[34] While some commodity exchanges based in commodity-dependent developing countries, such as the Ethiopia Commodity Exchange and the East Africa Exchange, have been growing in terms of traded volume and product scope, others have struggled to achieve a sufficient market size.[35]

II. Summary and policy considerations

40. Transparency is the basis for the accountability and good governance of commodity sectors, which is required to ensure that resource exploitation contributes to sustainable development in commodity-dependent developing countries. In this regard, strengthening transparency in commodity markets requires a joint effort by commodity-dependent developing countries and developed countries. Commodity-dependent developing countries need to build institutions and implement rules and procedures that promote transparency and good governance. International and regional initiatives and standard and certification schemes can be effective vehicles for the collaboration and coordination of efforts to improve transparency. In this context, it is essential that transparency rules and standards are applied not only in commodity-dependent developing countries and other resource-rich developing countries from where the bulk of commodities are supplied to global markets, but also in developed countries and emerging economies where many of the companies that dominate global commodity production and trade are headquartered.

41. In addition to formulating rules and regulations, it is crucial for commodity-dependent developing countries to build and maintain the capacity that is required to monitor and enforce them. For example, commodity-dependent developing countries together with development partners need to address capacity requirements to effectively combat illicit financial flows related to commodity markets. This includes building and strengthening of capacity to detect and tackle the transfer mispricing of multinational enterprises. For instance, tax investigators need to be properly trained and enabled to assess whether the arm’s length principle has been applied, which is complicated in many developing countries due to the scarcity of data. In this context, initiatives such as the Platform for Collaboration on Tax, a joint International Monetary Fund, OECD, United Nations and World Bank Group initiative, can help through knowledge- and information-sharing, technical assistance and capacity-building.

[34] UNCTAD, 1997, Emerging commodity exchanges: From potential to success. Report by the UNCTAD secretariat.

[35] Sitko NJ and Jayne TS, 2012, Why are African commodity exchanges languishing? A case study of the Zambian Agricultural Commodity Exchange. *Food Policy*, 37(3):275–282.

42. Finally, commodity-dependent developing countries together with developed countries and the private sector may benefit from evaluating technological options to improve transparency in commodity markets. For instance, electronic warehouse receipt systems and trading platforms can improve the efficiency and transparency of commodity exchanges. Also, mobile technology and blockchain-based systems can help to track commodities or link farmers with marketplaces and service providers. For instance, blockchain technology is used to ensure the traceability of commodities, such as gold, rice and coffee, along supply chains.[36] Also, blockchain-based application have been designed to improve smallholder farmers' access to finance and insurance.[37]

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[36] See https://www.ledgerinsights.com/blockchain-food-traceability-rice-thailand/ and https://www.ledgerinsights.com/douwe-egberts-coffee-traceability-blockchain-farmer-connect/ (accessed 21 January 2020).

[37] See Global Lab for Climate Finance, 2019, Blockchain climate risk crop insurance, available at https://climatepolicyinitiative.org/wp-content/uploads/2019/10/Blockchain_instrument-analysis.pdf.