

# IAN: Managing Tenure Risk

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*In recent years, sectors like mining, energy and agriculture have seen a substantial increase in disputes with local populations over land and resource rights, which threaten the viability of projects. The problem is particularly acute in emerging markets, where 93% of concessions are inhabited. We refer to this problem as “tenure risk”.*

*Conversations with a range of investors and companies indicated that handling this risk was not only impossible using current approaches, but also, that coverage for the risk may well be excluded from standard forms of insurance. Addressing this problem requires close analysis of tenure risk, and better tools for translating those lessons into concrete action. To that end, this document:*

- 1. Explains what tenure risk is and offers objective evidence that the problem is widespread and of increasing frequency, with reported cases increasing by more than 300% since 2003. This is financially meaningful, since more than 54% of tenure risk cases we have examined show a material impact.*
- 2. Provides highlights from an exhaustive, real-world analysis of over 360 case studies that shows when disputes occur and what causes them. These findings upend the conventional wisdom about what drives conflicts, showing that the vast majority are not about financial compensation.*
- 3. Announces the beta launch of two tools designed to address tenure risk. One is IAN:Risk, which is an open-source database designed to give investors a quick and easy means of approximating tenure risk exposure for any given site or across a portfolio second component. The second is IAN:Diligence, a clearly defined set of guidelines for identifying and managing tenure risk as a part of the due diligence process.*

*This kind of engagement may sound difficult – and it can be – but we firmly believe that companies and investors active in emerging markets will benefit from a new approach. And it will come at little risk since public support for IAN means we are not only able to offer IAN:Risk and IAN:Diligence free of charge, but require no notification from companies or investors seeking to use the tools or write custom applications using them to inform their risk management processes.*

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## Tenure Risk: The Basics

Tenure risk refers to the likelihood of a materially significant dispute between local people and investors<sup>1</sup> over land and natural resource rights. For example, a company may acquire a piece of land or water rights from a central government that local inhabitants believe customarily belongs to them.

Disputes can lead to delays, increased compensation payments, new or higher regulatory costs, higher resource costs, higher insurance premiums, unplanned capital expenditure, loss of license and inflated legal costs.

Tenure risk is inherent in emerging market concessions, which geospatial data demonstrates are almost entirely inhabited.<sup>2</sup> Typically, emerging market laws do not recognize these populations' presence in these areas, nor do they accord them legal standing in concession agreements. This leaves them as a kind of unrecognized counterparty to the concession arrangement.

And in many instances, local people take “direct action” to undermine a project. Such tactics include blockades, protests, site invasions, sabotage, threats to employee safety and arson – as well as potentially massive damage to the operator's or investor's reputation. The financial impacts of such disputes can be significant: as explained below, 54% of the cases we reviewed saw tenure risk result in a materially significant impact<sup>3</sup>.

But what may surprise you is that very few of these disputes (under 7%) are primarily about compensation. Our research suggests that you cannot simply hope to pay people off, even if you have a sizeable compensation budget, because people are looking for substantive engagement with their social and environmental interests than remuneration<sup>4</sup>.

For investors and companies, doing that often sounds messy, expensive or distracting. This is because it can be – if not done properly – and because many of the issues raised in such a process fall outside the typical operational concerns of a mine, plantation, dam or rail project.

We are trying to address this problem through a deliberate, thorough research and development process that examines quantitative and qualitative data and translates this into clear, time-bound and cost-conscious risk management tools. The following pages provide a summary of that effort.

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<sup>1</sup> We use the word “investor” broadly, and what we're saying applies whether you're charged with constructing a capital plan for a corporate, valuing a project finance deal in a PE fund or analyzing a public company for an equities fund.

<sup>2</sup> [http://www.rightsandresources.org/wp-content/uploads/Communities-as-Counterparties-FINAL\\_Oct-21.pdf](http://www.rightsandresources.org/wp-content/uploads/Communities-as-Counterparties-FINAL_Oct-21.pdf)

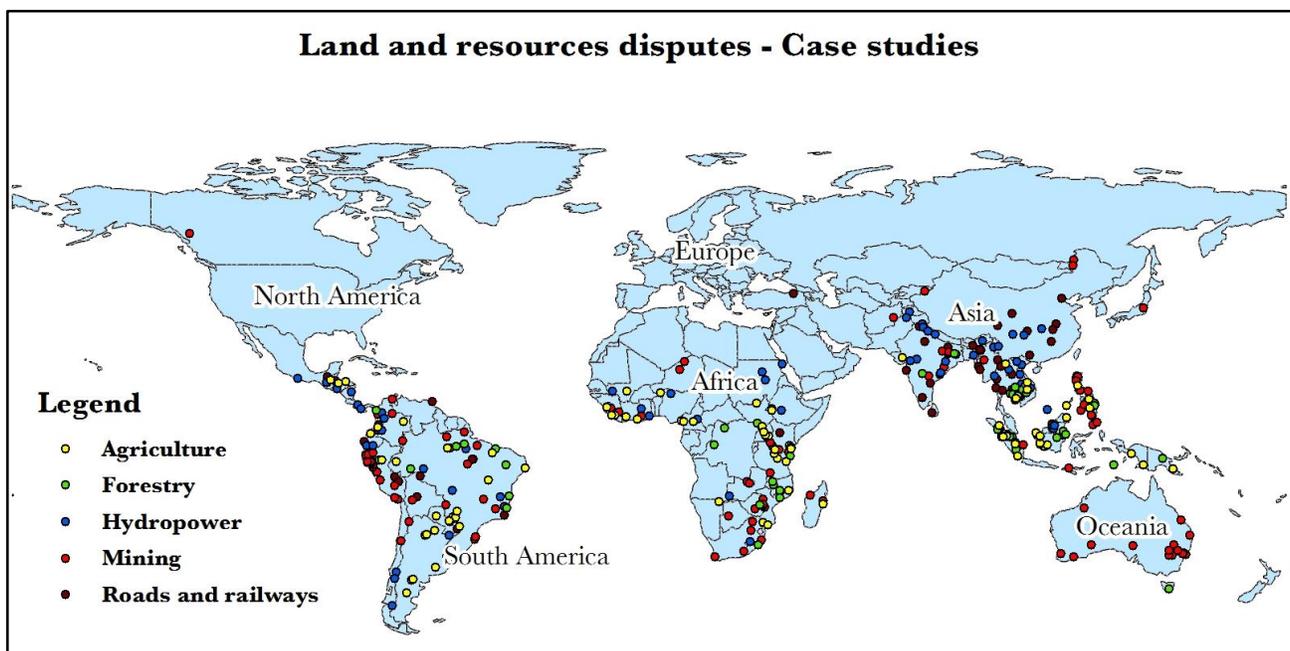
<sup>3</sup> Situations where valuable property or equipment is damaged or destroyed by arson and violent invasions; interruptions lasting five days or more; and fines costing above US\$500,000.

<sup>4</sup> This is particularly clear when we examine the remarkably high proportion of cases (64%) that involve minorities and indigenous people. Successful negotiations with these groups focus on developing trust rather discovering someone's price

## Problems: What Does the Evidence Tell Us?

The idea that there is idle, unclaimed land in emerging markets is pervasive, but easily disproven by evidence. Geospatial data indicates that the vast majority (93-99%) of concessions in those countries are inhabited<sup>5</sup>, making it virtually certain that a project developer or operator will have to engage with the interests and claims of local people.

How that engagement should work requires learning from others' mistakes. To that end, we have conducted an exhaustive examination of 362 cases in which projects in agriculture, mining, hydropower, infrastructure or forestry encountered a significant dispute with local populations over land or resource rights. These extended across a wide range of countries, as displayed on the map below:

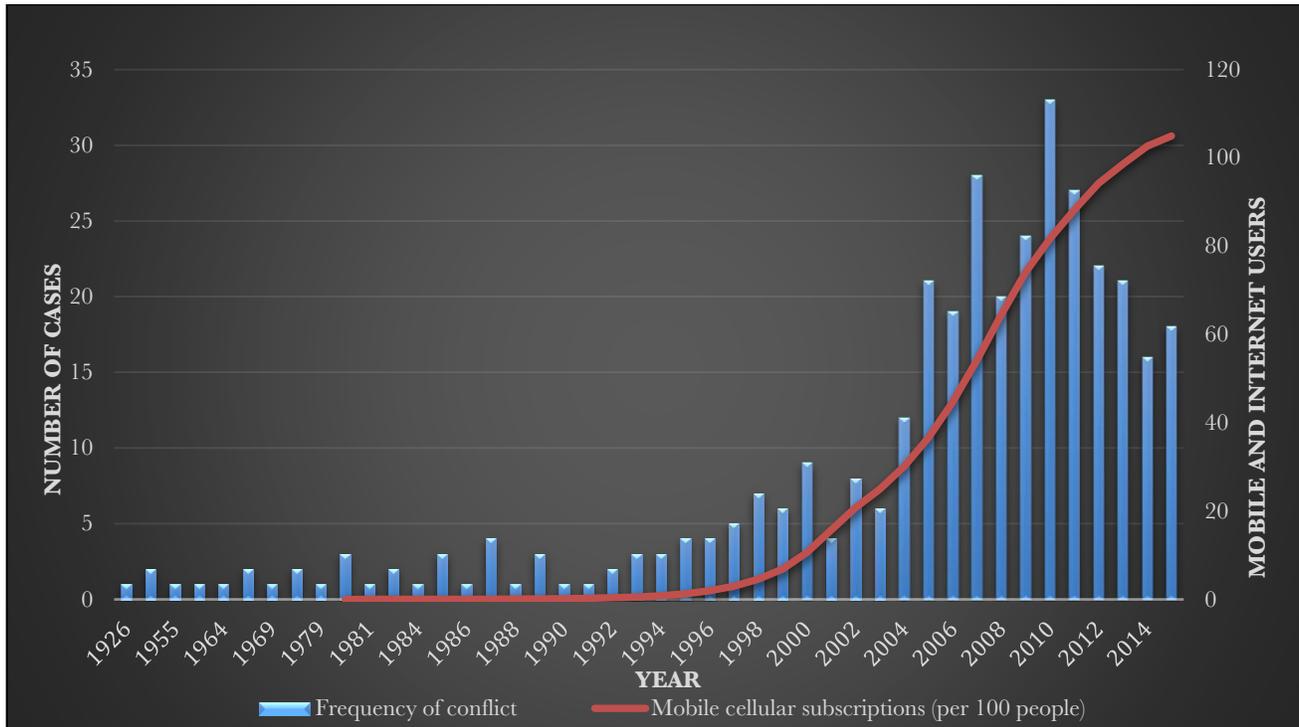


In examining these case studies, several facts became apparent. First, the number of observed disputes appears to be escalating. The reasons for this are impossible to determine scientifically, but anecdotal evidence and plain common sense suggest a couple of possible reasons.

One is a connection with the increasing penetration of mobile communications technology. That penetration is making it easier to report abuses and for local groups to organize themselves. Another is the fact that investments in major land use projects are being pushed to more

<sup>5</sup> [http://www.rightsandresources.org/wp-content/uploads/Communities-as-Counterparties-FINAL\\_Oct-21.pdf](http://www.rightsandresources.org/wp-content/uploads/Communities-as-Counterparties-FINAL_Oct-21.pdf)

challenging locations. Either way, tenure risk is becoming more pervasive (and along the same trendlines as mobile subscription increases), as shown below.<sup>6</sup>



Second, the case studies suggest tenure risk is a severe issue: over half (54%) suffered materially significant impacts. Within this, we also found that around a third of cases experienced a severe impact, such as suspension of production, project cancellation or large fines.<sup>7</sup>

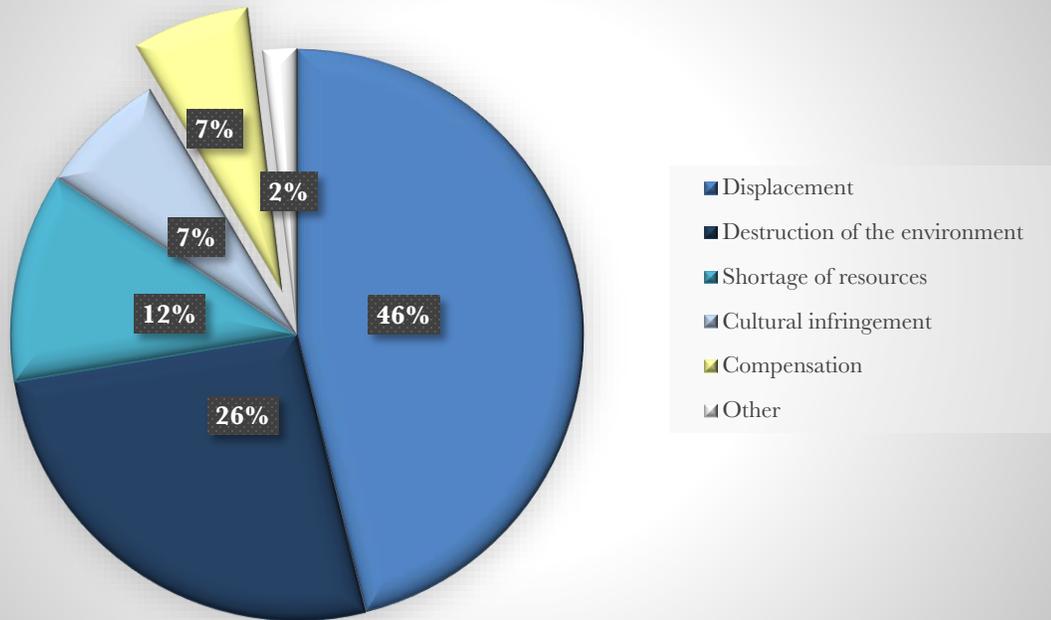
Third, the received wisdom that payoffs are the way to handle this problem is contradicted by the case studies. These show that compensation is rarely a leading cause of dispute: it was a primary driver of dispute in just 7% of the cases analyzed, as shown below<sup>8</sup>.

<sup>6</sup> The drop off we see in the graph is explained by the lag in reporting, particularly since we have focused on cases where the details are clear and well-established.

<sup>7</sup> For example, when opposition to Newmont’s Conga gold mine escalated to violent conflicts and fatalities in 2011, the Peruvian government suspended the \$4.8 billion project and declared martial law. Discontent has since spread to surrounding mining areas such as Cocachacra and Quellaveco, effecting a number of mining companies and propelling the issues of mining and tenure to the forefront of this year’s presidential elections. (<http://www.wsj.com/articles/peruvian-voters-favor-anti-mining-candidates-1412634947>)

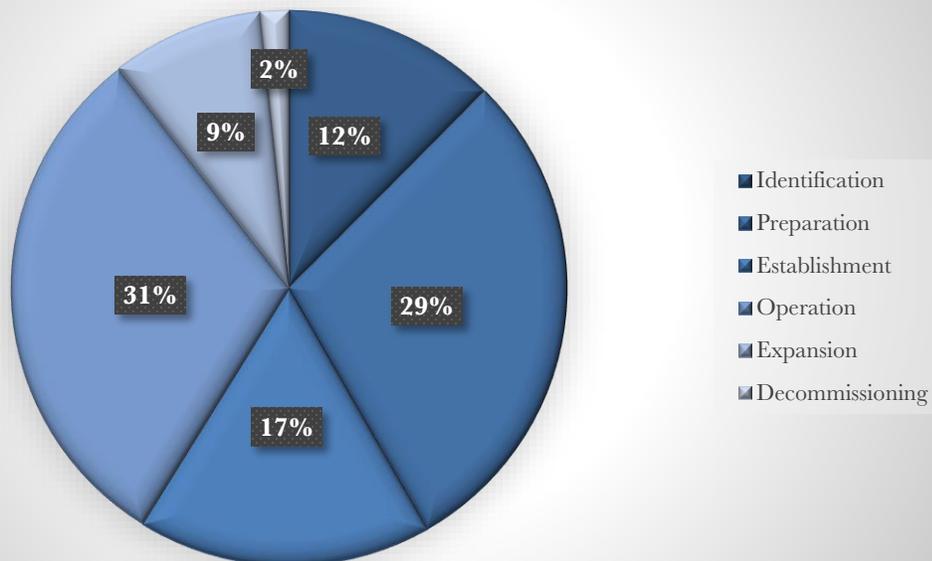
<sup>8</sup> The shortcomings of an approach based on compensation are particularly acute in cases that involved minorities and indigenous people. Overall, we found that 64% of cases involved these groups, who are often uninterested in economic conceptions of valuation and are principally interested in opportunities to continue traditional livelihoods (this trait helps to explain why the presence of minorities is perhaps the single clearest indicator of the likelihood of dispute).

## What is the primary cause of dispute?



This brings us to our fourth conclusion, which is that tenure risk is not exclusive to any part of the operational process. As shown below, it arises in every phase of a project’s lifecycle:

## When do disputes start?



This confirms the importance of getting on the right operational footing at the very start of project development and maintaining that proper footing throughout.

## Solutions: New Tools for Risk Management

Based on this evidence, we see the need for new risk management tools that can help identify and manage tenure risk more effectively. Our current project – called IAN – is an effort to produce those tools, and we launched two beta versions of them in recent months.

These are explained below in superficial detail, and we emphasize that they are both completely free to download, use and modify. Interested parties should contact Ben Bowie, our lead partner for IAN, at [ben.bowie@tmpsystems.net](mailto:ben.bowie@tmpsystems.net) to ask for more details.

### *IAN:Risk*

IAN:Risk is a quantitative risk tool built on 25 large, reliable and publicly available databases. It is designed to give investors a quick and easy means of approximating tenure risk exposure for any given site or across a portfolio. It provides a catalogue of useful information, and quite soon, will also use transparent algorithms to generate an index of tenure risk.

IAN:Risk takes advantage of the wealth of reliable, granular data that is available from public institutions for free. It collates location-specific information on key tenure-related issues like the presence of people, land use, social unrest and welfare, water and food security and governance. This can be used directly or it can be employed for verification purposes.

IAN:Risk offers strategic direction for diligence efforts. It can tell investors which issues to investigate and which to dedicate less time to. It can even help to tell whether a site or asset should be ignored completely.

### *IAN:Diligence*

IAN:Diligence provides step-by-step, sector-specific guidance for diligence on tenure risk. It aims to give investors a much clearer picture of what causes conflict, when they happen and what can be done to prevent the problem. Much of the research reproduced in this paper is drawn from analysis for IAN:Diligence -- where it is broken down according to sector and stage in the project lifecycle.

IAN:Diligence has two core objectives: first, it gives investors the data they need to make an informed decision about a project or portfolio. Second, it helps investors to engage local people as counterparties. This relationship is key to tenure risk management but can also, as we see below, provide an array of additional benefits.

IAN:Diligence differs from other available guidelines because its recommendations are based on quantitative analysis of a large body (362) of case studies. This concrete analysis of the risk case, along with a comprehensive literature review, provides a hard-headed financial basis for decision-making.

## **The Big Picture: Why Does This Matter?**

The preceding sections argue that engaging local populations as project counterparties provides a cost-effective means of identifying and reducing tenure risk. We hope that IAN's progress and eventual adoption will help substantiate this view.

But this leaves out a very important point: engagement is not merely beneficial from a risk management perspective. It may also produce more viable projects, and help companies increase their value.

For example, consider the micro level: local populations are likely to know most about the complexities and nuances of local social and environmental conditions, and in some cases far better than engineers dropped in from somewhere on the other side of the globe. In those situations, local populations are also likely to know most how to configure workable solutions. These are not only key to resolving tenure risk and improving project operational efficiency, but they are also solutions which might not have been discovered had the engagement not happened in the first place.

We can also expect some macro benefits, too: companies with the capacity to develop effective relationships with local counterparties can open up previously challenging operational environments. A systematic approach to winning and maintaining trust provides a clear competitive advantage in emerging markets and especially in the remote regions of the world that hold a growing share of the natural resources. In similar fashion, a policy of good engagement can also allow investors to accrue reputational gain.

In other words, we think there is a chance that managing tenure risk can be bigger than limiting the downside from conflict. We hope that this paper and its supporting materials assist companies and investors in working with local populations to achieve those benefits.