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Why the EITI Rules need to cover licensing:
the case of the Democratic Republic of Congo

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In July and August 2011, news came out that state mining companies in the Democratic Republic of Congo (DRC) Gécamines and Sodimico had sold stakes in four major mining sites without making the information public. There are several major concerns over the deals, notably:

- They were done in secret and not disclosed publicly;
- Certain assets were sold for far less than most commercial estimates of their value.
- The companies that benefited from these deals were based in offshore tax havens and could thus keep their real owners secret;
- The state mining companies conducting the sales and the relevant Government bodies publish virtually nothing in terms of financial statements. This means it is impossible to trace what has happened to the sums officially received from the sales.

The behaviour of the DRC authorities in these deals appears to be part of a pattern of selling off assets to opaque offshore-registered companies. Sometimes the assets sold had been confiscated in unclear circumstances from previous owners and the sales prices subsequently agreed with the offshore-registered companies were much lower than most commercial estimates. In such circumstances, and given the well-established risks of corruption in the DRC, there is an evident concern about the risk of embezzlement and significant losses of revenue to the country.

What further forms of transparency are needed?

In order to comply with the EITI rules, the DRC government is expected to publish all payments received from companies for mining licences but this would not, in itself, address the question of who owns these companies, and who is ultimately benefiting from the deals.

After news of the sales became public knowledge, the Government did publish some details in the form of contracts related to Sodimico's sale of stakes in two mines – Frontier and Lonshi. These mines had been confiscated previously from international mining firm First Quantum, in circumstances First Quantum vigorously disputed. Though it is commendable that the government published the contracts, this does not clear matters up.

Many questions remain, including over the sales price. The International Monetary Fund was sufficiently concerned by the sales to write to the DRC authorities for clarification. Sodimico stated, in a response to the IMF that was published on the website of the Congolese Ministry of Mines, that the stakes had been sold for $30 million.[1] But Bloomberg, the business news service, has cited research by two London-based securities firms that valued the two mines at more than $1.6 billion. If these estimates are accurate, then they would indicate that the stakes were sold for less than a sixteenth of their value.[2] This obviously raises profound questions about the rationale and commercial motives of the deal which cannot be addressed purely by the reporting of revenue flows under EITI rules. EITI reporting can only show what was actually paid for access to a natural resource asset, not whether the payment was proportionate to the value of that asset or not.

The whole episode, including the confiscation of Frontier and Lonshi, is worrying. Frontier is now in disuse and, according to a donor source, is flooded with water. Before its confiscation, the company was the largest taxpayer in the DRC, contributing some $70 million to state coffers and producing 84 per cent of the country's copper ore exports.[3] The financial impact of the affair on the DRC will evidently be huge.

In this kind of situation, the current reporting rules of the EITI would show only that revenues from a particular company have fallen from one year to the next. Even this assumes that the country concerned is applying disaggregated reporting: aggregated reporting would reveal almost nothing about the cases discussed in this note, even though they go to the heart of the EITI's principles and aims.

Contracts have not been published for the sale of stakes in two other mines – 20 per cent of Mutanda and 25 per cent of Kansuki – to offshore companies associated with Dan Gertler, a businessman who is an associate of President Kabila.[4] Here, the sales price similarly remains an issue. In October 2011, Gécamines reportedly confirmed the sale value of $137 million for both mines, although in a response to the IMF Gécamines suggested that this represented the value of the stake in Mutanda mine only. According to Gécamines, BNP Paribas valued the Mutanda stake at $108 million.

However, the May 2011 share prospectus issued by Glencore (which owns shares in Mutanda via a subsidiary), contained an independent consultant's report commissioned by Glencore which valued Mutanda at over $3 billion[5]: this would value the 20 per cent stake in Mutanda sold by Gécamines at around $600 million. And Deutsche Bank said in a June 2011 report that Glencore's 37.5 per cent stake in Kansuki was worth $313 million: at the same valuation, the 25 per cent sold by Gécamines would be worth more than $200 million. [6]

A spokesman for Mr Gertler told Global Witness that although Mr Gertler and his companies had good relationships with the DRC leadership, they never enjoyed "free rides". He said that the sale price reflected the true value of the mining assets and disputed that the valuation figures for Mutanda and Kansuki were accurate assumptions of value. [7]

Without official, published and verified information about the pricing of the sales, it is not possible to address the concern (denied by Mr Gertler's spokesman) that the assets may have been sold at well below their market value.

To sum up

The DRC's people are desperately poor. Under-five mortality is 199 for every 1,000 births. Over half the population lives on less than $1.25 a day. The country ranks bottom on the UN's Human Development Index. It needs to earn revenues from its natural resources sector to develop. However, a series of mining deals this year show there is a danger that natural resources are being mismanaged.

The wider implications for the EITI are that the initiative needs to adopt international requirements to ensure greater public oversight of the allocation of extraction licences. Global Witness is aware of cases in several other countries where licences have been allocated to companies in a questionable way, including one country which is now EITI Compliant, and we expect to publish our findings in the near future.

So the scope of EITI reporting needs to be extended to ensure:

- Publication of contracts, as already required in the DRC and as practiced or envisaged by several other EITI implementing countries.

- Publication of the valuations, carried out by independent auditors, of oil and mining assets, to be sold by the state.

- Public disclosure of the ultimate beneficial ownership of companies that bid.

- Clear and transparent bidding rules and criteria that enable legislators, the media, civil society groups and other concerned citizens to determine why a particular company won a particular asset and what the financial benefits of the deal are, both to the state and to the company itself.

- An independent review mechanism, possibly housed with the EITI multi-stakeholder group in the country concerned, with the power to scrutinise the allocation of licences and contracts and confirm that all applicable laws have been complied with (a power granted to the EITI in both Liberia and Nigeria).

Transparency is not an end in itself, but a means of ensuring greater public scrutiny of the allocation of oil, gas and mining contracts and deterring corruption and fraud by exposing it to sunlight. The EITI needs to extend its scope in order to address the risk that countries deemed to be EITI Compliant may nonetheless have significant flaws in their licensing regimes that could enable significant corruption and financial losses to the state.

[1] Letter to DRC Minister of Mines from Sodimico. 16 September 2011. http://mines-rdc.cd/fr/documents/Reponse_Sodimico_questionnaire_FMI.pdf.

[2] Bloomberg, Congolese State Miner Sodimico Sells Stake in Former First Quantum Mines, by Michael J. Kavanagh and Franz Wild. 17[t] August 2011

[3] For data on copper ore exports: Congo Business Lobby Criticizes Prime Minister Over Changes to Mining Laws, by Michael J. Kavanagh. For data on Frontier, also see First Quantum President Clive Newall's evidence to the UK parliament's International Development Select Committee, in which he says: "Frontier paid $54 million in taxes alone for 2009, and contributed over $70 million in 2009 including royalties, import duties etc."

[4] For Gertler's links to Kabila see, for example, Jason Stearns's Congo Siasa blog of 21 June 2010 (http://congosiasa.blogspot.com/2010/06/dan-gertler-at-it-again.html) and Sunday Times piece of 6/3/11: "Israeli holds key to Congo riches", by Danny Fortson.

Regarding Gertler's links to the companies that bought stakes in Mutanda and Kansuki, Glencore's Initial Public Offering prospectus from May 2011 says that a 20 per cent. interest in Mutanda Mining was recently acquired by Rowny Assets Limited (an entity associated with Dan Gertler) from Gecamines and a 25 per cent interest in Kansuki was bought by Biko Invest Corp. Both companies, the prospectus says, were at the time "associated" with Dan Gertler.

[5] Glencore International Plc. Prospectus for initial public offering. 4 May 2011. Page 958

[6] Deutsche Bank. Glencore. The value in volatility, initiating with a buy. 6[t]June 2011. Page 118. http://www.scribd.com/doc/57254342/34/Mutanda-%E2%80%93-a-tier-1-greenfield-development-asset

[7] E-mail from a spokesman for Mr Gertler to Global Witness, 12 September 2011.