Title: The Social License to Operate in the Latin American Mining Sector: The cases of *Bajo de la Alumbrera* and *Michiquillay*

Authors:

Zamprile, Alejandro; Austral University – IAE

Llorente, A. Ariel; Austral University - IAE

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Abstract: In this extended abstract we intend to show that, in several of the Latin American (LA) countries, the outcomes that may derived from the interactions between Multinational Corporations (MNCs) and the ever widening variety of interest groups that are part of civil society are deeply influenced by the recipient country's government political and economic attitudes regarding Foreign Direct Investments (FDIs). There are other effective ways to reduce the non commercial risks that FDIs, even when MNCs from environmentally ill reputed industries are involved, confront in the region: the Social License to Operate (SLO). Our research, in the form of a case study, analyzes the processes by which two different mining MNCs implemented their respective projects; the presence or absence of the SLO, as part of their corporate ethical behavior, led to polar outcomes: *how* and *why* that happened is the subject of

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Abstract

In this extended abstract we intend to show that, in several of the Latin American (LA) countries, the outcomes that may derived from the interactions between Multinational Corporations (MNCs) and the ever widening variety of interest groups that are part of civil society are deeply influenced by the recipient country's government political and economic attitudes regarding Foreign Direct Investments (FDIs). There are other effective ways to reduce the non commercial risks that FDIs, even when MNCs from environmentally ill reputed industries are involved, confront in the region: the Social License to Operate (SLO). Our research, in the form of a case study, analyzes the processes by which two different mining MNCs implemented their respective projects; the presence or absence of the SLO, as part of their corporate ethical behavior, led to polar outcomes: *how* and *why* that happened is the subject of our research.

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Social and environmental impacts are indistinctively connected with certain corporate operations; social awareness around both types of impacts is a motive for frequent collisions between governments, corporations and the civil society. These three parties' divergent interests arise, with excessive frequency, public disputes. Corporations' executives have learned how damaging accidents and inadequate managerial responses to crisis may turn up to their financial results: Eveready's Bhopal plant catastrophe, Exxon Valdez's shipwreck and oil spill in front of Alaska's seashore or Shell's Brent Spar controversy showed how harmful to the firms' reputation and finances, personal, environmental and social damages are (Massey, 2001; Zyglidopoulos, 2001; Hoffman & Bazerman, 2005).

We choose the LA mining sector because it is a driving economic force for many of the region's countries; in recent years, most governments introduced, with the encouragement and support of the World Bank and the Inter American Bank of Development, profound changes in their legal structure in order to encourage and facilitate FDIs to fund this sector's expansion. As the success or failure of operations within the mining sector is deeply influenced by each host country's legal and fiscal framework; these crucial factors are taken into account along the corporate decision making process that usually leads to multimillion investments.

From 2003 through 2008, metals and industrial minerals international market prices showed a steep growth; that trend fueled governmental eagerness to capture new FDIs. Most of the proposals provoked social opposition on the basis of three main claims and perceptions: a widespread nationalistic sentiment, against the presence and operation of MNCs, that involves sovereignty implications about the exploitation of natural non renewable resources; an unbalanced distribution of the economic gains –too much for the MNCs, a little for the host country's government and almost nothing to the affected communities- and the social and environmental damages that mining operations reputedly afflict to both surrounding communities and the natural environment.

This study explores, in two of the LA countries, how instrumental the negotiation process that leads to obtain and sustain a SLO is for the successful implementation, and continuous operation, of mining FDIs. This investigation focuses on two cases, each of them involving a different mining MNC, which were socially and environmentally rejected –at least at their inception- by their surrounding communities. Successive corporate interactions with the projects' stakeholders -communities and governments- led to divergent outcomes. One case is: the copper and gold open pit mine *Bajo de la Alumbrera*, in Argentina, that is operated by *Minera Alumbrera* Ltd. (*Alumbrera*), owned by Switzerland based Xstrata plc, Goldcorp Inc. and Northern Orion Resources Inc., under a concession contract granted to the transitory union of businesses (UTE, in its Spanish acronym) that it conformed with the state owned *Yacimientos Mineros de Agua de Dionisio* (YMAD, in its Spanish acronym). The other one is in Peru: the copper mine *Michiquillay* project, belonging to the London based Anglo American plc (AAUK).

Literature Review

The social license to operate and corporate ethical behavior

Managers conduct their firms' operations in an environment that has been characterized as one that comprises "*the totality of physical and social factors that are taken directly into* *consideration in the decision making behavior of individuals in the organizations*" (Duncan, 1972). The social sphere of that environment was for a long period limited to the organization itself, later it was amplified to include the shareholders and only recently widened to comprise new participants: the stakeholders. Stakeholders are currently defined as those with a stake or an interest in an organization, including anyone who may be impacted by or have an impact on the firm including employees, suppliers, customers, the local community and the environment (Collins, Kearins & Roper, 2005; Campbell, 2006).

Empirical research shows that MNCs, which are deeply committed to attain positive social performance goals, are in a better condition to recoup the costs of those efforts and to enhance their competitiveness in foreign markets (Bouquet & Deutsh, 2007). As Abbas J. Ali (2007) recently pointed, commenting the results of two *McKinsey Quarterly* surveys, there is an increasing awareness amongst corporate executives that sociopolitical concerns are not outside the range of their duties and that consumers expect corporations, particularly the big ones, to address them properly; there exists an evident necessity of aligning corporate objectives with societal expectations.

A widespread societal rejection of the negative effects, on both the surrounding communities and the natural environment, that some corporate economic activities produce –particularly the extractive sector: oil, gas or mining- led to have been labeled as *Corporate Environmentalism*. Corporations' management is currently aware that the firm's operations need to be environmentally responsible without any lessening of their profitability (Williams & Aguilera, 2008); the ultimate goal is, to be *green* and to remain competitive and profitable as well (Porter & van der Linde, 1995).

Environmental Non Governmental Organizations' (ENGOs) members and sympathizers are reluctant to concede that corporate profits may be positively linked with sound environmental performance; instead, they uphold that more stringent standards and regulations in developed countries provoked a corporate migration flow to what they catalogue as *pollution havens* in less developed societies. ENGOs' partisanship emphasize that the only way to make polluters comply is by means of an extremely stringent set of environmental regulations and standards that structure a *command and control* scheme based on governmental agencies –local, state and federal– with overlapping jurisdictions and responsibilities (Coglianese, 2002; Gunningham & Sinclair, 2007).

Laws, rules and regulations define what governments have decided that is legally permissible; those frameworks are unable to mark the boundaries of what is an ethical conduct. This gap is, among others, a superabundant source of individual and societal demands for adjustments; that societal pressure leads firms to respond, as effectively as possible, to two volatile sets of demands: the frequently changing governmental regulations and the ever evolving requirements of neighboring communities (Gunningham, Kagan & Thornton, 2004); accordingly, firms' managers must deal with the constraints posed by the natural and the social context within which they operate (Kagan, 2003).

Firms' executives are continuously delineating a new corporate environmental management standard and opting to go *beyond compliance* of the prevalent governmental regulations, regardless of their stringency, rather than strictly fulfilling them, in order to respond to the increasingly more severe societal pressures (Gunningham, Kagan & Thorton, 2004; Hoffman & Bazerman, 2005; Howard-Grenville, Nash. & Coglianese, 2006).

The SLO is a recently developed corporate attitude towards the socially and environmentally sustainable development of the surrounding areas and communities where firms are active (Van Lee, Fabish, and McGaw, 2005); the main thrust surged, primarily, from within the extractive industries (Nelsen & Scoble, 2006). The World Bank Group's President James D. Wolfensohn appointed Dr. Emil Salim (former State Minister of Environment and Population, Indonesia) as *Eminent Person* to conduct a stakeholder review as a preliminary step in the preparation of a Extractive Industries Review (EIR); basically, the EIR proposes that corporations must earn their SLO by means of a *prior fully informed consent from indigenous peoples, or local communities, that may be only acquire through mutual agreements, in a forum that gives communities leverage to negotiate conditions, as well as an offer based on multidisciplinary analysis* (Salim, 2003).

The SLO is an intangible, non-permanent, measure of an ongoing acceptance of a company's activities by communities. The SLO is mandatory to maintain a positive corporate reputation, to understand the communities' culture, language and history, to educate local stakeholders about the project and to ensure open communication amongst all of stakeholders. The two main positive indicators that a company's executives need to seek to earn a SLO for a project are: the results of a community consultation program and a letter of support of the community; the process to earn a SLO has two main protagonists: the company and the community (Nelsen & Scoble, 2006; Kasatuka & Minnitt, 2006). The SLO negotiation process provides a stimulating reward in return: a significant reduction of the project's non-commercial risks that may provoke, if they happen, serious financial damages (Kasatuka & Minnitt, 2006).

Method

In order to progress in our research we will conduct an empirical case study combining multiple data collection methods (Eisenhardt, 1989); our aim is to study how instrumental is the corporate ethical behavior in the process of earning the SLO for each project and how firms manage governmental intervention along it. We consider the case study method a suitable research strategy to accomplish our purpose; the case study method, as Robert K. Yin (1981) put it, is: "*an empirical enquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident.*"

The case study method is the most appropriate means to address *how* and *why* questions regarding a set of facts (Eisenhardt, 1989). Thus, we propose an explanatory analysis of two FDI mining projects, to compare similarities and differences –that led to polar outcomes- between them (Pettigrew, 1990). As Yin (2003) stated:

> *... case studies, like experiments are generalizable to theoretical propositions and not to universes. In this sense, the case study, like the experiment, does not represent a "sample" and the investigator's goal is to expand and generalize theories (analytic generalization) and not to enumerate frequencies (statistical generalization)...* (Yin 2003:10).

At a first stage, we examined an ample scope of secondary sources of information, such as public documents, reports or books from both MNCs, from both LA countries' national mining authorities and from international and national ENGOs in order to confirm or contradict, to "*triangulate*", the information gathered (Eisenhardt & Graebner, 2007).

In a second phase we plan to conduct a mail survey amongst officials of the governments' mining officials, corporate executives and the leadership of the communities' opposing groups that claimed being affected by the FDI projects. The questionnaires will include two sets of open and close ended questions around a few main themes: the ways in which the respondents think that the firm's precedent ethical behavior –the corporate reputation- facilitated or not the process to acquire or not the SLO for the analyzed projects; the interviewees' judgments about the relevance –within their organization and/or for themselves- of the SLO along the lifecycle of each corporate operation; their views about why most mining FDIs in LA are subject of explicit social opposition and conflicts and the real or perceived influence exerted by governmental political and economic attitude towards FDIs in general and towards the mining sector in particular. The questions will be phrased and ordered as to limit, as much as possible, a convergent retrospective sense-making that could biased the interviewees' responses (Eisenhardt & Graebner, 2007). The survey will include a clause of confidentially by which the identity of each of the respondents will remain anonymous.

This case study intends to expose the dynamics of the interactions that MNCs' natural resources based FDIs unleash and that, at least in most of the LA countries, frequently evolve into conflicts. Governments' political and economic attitudes with relation to FDIs, previous corporate ethical behavior –of which the SLO is a relevant component- and societies' needs, real or perceived, will collide whenever the discrepancies between them are improperly managed.

The ethical performance, social and environmental, particularly that of mining MNCs' FDIs, and the sustainability of their negotiated LSO, is an incessant process that impose firms to pursue and to attain the highest corporate standards; this valuable goal can only be accomplished if it is buttressed by a global and persistent technological and managerial progress (Sharfman, Shaft & Tihanyi, 2004).

A revision and analysis of two recent experiences may provide useful tools to enhance firms' knowledge and capabilities to face and enhanced their performance in future FDIs in which the SLO may be part of the sensitive issues that conform the context of the operation. At the same time, we intend to expose an unexplored –at least in the LA countries- area of corporate, governmental and social interactions, which may be of academic interest for further investigation.

Two cases' polar outcomes

Bajo de la Alumbrera

The Argentinean, nationally and provincially-owned, mining company *Yacimientos Mineros de Agua de Dionisio* (YMAD), is the legal owner of the estate where the *Bajo de la Alumbrera* deposit, in the province of Catamarca, is located. In 1992, YMAD's Board of Directors awarded, by means of an international tender, *International Musto Exploration* the concession to exploit it. Mineral extraction started in 1997. Owners changed several times until, in 2003, Switzerland based mining MNC Xstrata plc -the seventh largest mining company registered on the London Stock Exchange (Reuters, 2008a)- acquired 50 percent of the shares of *Minera Alumbrera* Ltd. (*Alumbrera*) and became its operating partner; Goldcorp Inc. and Northern Orion Resources Inc. own the remaining 50 percent.

Since *Alumbrera*'s operation started, some 70 local health centers have been assisted and educational aids were provided to one hundred local communities as part of the firm's widely publicized Corporate Social Responsibility (CSR) program (Asongu, 2007). Notwithstanding, environmental advocates oppose *Alumbrera* for being part of what they call *Big Mining,* for the progressive and irreversible alteration of the natural landscape (Hancock & Turley, 2006) and for the depletion of their natural resources.

In *Bajo de la Alumbrera*, miners move 120 million metric tons of earth annually -two shifts of workers, operating day and night, every day of the year- to obtain an average of 200 thousands metric tons of copper and around 650 thousands ounces of gold; it is the largest, oldest and most profitable open-pit metals mine in Argentina. Extracting and processing such level of production demands a large amount of water; a 220 km long power line that provides the site with 220 volts power feeds the intensive energy consumption.

In the mine's site, mountains are exploded and ore is removed, crushed and leached with chemicals to produce a thick, metal-rich slurry. The mine's operation demands approximately 5,000 cubic meters of water a month -extracted from thinly fed water tables in an area with not much more than 150 mm of yearly rainfall- which are returned, after used, to a distant river system. The metal-rich slurry is pumped 140 miles through a pipeline -over a 8,000 foot mountain pass- to a plant, in the province of Tucumán, where it is "dewatered" and the extracted liquid thrown into the canal DP2 which is part of the Salí–Dulce rivers basin. From there, the dried sludge containing the minerals is transported 450 miles by train to *Puerto Alumbrera*, on the river Paraná shores, near Rosario, in the province of Santa Fe; there the mix is shipped to overseas plants where the extraction and foundry of gold, copper, silver and other minerals is completed.

After several accidents –spills from the long pipeline- community pressures grew persistently; meanwhile, *Alumbrera*'s management produced, every two years, several

Environmental Impact Reports (EIRs) without acknowledging them. In an accident provoked, on September 17 2004, by an earthquake –6.5 on the Richter scale- concentrated minerals spilled in Villa Vil river which provides drinking and irrigation water to the Andalgalá department, in Catamarca; shortly after, a team of legal advisors, representing the inhabitants of that town, accused before the Federal courts *Alumbrera* for the "dissemination of dangerous wastes" for the infringement of the provisions of Law 25612 (*Integral management of industrial and service sector wastes*).

Societal grievance reached the courts in Tucumán; after a trial motivated by a series of fish die-offs, in 2001-2004, in the Salí-Dulce river system, environmentalists succeeded: Tribunal judges decided to press criminal charges against *Alumbrera*. Members of the Vis-Vis community in Amanao district, Andalgalá Department of Catamarca, asked the Federal Prosecutor to start a criminal action against the firm's executives for considering them responsible of the alleged contamination generated by the mine. Federal Justice pursued Mr. Julian Rooney, *Alumbrera*'s Vice-President, in order to compel him to make statements in the case; at the same time, in Santiago del Estero´s courts the firm was denounced for environmental contamination of the *Termas de Río Hondo* dam's lake and the river Dulce basin (MiningWatch Canada, 2007).

By that time, several citizens' groups reacted against a number of different mining operations scattered through Catamarca's territory. Residents of the town of Aconquija set blockades to roads as a protest for the mineral sludge pipeline spills; in Tinogasta, in western Catamarca, numerous groups of residents decided to blockade one truck which was carrying explosives and chemicals from Chile to the *Alumbrera*'s site; the firm's train has been repeatedly stopped, in Santiago del Estero, by different groups of protesters.

By the end of May 2008, the Federal Tribunal in Tucumán brought criminal charges of environmental contamination against Mr. Rooney; he remained free, but his personal possessions were impounded. This was the first judicial ruling, in any LA country, against a mining company's executive for crimes against the environment. The company's lawyers announced that the ruling would be objected before the Court of Appeals and that, if needed, before the Supreme Court; this pending final decision will certainly affect the future of mining in Argentina.

Michiquillay

Michiquillay is located in the northern district of Cajamarca -a mineral district which already hosts a number of mines- about 30 miles from the region's capital (also called Cajamarca) and some 560 miles north of Peru's capital, Lima. Besides copper, the property has gold and silver. Peru is the world's third-largest producer of copper, its fifth-largest producer of gold and its largest silver producer (Tejerina, Tarta & Lawrence, 2008). The Peruvian government called for a public bid, on April 2007, in order to reopen the mine by granting a concession contract over the deposit's area; the Peruvian mining authorities estimated that the project's exploration stage will take four years -after that lapse infrastructure construction will start- and that the project's total investment will amount, at least, US $700 millions. London based AAUK -one of the world's largest mining and natural resource groups, with operations in Africa, Europe, South and North America, Australia and Asia- won the bid for the *Michiquillay* copper project with an offer of US $ 403 millions (Anglo American, 2008a). The firm offered to disburse the bid price to the Peruvian government in yearly installments during the first five years of the project. The Peruvian authorities publicly asserted that half of those payments would be allocated to a trust fund for the development of the local community.

La Encañada district has almost 23,000 residents, which includes the 1,100 living in the *Michiquillay*'s area. The project has a substantial number of opponents; their argument is that several valleys –some argue that they are five while others say the number is six- that are connected to the *Michiquillay* site's service land, comprising almost 60 thousands families, would lose vital water supply for their crops and farms together with other severe environmental damages.

In Peru, there is a statutory provision, commonly branded as *"social agreement"* (acuerdo social, in Spanish) -a close relative to the distinctively negotiated SLO- that makes mandatory the community's acquiescence for a mine to be operative; without this permission, a mine cannot function. Peruvian President Alan García tried, during 2007, to circumvent it by issuing a Decree –invoking Peru's *national interest*- that would have allowed 20 different mines (including *Michiquillay*) to be developed without full compliance of the applicable Mining Law's stipulations; his initiative was rejected by the national legislative power and, thus, the *"social agreement"* still holds.

There is significant additional exploration potential associated with the *Michiquillay* deposit; AAUK's surveyors identified other copper projects that are already under evaluation: one of the most promising and advanced is *Quellaveco*. In her speech at the Amsterdam Global Reporting Initiative (GRI) Conference, on May 7 2008, AAUK's CEO, Ms. Cynthia Carroll, said:

Perhaps the most critical issue in the entire sustainable development arena is that of water. Many of our own operations are in extremely arid areas, where there is inevitably competition with other users and industries, such as farming, over this vital resource. Increasingly, all of us must compete for water resources and account for our full social and *environmental costs... in Peru, we have copper projects at* Quellaveco *and* Michiquillay*, where a great deal of dialogue is taking place with the local communities and farmers to work out an acceptable arrangement to guarantee water supplies to both the proposed mines and the communities concerned... In this respect, a very important differentiator in terms of the gaining and maintenance of Anglo American's license to operate, is our Socio Economic Assessment Toolbox, or SEAT process, which provides a consistent framework for our community-engagement and development activities.* (GRI - Conference Report, 2008)

Michiquillay's and *La Encañada*'s residents are quite familiar with the arguments both pro and against mining development; albeit their apprehensiveness about the return of full scale mining to their community, they decided to engage in series of meetings with both governmental authorities and AAUK's official representatives. After a long sequence of encounters, Peru's Mining Ministry issued a statement indicating that as result of those deliberations AAUK's executives and both communities have reached, each of them, agreements that will allow the firm to start the exploration phase in the project's area (Reuters, 2008b). The *Michiquillay*'s agreement reflected a prior definition made within the community: 736 of its members voted in favor of AAUK's project development and 432 against it. The salient clauses of the negotiated SLO are:

…the parties' commitment to build and maintain an environment of dialogue, respect and harmony; the establishment of a Community Development Foundation; the creation of participative monitoring committees and the execution of an environmental base line study

and a detailed study on soil usage before starting the exploration activities…(Anglo American, 2008b).

The deliberative process delayed the project's inception more than a year; during that period the firm's management delivered a permanent flow of technical information to the stakeholders in order illustrated them about the expected positive triple bottom line –financial, social and environmental- performance of the *Michiquillay* project.

Discussion

This study should advance our understanding of the dynamics of the interactions, and of personal and organizational stances, that may lead to productive or unproductive conflicts. This study intends to refine our understanding of the integrative relationship between corporate ethical behavior and the SLO, as well as how and why governmental intervention may encourage or dissuade the development of societal conflicts related with sensitive issues such as socioeconomic development and the sustainable management of natural resources. We hope that the final results of our study will have practical implications for improving intra and inter group processes, communication and deliberation on those matters.

Given our findings (once we have all of them) we may consider to implement a wider study comprising all the extractive industries, the societal objections and the opposition that the firms active in this sector continuously face -and how they manage them- in all the LA countries. This paper does not pursue the purpose of testing formal hypotheses but to expose some arguments derived from real world corporate and personal deeds; our main theoretical and managerial contribution emphasizes the positive impact of a sound corporate ethical behavior on the sociopolitical environment in which the firms operate.

To our knowledge, little research has been done in the LA countries on the instrumental role that the corporate ethical behavior influences the process of acquiring and sustaining a SLO with surrounding communities and on the ways governmental political and economic orientations regarding MNCs' FDIs helps or not to its successful accomplishment. Thus, we expect that this case study, when finished, will encourage scholars and practitioners to further explore this field.

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