Costs of Company-Community Conflict in the Extractive Sector

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This report is the product of research conducted by the Corporate Social Responsibility Initiative (CSRI) at Harvard Kennedy School and the Centre for Social Responsibility in Mining (CSRM) at the Sustainable Minerals Institute at The University of Queensland in Australia. During the course of the research, Rachel Davis, together with other colleagues, established Shift, a non-profit center on business and human rights, which joined CSRI and CSRM as a partner in this project.

The authors gratefully acknowledge the contributions to the design and execution of the research provided by Caroline Rees and John Sherman (of both CSRI and Shift), Deanna Kemp, Saleem Ali and Warwick Browne (CSRM), and Anthony Bebbington (Clark University). They are also grateful for the dedication of a number of research associates: Katharina Hermann, Ming Lei, Jack Nichols, Kristen Roy, Olivier Salas, Ashlee Schleger and Daniel Tuazon.

In relation to the fieldwork in Peru, Rachel Davis is grateful to Caroline Rees, Deanna Kemp, Rebekah Ramsay (CSRM) and Magaly Garcia-Vasquez (graduate student with the University of British Columbia) who worked on a closely related project exploring Corporate Culture and Conflict Management. She also thanks David Plumb (Consensus Building Institute) for his collaboration in conducting interviews at one of the mine sites.

The research also benefited from interviews conducted by Sanford Lewis, an independent attorney; with Enterprise Risk Management professionals, and from input by Robert Eccles at Harvard Business School and Ron Nielsen at the Canadian Business Ethics Research Network.

An earlier version of this research, with a more limited dataset, was presented at the First International Seminar on Social Responsibility in Mining, 19-21 October 2011, Santiago, Chile. External funding support was not received for this research. The authors have undertaken research on behalf of companies in the extractive sector as well as for governments, multilateral institutions, and civil society organizations. Deanna Kemp and Anthony Bebbington received funding support from an internal University of Queensland Sustainable Minerals Institute grant to participate in the research.
Stakeholder-related risks in the extractive sector have risen rapidly over the last two decades. Time and again, companies have experienced how negative environmental impacts – such as a spill from a tailings dam – can generate significant negative social impacts as well, for example on local community health and livelihoods. Local communities’ reactions to these impacts can quickly escalate from complaints to protests and road blockades, raising the risks of the company or its security providers using heavy-handed tactics that can lead to even more serious impacts, such as injury or even deaths. This all-too-familiar situation has significant costs – for the community of course, but also for extractive companies themselves.

I drew attention to these issues during my mandate as the former Special Representative of the UN Secretary-General for Business and Human Rights. In my 2010 report to the UN Human Rights Council, I cited a Goldman Sachs study of 190 projects operated by the major international oil companies. It showed that the time for new projects to come on stream nearly doubled in the previous decade. In my report I also referred to an independent analysis of a sub-set of those projects, which indicated that non-technical risks accounted for nearly half of all risk factors faced by these companies, with stakeholder-related risks constituting the largest single category. One international oil major that shared its findings with me on a non-attribution basis estimated that it may have experienced a US$6.5 billion value erosion over a two-year period from stakeholder-related risks.

The authors of this study – Rachel Davis and Daniel Franks – have carried out important follow-up research that confirm and deepen these findings. From this research we learn that extractive companies do not typically identify and aggregate the full costs arising from conflict with local communities into a single number that would catch the attention of senior management or Boards. Instead, they tend to be rolled into local operating costs. This is ironic, if not perverse, because the positive things that companies do to try and prevent such losses do show up as direct costs.

We also learn that the single most often overlooked cost is staff time spent managing conflicts with local communities. But as I illustrated above, such conflicts can easily escalate – and then come the major advocacy campaigns and law suits, which certainly do show up on the corporate ledger.

The good news is that, as my UN business and human rights mandate demonstrated, the kinds of policies and processes that extractive companies (and others) need to put in place to prevent and address negative social impacts and their associated costs are clear and increasingly well-understood. The study highlights the connections between key systems – for identifying social impacts, responding to grievances, and tracking performance – that responsible companies in the extractive sector are putting into place and refining in order to better manage their social impacts.

This report is the first to systematically evaluate both confidential and publicly available data of the costs of company-community conflict on such a scale, drawing as it does on 45 confidential interviews with leading practitioners and 50
public cases of sustained company-community conflict. It builds on CSRI’s work exploring the growing range of influences and approaches that shape the actions of global companies, beyond the regulatory sphere alone.

As the Faculty Chair of CSRI, and as the Chair of the Board of Shift, I am particularly pleased to introduce this important report and to commend it to you.

John Ruggie
Berthold Beitz Professor in Human Rights and International Affairs, Harvard Kennedy School
Affiliated Professor in International Legal Studies, Harvard Law School
Faculty Chair, Harvard Kennedy School
Corporate Social Responsibility Initiative
Over the past decade, high mineral and energy commodity prices have driven expansion of the extractive sector. Mineral and energy developments profoundly transform environments, communities and economies – and can often generate social conflict. This study seeks to answer the question: if the costs of conflict experienced by companies in the extractive industry were better understood, would relationships between companies and local communities receive greater priority and attention? Through in-depth interviews and empirical case analysis, the study explores the value at stake when companies in the extractive sector experience conflict with local communities.

The study involved detailed case analysis of publicly available information regarding 50 situations of prolonged or otherwise significant company-community conflict, as well as 45 in-depth confidential interviews with individuals from, or with great experience in, the extractive industry. The research shows that most extractive companies do not currently identify, understand and aggregate the full range of costs of conflict with local communities. Although company-community conflict may generate the same broad effects as those caused by technical problems, contractual or regulatory disputes, or environmental or safety breakdowns (such as a reduction in or suspension of operations), it is typically not given equivalent attention or resources.

In the research, costs were understood broadly as meaning any negative impacts on a company’s tangible or intangible assets, including value erosion, from failing to avoid, mitigate or resolve conflict at an early stage.

The case analysis revealed that environmental impacts such as pollution typically precipitate or trigger conflict, while broader social and economic issues (such as the distribution of project benefits or the quality of the company’s ongoing consultation processes) typically underlie situations of conflict. These underlying issues can affect the quality of the relationship between the company and community and lead to a situation in which a trigger is more likely to set off a confrontation. Nearly half of the cases analyzed involved a blockade, while a third involved a fatality or injuries, damage to property, or the suspension or abandonment of a project – a particular risk in the feasibility and construction stages.

The research explored the most frequent, greatest, and most often overlooked costs of company-community conflict. The most frequent costs were those arising from lost productivity due to temporary shutdowns or delay. For example, a major, world-class mining project with capital expenditure of between US$3-5 billion will suffer costs of roughly US$20 million per week of delayed production in Net Present Value (NPV) terms, largely due to lost sales. Direct costs can accrue even at the exploration stage (for example, from the standing down of drilling programs).

The greatest costs of conflict identified through the research were the opportunity costs in terms of the lost value linked to future projects, expansion plans, or sales that did not go ahead. The costs most often overlooked by companies were indirect costs resulting from staff time being diverted to managing conflict – particularly senior management time, including in some cases that of the CEO. There may also
be costs associated with the inability to recruit and/or retain top talent, particularly in the community relations function.

The “language of costs” was seen as being particularly useful for a company’s community relations/social performance team in reaching two key audiences: senior management and financial colleagues. One company had undertaken a systematic review of the potential costs of non-technical risks connected to its various projects and identified a significant figure – a value erosion of more than $6 billion over a two-year period, representing a double-digit percentage of its annual profits – which it used to attract Board-level attention to these issues. Interviewees cautioned against relying on pure cost-benefit analysis; rather, those within companies that had experienced success with cost-based arguments emphasized the need to tie them closely to anecdotal experiences and to the company’s own values when communicating with internal audiences. The need for reliable data was emphasized; interviewees noted various challenges in determining causality when attributing certain costs to company-community conflict, and in aggregating costs across different projects or regions.

Interviewees saw a need for extractive companies to better understand the costs – in the sense of loss of value – that can arise from failing to build sustainable relationships with local communities; for example, a less-resilient supply chain or an unreliable local workforce, and the impact that this can have on core business. They highlighted the need for companies to distinguish their social investment spend from what they allocate to social risk mitigation; confusing the two tends to lead to a focus on money rather than on building relationships, as a way to address problems, and to rewarding those individuals who are most vocal while ignoring others who may also have real concerns.

Industry experts observed that the triggers of company-community conflict are increasingly predictable, yet not enough companies are using root cause analysis or similar processes to evaluate such incidents and learn the relevant lessons. Certain other company systems and processes were seen as particularly relevant to identifying (and preventing) costs arising from conflict, including impact assessment, risk and commitment registers, and operational-level grievance mechanisms.

Taking the necessary time to prevent and address such conflict, particularly the time needed to build sustainable relationships through engagement with local communities, is often in tension with short-term production targets or ambitious construction schedules. A failure to identify the connections between distinct budget lines (e.g., between security costs and community relations) can also limit understanding of these issues. Conversely positive internal incentives can help enhance attention to the costs of conflict – and the action needed to prevent it. The research highlighted some examples of creative approaches to social performance objectives and indicators by extractive companies.

External incentives that can enhance company attention to these issues include evidence of impacts on capital – for example, in a key study analyzing the impact of company-community relationships on the stock prices of Canadian gold mining juniors. Reputational impacts remain hard to quantify, but heightened stakeholder attention to issues of materiality and reporting regarding social
impacts appear likely to drive greater attention to this area.

Interviewees observed that effective management of community expectations requires “front-loading” the company’s investment in community relations. This may be easier for large multinationals with positive cash flow, while smaller and medium-size companies may face constraints in this regard. Limits on cash flow at the start of a project can lead a company to adopt an approach that relies on remediation of social impacts after things have gone wrong, rather than seeking to prevent impacts, and conflict, from occurring. Yet experienced interviewees emphasized that it only gets more expensive to try to “buy support” later in the project lifecycle and that this almost never leads to sustainable relationships. Analyzing the costs of conflict can thus help community relations staff to make the business case for increased attention to community engagement before severe impacts occur and the company reaches a tipping point in its relationships.

Finally, the research explored a number of market drivers of greater company attention to company-community relationships. These include project lenders and insurers, some of whom are increasingly sensitive to their clients’ social risk exposure – and to their own as a result. In some cases, this is translating directly into financial risk for lenders. For example, there is emerging evidence in Peru to show that banks are exposed to higher default rates on the financial support that they provide to small businesses or individuals in areas around extractive projects that are experiencing high levels of company-community conflict. There is also increasing awareness of these issues among juniors because of the growing implications for successful onwards sale of assets, and among business customers and consumers in areas like conflict minerals and coal. Government, of course, can play a variety of roles – as a source of positive pressure on the sector, as a hindrance to company efforts, or as a potential partner in joint venture situations.

Overall, the research suggests that improved identification and analysis of the costs of company-community conflict is important for the extractive sector. It identifies a range of factors that are likely to influence the extent to which companies pay attention to these costs, and invest in the underlying relationships with local communities.
A. BACKGROUND

The extractive industry can bring significant social, economic and environmental change to the regions in which they operate, which can lead to conflict between the company and local communities. Company-community conflict can also arise because change is experienced differently by different stakeholders and can be inequitable or incompatible with community members’ values and interests.

A 2008 study of 190 projects operated by the major international oil companies showed that the time needed for projects to come online has nearly doubled in the last decade, causing significant increase in costs. A confidential follow-up analysis of a subset of those projects, which informed the work of Professor John Ruggie, the former Special Representative of the UN Secretary-General for Business and Human Rights, found that non-technical risks accounted for nearly half of the total risks faced by such companies, and that stakeholder-related risks constituted the single largest category. It also estimated that, over two years, one company may have experienced a US$6.5 billion value erosion from non-technical risks, amounting to a double-digit percentage of its annual operating profits.

Separately, an empirical study of 19 publicly traded junior gold mining companies has found that two-thirds of the market capitalization of these firms is a function of the individual firm’s stakeholder engagement practices, whereas only one third of the market capitalization is a function of the value of the gold in the ground. Recent research has also sought to better understand the implications of broader conflict contexts at the company level (for example, on production costs and on company exit from a conflict-affected market).

This report is the product of research into how, and the extent to which, companies in the extractive sector currently identify and understand the costs arising from conflict with local communities around their operations. Many companies are familiar with costing and managing various potential areas of conflict in their operations, including employee, consumer, business-to-business and business-to-government disputes. Responsible companies also routinely implement preventative and protective measures against the risk of failures in their health and safety and environmental systems. However, companies are not as advanced in understanding the costs of conflicts with local communities and often do not appear to analyze the costs that can arise at different stages in a project’s lifecycle, aggregate those costs over the full life of the project, and recognize the potential value that is at stake. Clear lines of accountability also may be lacking, especially where no single company is involved in the full lifecycle of the project — creating the potential for disputes and confusion over where responsibility lies for conflict arising from actions taken at earlier stages of the project.

There is a growing recognition within the extractive sector of the importance of a “social license to operate”. However some commentators, including from within the industry, observe that too many extractive companies still regard stakeholder-related risk as an entirely external phenomenon that cannot be prevented or “managed.”

This study seeks to answer the question: if the costs of conflict experienced by companies in the extractive industry were adequately understood, would their relationships with local communities receive greater priority and attention?
B. RESEARCH OBJECTIVES
Through in-depth confidential interviews and empirical case analysis, the study sought to explore how an understanding of the costs of conflict – the negative impacts on a company’s tangible and intangible assets – might change the way companies engage with local communities around mineral and energy developments.

In the research, costs were understood broadly as meaning any negative impacts on a company’s tangible or intangible assets, including value erosion, from failing to avoid, mitigate or resolve conflict at an early stage. ‘Conflict’ was defined broadly along a continuum, from low-level tension to escalated situations involving a complete relationship breakdown or violence.8

In this paper, we use the term “social risk” to refer to risks experienced by local community actors and “business risk” to refer to risks experienced by company actors. As the research shows, social and business risks are increasingly inter-related.

The research sought to build knowledge about how companies can assess, aggregate and understand the costs of conflict with local communities around their operations, and the potential loss of value where this is not done. Communities, governments and other stakeholders can and do experience significant costs as a result of such conflict; however, the objective of the research was to identify the costs by companies in such instances, in order to gain greater insight into the business case for improved risk management aimed at avoiding and mitigating company-community conflict.

The research team recognized the risks inherent in adopting a simple cost-benefit approach to the management of social impacts, including human rights impacts. Instead, the research sought to explore the utility of quantification-based arguments that are closely linked to a company’s values to support improved management of social risks and impacts as part of broader corporate risk management in the extractive sector.

C. RESEARCH METHODOLOGY
The research was led by Rachel Davis from Harvard Kennedy School’s Corporate Social Responsibility Initiative (CSRI) and Shift, and Daniel Franks from the Centre for Social Responsibility in Mining (CSRM) at the University of Queensland’s Sustainable Minerals Institute.

The research consisted of three main stages:
• Stage 1: Desktop research, more than 45 confidential interviews, development of a working typology of potential costs and application of the typology to 50 publicly available cases;
• Stage 2: Field research in Peru to test emerging findings;
• Stage 3: Refinement of typology and analysis of data.

In Stage 1, initial research was conducted into relevant literature looking at costing efforts in the environmental, occupational health and safety and other “ESG” areas more broadly. Scoping interviews were conducted with key individuals from relevant organizations, including extractive companies.
Building on the results of the desktop research and scoping interviews, the research team then pursued over 45 in-depth confidential interviews using a common interview protocol with individuals from extractive companies, industry bodies, corporate law firms, lenders and insurers, and research institutes. The bulk of these interviews were conducted in 2010-2011. A list of organizations that participated in the interview process and agreed to have their name included is contained in Annex A.

Interview questions were semi-structured and focused on the most frequent, greatest and most often overlooked types of costs that arise from such conflict; the methods used for identifying, assessing and aggregating these costs; where responsibility for managing them is assigned; whether information about such costs is used for the purposes of wider decision-making and/or incentive structures within extractive companies; and what the major incentives and disincentives may be for extractive companies to better understand such costs. Interviews were held in person and by telephone, and were between 60-90 minutes in duration.

In parallel, the research team developed a classification or typology of costs experienced by extractive companies (included in Section II (A) below). The team then examined 50 emblematic cases of company-community conflict, drawing on publicly available information to determine the nature and scale of community conflict in the extractive industry and coding relevant information (see Annex B for the full coding terms). Material for the case analysis was drawn from primary and secondary data sources, including fieldwork, media, company reports, advocacy and industry organizations, academic literature, legal cases and other publicly available data. Case details have been anonymized and, where possible, sources have been triangulated to improve accuracy. Data collected for the case analysis included details on the operation and the relevant community (or communities); the issues in dispute (both proximate and underlying); the manifestations of the conflict; and, where possible, details of the costs experienced by the companies involved. The coding did not differentiate between alleged and actual issues in dispute, partly due to the difficulty in reaching an objective assessment in any particular case, but also in order to capture the diversity of perspectives among the parties to conflicts. Further details of the case analysis methodology are provided in Annex C.

A selection of these cases was then explored in further detail in Stage 2 of the project through field research in Peru – a country with an active mining industry with current conflict issues. The second stage of the research fed directly into, and benefited from, a related study on Corporate Culture and Conflict Management in the Extractive Sector, also undertaken by CSRI in collaboration with Shift and CSRM, which explored the internal organizational factors (including corporate culture, leadership, policies and systems) that influence a company’s approach to handling conflict with local communities.

Five companies agreed to participate in the Corporate Culture and related Costs of Conflict research: Compañía Minera Antamina, an open pit copper-zinc mine owned by GlencoreXstrata, BHP Billiton, Teck and Mitsubishi; Rio Tinto Peru’s La Granja copper exploration project; Barrick Gold’s 100 percent owned and operated...
Pierina open pit gold mine; Tintaya, an open pit copper mine 100 percent owned and operated by Xstrata Copper (now part of GlencoreXstrata); and Yanacocha, with its complex of five gold mines, owned by Newmont Mining Corporation, Minas Buenaventura and the International Finance Corporation.

The five sites represented different stages of the mine lifecycle, from advanced exploration all the way through operations and toward mine closure. Interviews were conducted with personnel (both individually and in groups) from a broad range of functions, including senior management, technical departments (exploration, construction, operations), procurement, government relations/communications, legal, human resources, security, social/community relations and social development. Interviews were conducted between May and July 2011, with most undertaken at the site level. They were conducted on a confidential basis, using a common interview protocol, either in English or Spanish, with simultaneous interpretation where necessary. Researchers primarily used qualitative research methods; however, they sought to gather quantitative information where possible.

In Stage 3, data from the initial and field research stages was analyzed and the typology adjusted and refined to reflect, where possible, gaps in the way in which companies assess and aggregate such costs that may inhibit understanding of their scope and impact. The research team’s analysis focused on exploring the extent and nature of the business case for improved risk management aimed at avoiding and mitigating company-community conflict.

D. REPORT STRUCTURE

The remainder of this report is divided into two main parts. Section II outlines the typology of costs developed by the research team, and the results of the case analysis undertaken.

Section III then explores cross-cutting themes arising from the interviews, namely:

A. The greatest, most frequent and most often overlooked costs of conflict;
B. The utility of quantification as a “language;”
C. Incentives (internal, external and perverse);
D. Timelines (relating to project schedules and conflict escalation); and
E. Market drivers (including lenders, insurers, junior extractive companies, large corporate customers and government).

Section IV offers some reflections on further research.
A. TYPOLOGY OF COSTS

In Stage 1, the research team developed a typology of costs experienced by extractive companies arising from conflict with local communities (see Table 1 below). The typology was initially drawn from existing literature, and was then expanded and verified – with interviewees, through related field research, and detailed case analysis.

The types of costs identified fell into two broad categories: costs associated with preventing or responding to conflict (e.g., security, risk management, personnel costs) and costs associated with the outcomes of conflict (e.g., project modification, redress, material damage, lost productivity, impact on capital, reputational impact, and impacts on personnel). In keeping with the project’s definition of costs, it also includes loss of value.

TABLE 1. TYPES OF COSTS THAT MAY BE EXPERIENCED BY EXTRACTIVE COMPANIES AS A RESULT OF CONFLICT WITH LOCAL COMMUNITIES

<table>
<thead>
<tr>
<th>TYPES OF COSTS TO COMPANY</th>
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<tbody>
<tr>
<td>Security</td>
<td>• Payments to state forces or company security contractors</td>
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<tr>
<td></td>
<td>• Increased operational costs of security: fences, patrols, escorts, transport, alarm/leak monitoring systems, reduced mobility</td>
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<tr>
<td></td>
<td>• Increased security training and management: staff time, lost production, cost of programs</td>
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<tr>
<td>Project modification</td>
<td>• Design modification costs: application, redesign, legal</td>
</tr>
<tr>
<td></td>
<td>• Additional works</td>
</tr>
<tr>
<td>Risk management</td>
<td>• Insurance: higher premiums and coverage, risk rating, withdrawal of coverage</td>
</tr>
<tr>
<td></td>
<td>• Legal and conflict expertise: specialist training for staff, additional staff</td>
</tr>
<tr>
<td>Material damage</td>
<td>• Damage or destruction to private property or infrastructure</td>
</tr>
<tr>
<td></td>
<td>• Damage or destruction to public property or infrastructure</td>
</tr>
<tr>
<td>Lost productivity</td>
<td>• Operations discontinued: voluntary closure or enforced through injunction</td>
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<tr>
<td></td>
<td>• Temporary shutdown of operations</td>
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<td></td>
<td>• Lost opportunity for future expansion and/or for new projects</td>
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<tr>
<td></td>
<td>• Disruption to production: temporary or indefinite delays, absenteeism</td>
</tr>
<tr>
<td></td>
<td>• Delays in deliveries/supplies</td>
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<tr>
<td></td>
<td>• Greater regulatory burden/scrutiny</td>
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<tr>
<td>Capital</td>
<td>• Loss of value of property: full write-off, other depreciation, sale at a loss, theft</td>
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<tr>
<td></td>
<td>• Inability to repay debt or default on debt</td>
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<tr>
<td></td>
<td>• Difficulty raising new capital</td>
</tr>
<tr>
<td></td>
<td>• Share price instability/loss in value (within relevant time period)</td>
</tr>
<tr>
<td>Personnel</td>
<td>• Staff time spent on risk and conflict management</td>
</tr>
<tr>
<td></td>
<td>• Costs of remediation: meetings, negotiations, mediators</td>
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<tr>
<td></td>
<td>• Hostage-taking: ransom payments, rescue operations, compensation</td>
</tr>
<tr>
<td></td>
<td>• Arrests of staff</td>
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<tr>
<td></td>
<td>• Injuries to staff and fatalities</td>
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<tr>
<td></td>
<td>• Low morale and stress-related effects</td>
</tr>
<tr>
<td></td>
<td>• Retention: higher salaries, compensation packages, bonuses</td>
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<tr>
<td></td>
<td>• Recruitment: advertising positions, screening, interviewing, induction training</td>
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</table>
The typology suggests that the range of costs experienced by companies may be significant in their scope and magnitude and that conflict is a means by which the social (and environmental) risks posed by projects can translate into serious business risks.

B. EMBLEMATIC CASES OF COMPANY-COMMUNITY CONFLICT

Publicly available information about cases of prolonged or escalated company-community conflict around extractive operations then were analyzed \( (n=50) \) to understand the issues in dispute, the manifestations of conflict, and the project characteristics. The case analysis does not purport to reflect the circumstances of the entire extractive sector, but instead seeks to draw insights from a pool of cases of prolonged or escalated conflict to understand broader trends. The coding did not differentiate between alleged and actual issues in dispute.

A first empirical finding is that environmental issues were the most common issues to precipitate conflict (see Figure 1). Pollution and access to/competition over environmental resources were identified as the most common proximate issues that can trigger conflict (or “issues in dispute”), followed by the absence of opportunities for community stakeholders to provide consent at the outset of projects, and changes affecting community health and safety. However, the most common underlying issues – those that affected the nature of the relationship between the parties and its robustness, while not necessarily precipitating conflict themselves – were socio-economic issues, particularly the distribution of project benefits, changes to local culture and customs, and the quality of ongoing processes for consultation and communication related to the project. Where conflict triggers were present, there were typically underlying issues with the quality of the relationship between the company and community.

A second finding is that the feasibility and construction stages of projects are over-represented in the proportion of conflicts that led to the suspension and abandonment of projects (see Figure 2). One explanation is that these periods can represent dramatic transitions for local communities with major project impacts experienced for the first time, including impacts arising from a large influx of workers. However, they also represent time periods when community stakeholders, if mobilized, can influence whether and how projects proceed before capital is sunk, changes become costly to retrofit, revenues begin to be generated, and there are increased incentives

<table>
<thead>
<tr>
<th>TYPES OF COSTS TO COMPANY continued</th>
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<tbody>
<tr>
<td>Reputation</td>
</tr>
<tr>
<td>• Higher expenditure on public relations: consultants, dissemination of information</td>
</tr>
<tr>
<td>• Competitive loss/disadvantage: impact on brand, investor confidence</td>
</tr>
<tr>
<td>Redress</td>
</tr>
<tr>
<td>• Compensation (out of court payments);</td>
</tr>
<tr>
<td>• Fines</td>
</tr>
<tr>
<td>• Increased social and environmental obligations: health care, education and training, provision of other services, clean-up and remediation costs</td>
</tr>
<tr>
<td>• Costs of administrative proceedings or litigation: costs of proceedings themselves, judgment/settlement costs.</td>
</tr>
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</table>
for companies and governments to defend projects.

A third finding is that company-community conflict tends to escalate from campaigns and procedure-based actions through to physical protest. Strikingly, half of the cases analyzed involved a project blockade (25 of 50 cases; see Figure 3) while, around a third involved a fatality (21 of 50) or injuries, damage to private property (17 of 50), or the suspension or abandonment of the project (15 of 50).
II. TYPOLOGY OF COSTS AND CASE ANALYSIS

**FIG. 2. CASES OF COMPANY-COMMUNITY CONFLICT: OPERATING STAGE \((n=50)\)**

![Graph showing cases of company-community conflict at the operating stage](image)

**FIG. 3. CASES OF COMPANY-COMMUNITY CONFLICT: MANIFESTATIONS OF CONFLICT \((n=50)\)**

![Graph showing manifestations of company-community conflict](image)
n-depth interviews were conducted with key individuals, primarily from extractives companies, but also from industry bodies, corporate law firms, lenders and insurers (see Annex A).

This section summarizes the key themes emerging from those conversations, namely:
A. The greatest, most frequent and most often overlooked costs of conflict;
B. The utility of quantification as a “language;”
C. Incentives (internal, external and perverse);
D. Timelines (relating to project schedules and conflict escalation); and
E. Market drivers (including the role of lenders, insurers, junior extractive companies, large corporate customers and government).

A. GREATEST, MOST FREQUENT AND MOST OFTEN OVERLOOKED COSTS

Lost productivity in the form of temporary delays in operations was the most frequent cost cited by all interviewees. A major, world-class mining project with capital expenditure of between US$3-5 billion will suffer costs of roughly US$20 million per week of delayed production in Net Present Value (NPV) terms, largely due to lost sales. This figure was confirmed by multiple interviewees and supported by an analysis of project financial data.

For example, at one Latin American mine, a nine-month delay during construction in 2010 resulted in US$750 million in additional project costs. Community conflict in one country led to stoppages and down days that cost another project US$100 million per year. In another case, community conflict that shut down a few key power lines caused an entire operation to halt at a cost of US$750,000 per day. A seven-day blockage of an energy project’s supply route in a Middle Eastern country, which interrupted operations, cost US$20,000 per day.

In at least one case, these kinds of costs had been integrated into “construction costs” in the project budget, which included a 50 percent margin to cover delays due to community conflict. As one interviewee put it with regard to the construction phase:

“When we were building [the mine] the number was frequently thrown around that every day of delay in the construction schedule cost $2 million, partly because of additional costs, but mainly because of delay in the start of the revenue stream.”

Even at the exploration stage, direct costs can accrue: “We’ve got drilling contractors sitting in the nearby town racking up day rates while we negotiate [with the community]. So, there is a cost. In that case it is a few hundred thousand dollars. So, it’s not going to break anybody, but it certainly is not a sensible way to spend a few hundred thousand dollars.”

In the case of initial mineral exploration (early reconnaissance work), interviewees estimated that around US$10,000 is lost for every day of delay – through lost wages and the costs of maintaining an exploration camp. For advanced exploration, involving drilling and geophysical delineation of ore bodies, up to US$50,000 a day can be lost when programs are placed on “standby.”

The most frequently overlooked cost, cited by a significant number of interviewees, was indirect costs arising from staff time being diverted to managing conflict, especially at the senior management level. For one company, the working assumption is that five percent of an asset
manager’s time should be spent managing social risk; yet for one of its subsidiaries in an African country, it is in fact 10-15 percent, and in one Asia-Pacific country, it is as high as 35-50 percent. Company staff successfully used these figures to make the case to management for up-front social risk planning in a new operation the company was developing in the Middle East and North Africa region.

A former senior manager of one operation in a challenging context estimated spending only \( \frac{1}{3} \) of his time on “actually doing my job,” with the rest spent managing internal staff and external community issues arising from conflict. For another company, the CEO’s stated reason for pulling out of a problematic joint venture was that the project was responsible for only 10 percent of the company’s income yet demanded 90 percent of senior management time, including a significant proportion of his own. While not an exact assessment, this illustrated a clear awareness at the highest levels of the company of the scale of the problem. According to another former CEO, managing an asset that only amounted to three percent of the company’s turnover cost 70 percent of his management time and meant that he was unable to focus on other business opportunities.

Interviewees noted that even what one called the “mosquito bites” of constantly needing to “smooth things over” with government regulators, shareholders, lenders and other stakeholders due to low-level conflict can be a drain on staff. Interviewees observed that these kinds of costs can have implications for staff retention and recruitment rates. Some within the industry expressed concern about how hard it can be to find staff with the skills to prevent and address community conflict. As one interviewee put it: “If you lose two or three potentially excellent recruits into a decent-sized corporation, I think that’s already significant, and you want to be making decisions on the basis of that.”

The issue of personnel time is closely related to the opportunity costs arising from conflict. In the words of one interviewee:

“I had a meeting with the CEO and CFO [of a large mining company operating in a conflict-affected country] and they were very clear. They said ‘Listen, [Country X] is only 5 percent of our turnover. We have vast business opportunities in [neighboring Countries Y and Z] and in the rest of the world. We simply don’t have time to look at this stuff. Because [X] is absorbing all our time. It is not about money, it’s about opportunity cost.”

Interviewees identified the greatest costs of conflict as the opportunity costs arising from the inability to pursue projects and/or opportunities for expansion or for sale. For large multinational companies with multiple operations, the financial impact of individual or isolated project delays or interruptions may be hard to detect. But where the company is seeking to expand or acquire major new assets, then the existence of conflict with local communities – and a reputation for failing to prevent or manage it – can hurt a significant potential revenue stream. As one former company manager put it:

“A larger mining company outlives the mine life of the individual mines it has. As one mine plays out, you have to be finding new projects elsewhere in the world and starting new mines … The argument that I made is: ‘If we leave this mess, even if we didn’t cause
it, and there was a certain level [of], not conflict, but I’d say dissatisfaction and potential conflict in those communities, if we leave this thing festering, five years from now you could be going into a community in [Country X] to promote a project and the people say ‘No, we heard what you did in [Country Y] and we don’t want any of that here’. So that long term contribution to reputation or social license…was all about the value of constantly having access to new projects.”

Publicly available examples confirm the magnitude of the costs involved. For example, in February 2006, the developers of the Esquel project in Argentina were forced to write down US$379 million in assets and forego development of US$1.33 billion in projected reserves.12 In 2003, the owners of the Tambogrande project in Peru reported an asset write-down of US$59.3 million following the abandonment of the proposed project, with reserves valued at the time at US$253 million.13 And in November 2012, the owners of the Conga project in Peru suspended construction at the request of the Peruvian government following community conflict. The estimated life production of the deposit is 15-20 million ounces of gold and 4-6 billion pounds of copper, with Newmont, the majority owner (51.35%), reporting capital expenditure of US$1455 million between 2010-2012. Minority partner (43.65%) Compañía de Minas Buenaventura reported capital expenditure of US$498 million on Minas Conga in 2012.14

In another case, a temporary shutdown of a mine was initiated in order to prepare for an expansion, but rising tensions with local communities led to a situation in which the mine could not be reopened. The company decided to engage in a systematic process of community consultation and dialogue and gradually built up a more cooperative environment for addressing community concerns. This enabled the reopening of the mine. The mine was sold five years later for several hundreds of millions of dollars. In the view of a manager at the time of sale, the company risked losing the full sale price if the underlying conflict with local communities had not been addressed.

**B. THE UTILITY OF QUANTIFICATION**

The interviews revealed a range of views about the appropriate role of quantification in relation to business risk arising from problems or a breakdown in relationships with local communities. Key issues included the following, which are discussed in this section:

i. The role of costs in communicating and raising awareness with internal colleagues and in influencing company decision-making;

ii. The challenges that can arise in generating reliable data to feed into assessments of costs;

iii. The importance of distinguishing between the company’s social risk mitigation and social investment spends;

iv. Using retrospective and illustrative approaches that are closely linked to the company’s values versus using cost-benefit approaches to drive ongoing management; and

v. The extent to which existing systems and processes (particularly impact assessment processes, risk and commitment registers, and grievance mechanisms) effectively capture information about social risks, including human rights risks.
i. Internal Communication and Decision-making

Interviewees saw significant potential for quantification of the costs of company-community conflict to help staff with responsibility for managing social impacts to reach two key audiences within the company: senior management and the financial team. Several interviewees, from different departments within extractive companies, felt that community relations staff needed to learn “the language of costs” to better make the case for early mitigation and remediation planning – a finding supported by a related study into corporate culture and conflict management in the extractive sector in Peru.\textsuperscript{15}

One interviewee from the sustainable development field critiqued the profession’s inability to “translate” social issues into costs: “We, just as a discipline, have been useless at doing that. And the more often that we’re able to…quantify the financial impact pro or con in a particular decisions, the more traction you get in a company.” A comparison may also be drawn with the issue of employee health: one company had to go through a two-year exercise to “discover” that it was experiencing a US$50 million loss annually due to sickness absence before the issue got the necessary attention internally.\textsuperscript{16}

One company interviewee cited an incident when a colleague from the social side of the business sought support in order to urgently address escalating community tensions:

“He got traction because he had the standing in the company, people valued his gut instincts. If you don’t have that standing, you’ve got to have a very strong case…But if you put dollars and cents on it, and that was enough to capture people’s attention…then you don’t actually need to be quite that senior to make the impact.”

However, interviewees cautioned that building the capacity of the social team to communicate in the language of costs should not occur instead or at the expense of building further understanding in operational departments about the qualitative aspects of the social team’s work.

One company interviewee suggested that classifying the difference between the way decisions are made on the social and operational sides of the business as “qualitative versus quantitative” risks creating a false dichotomy. Like the technical team, the social team also needs to set out a decision logic about how the company gets from a current to a desired situation – for example, what are the steps needed to ensure that the company has access to the land it needs to operate? Both functions also have a shared interest in prevention and problem-solving, but often express this differently.

“I think one of the … things that often happens is that the non-technical guys get baffled by [the technical side and] think that the engineers have got everything totally under control…Whereas if you’re involved in a feasibility study or a construction project, yes, there’s a general road-map to get from one point to the next, but there’s a hell of a lot of scrambling that goes on to get there, in the same way as there’s a hell of a lot of scrambling that goes on on the community side.”

For social and technical functions alike, “something will come out of left field that you’re going to have to react to, and come up with a work-around. What tends to happen is that a lot of community teams are just in that reactive mode. We can’t predict it, we can’t manage it, just wait until something goes wrong and then we’ll fix it.”
A number of company interviewees felt that senior management, and corporate-level staff more generally, need a better understanding of how social performance can affect core business issues like access to resources or the existence of a safe and secure working environment. As one interviewee put it, the perception often tends to be that if a company is spending one percent of its total turnover on “doing good” through social development programs, then social issues account for, or relate to, only one percent of the business. In fact, there are multiple ways in which an extractive company relates to local communities through its core activities – as an employer, as a procurer of goods or services, and as a natural resource user. Some interviewees said that they had found it helpful to highlight the loss of value to the company in failing to build or maintain the kinds of sustainable relationships with local communities that can lead to a more resilient supply chain or more secure local workforce. (The issue of distinguishing between social investment and risk mitigation spending is discussed further below in Section B(iii).)

Several interviewees raised the challenges of quantifying community support, as opposed to the costs of conflict. More than one interviewee drew a comparison to safety, in that “zero incidents” can be equated more easily with good safety performance than “zero blockades” can be equated with positive community relations.

One experienced industry interviewee reflected on the slow shift by extractive companies toward internalizing social costs of projects. In this interviewee’s opinion, if social externalities were taken fully into account by extractive companies, then between 10-15 mines in Africa alone would need to close; their true cost would make them unsustainable business propositions. Yet some companies in the sector are seen as deliberately entering situations of current or likely conflict with communities based on a business model that accepts the significant non-technical risks – and potential costs – involved.

**ii. “It’s only as good as the data”**

A number of interviewees raised questions about appropriate processes for quantifying the costs of conflict. One pointed to the risk of inflating costs, stating that it can be “very easy to come up with numbers in the very high millions” by combining actual figures for lost production (see Section A above) with assessments of reputational impact, which are much harder to assess (discussed below in Section C(ii)). Another observed that the final investment decision figure for a project often increases significantly from that in the initial proposal for a range of reasons, making it hard to identify how much is the direct result of company-community conflict. Others saw challenges in the variation between projects and the difficulty of isolating causation in some cases:

“We could actually give a…very clear annual accounting on what the cost of community conflict is to us [in one particular project]. We can actually total up the numbers and say, “Well, we lost this many truckloads, which we then subsequently had to do by air freight. It cost us this much in insurance and it cost us this much in headcount to actually just keep the dialogues going.” Plus costs [of impact-benefit sharing agreements and local jobs]. But that’s because it’s a nicely bottle-necked community with one road access.”

The interviews confirmed that stakeholder-related risks are generally not aggregated across a company’s
operations; the focus is usually on the most important projects, financially speaking, from the company’s perspective. A few interviewees queried company or group-wide aggregation as being too “diluted,” contrasting that with the utility of aggregating on a country basis or by issue.

Generally speaking, interviewees felt that the key question is: which lens will help make the business case to senior management? One company interviewee who had presented on the costs of company-community conflict to their company’s Board advised that it was better to acknowledge that it involved “apples and oranges” — i.e., that there are differences between the types of costs that can arise and their susceptibility to measurement — rather than trying to treat them all similarly. In that case, it was left to the Board to make the judgment about the appropriate balance or weight to be given to each.

Another company had undertaken a comprehensive internal review to better understand its exposure to non-technical risk (which included company-community conflict and other costs; for example, delays resulting from permitting problems or local or national political issues). A corporate-level team examined a dozen projects, including projects at both the pre- and post-financial investment decision stage. They asked project managers to identify the costs of delay and other capital expenditure impacts based on existing timelines and budgets, and then the corporate team reviewed the information. The results were scaled for a number of the company’s top projects based on cash flow models. The final figure identified was in excess of $6 billion in costs attributable to non-technical risk over a two-year period — representing a double-digit percentage of the company’s annual profits. The company used this data to attract Board-level attention to the issue; the review occurred at the same time as an internal restructuring process, so the team’s findings helped frame the importance of a strengthened social performance function. Yet the team felt that perhaps it had uncovered only the “tip of the iceberg,” since the review did not take into account other costs, such as staff time or opportunity costs.

### iii. Distinguishing social investment from risk mitigation

A number of interviewees emphasized the importance of distinguishing the costs of a company’s social investment or community development programs from specific measures designed to prevent and mitigate the risks of company-community conflict:

> “Many companies still see social investment as the number one risk mitigation strategy...[So if] you ask [Company A] how much they spend on [Country X] every year, which is probably about USD$60 or 70 million a year, they will do that for no other reason than conflict mitigation, social risk mitigation. The fact of the matter is, it doesn’t work. You know there’s no [Company A] employee that has the nerve to go outside the gate with a [corporate] emblem on his or her shirt. They don’t do it...If anything, it creates more conflict rather than reduces [it]...It is a widely held assumption that as long as you build schools and clinics, that people will be happy and won’t attack you. And the evidence is overwhelmingly that that’s not the case.”

Treating social investment primarily as a risk mitigation tool ignores the impacts of a company’s operational policies and processes on communities. It also means looking at community relations in...
terms of “dollars spent” rather than as a way to build sustainable relationships. Companies that treat social investment as risk mitigation often focus their spend on communities that are the most vocal; while they may have legitimate complaints, the company risks ignoring other communities who also have real concerns.19

A number of interviewees stressed the importance of an “intelligent” community relations spend that focuses on hiring the right staff who are committed to building the kinds of relationships with local communities that prevent and mitigate the risk of conflict. As one put it: “[Y]ou invest resources in staff, not in stuff. You invest in people, not in bricks and mortar.”

Some companies increasingly understand their community relations spend through a risk mitigation lens:

“We don’t talk about conflict so much, but we have a community engagement standard which is mandatory for all of our…sites. And that is there to make sure we don’t have any conflict with the community…So good community relations is a good insurance policy, if you like, and that would always have a budget line as a mandatory requirement for each of our [sites]…So there would never be a conversation where people would suggest abolishing the community engagement [function], for instance, because people have felt the consequences when there isn’t community cohesion, because you have to fear for your life. So now it’s an absolute part and parcel of any budget round.”

“Front-end loading” a community relations budget to help address social risks provides an opportunity for the community relations function to influence the risk picture of the project as a whole. However, project timelines can work against this, as discussed further below in Section C(i). Moreover, for smaller and medium-size companies, it can be hard to allocate sufficient resources up-front because of cash-flow challenges (see Section D(i)).

One interviewee with significant industry experience felt strongly that the triggers for company-community conflict are increasingly predictable and that the kinds of policies and processes needed to prevent and mitigate such conflict are increasingly well-understood; for example, those found in the UN Guiding Principles on Business and Human Rights and the IFC Performance Standards. In this interviewee’s perspective, it is time for companies to move on from an assumption that social conflict cannot be managed: “The cost of corporate prevention needs to be packaged in a much more comprehensive and structured framework to say, ‘Listen, we know this stuff. It’s predictable, there is a logic to it. We have seen it over and over, and we also know what are the minimum tools and the strategies that need to be in place to reduce our risk exposure.’”

Key processes identified by interviewees included processes for meaningful engagement and consultation with affected communities, including seeking the free, prior and informed consent of indigenous communities,20 and putting in place effective operational-level grievance mechanisms (see further Section B(v) below). As another industry expert put it: “I believe that, largely, mining companies get the community relations that they deserve.”

iv. Values-based versus cost/benefit-based approaches

Many interviewees stressed the need to avoid taking a classic “cost/benefit” approach to managing social
Company representatives that have successfully used quantification to help make a business case for improved prevention and mitigation of social risk emphasized that they had been careful to link their use of costs-based arguments to the company’s values and corporate responsibility commitments. Many interviewees strongly cautioned against the idea of creating a quantification-driven “management model” for community relations, which could lead to overly simplistic cost/benefit calculations driving all decision-making.

One company has a system for identifying and aggregating key costs during the operational phase of its projects that is very deliberately linked to the company’s values. In this company, the security function is responsible for weekly reporting on a series of issues (e.g., social disturbances, assaults, trespass numbers, theft, confrontations). A cost is attributed to each instance, using a combination of fixed estimates for certain types of incidents and taking into account compensation or other variable costs in particular cases. The company separately tracks the costs of downtime in various stages of production. When an incident occurs (e.g., a road is blocked or power lines are downed), the company can input the duration of the incident and come up with an approximate dollar figure for the costs involved. Security is responsible for reporting on both sets of figures on a monthly basis to a cross-functional committee that oversees operations. They are also fed into risk assessments that are updated quarterly. The legal function is responsible for presenting information about a range of other costs that can arise from company-community conflict, including not only litigation but also employee dissatisfaction, difficulties with recruitment and so forth, to help convey a more comprehensive picture and to tie this back to the company’s values. In the words of one business leader: “[F]irst and foremost is a values argument; second, is risk.” Key staff members with responsibility for the system commented that it has helped them justify the costs of appropriate prevention and mitigation strategies.

A number of interviewees commented that using root cause analysis can be particularly important, while noting that it is not used as often as it should be with respect to social incidents. In one company, senior management support using root cause analysis to assess social conflicts and have been conducting workshops with the company’s General Managers to familiarize them with the relevant tools. But the majority of companies interviewed did not appear to apply these kinds of methodologies to community conflict situations on a routine basis. Several company interviewees were interested in using the research team’s costs typology to conduct a “lessons learned” analysis.

In one example, an extractive company experienced a strike by its local workforce, which led to a day-long stoppage of its processing plant and coverage in the local media. Company managers acknowledged that if a safety incident had been involved, a root cause analysis would have been promptly undertaken and an action plan adopted. Yet two months later, the underlying causes of the strike had still not been identified or addressed and were beginning to affect broader company-community relations.

III. CROSS-CUTTING THEMES FROM THE INTERVIEWS
v. Relationships with existing systems

Extractive companies are increasingly integrating social, including human rights, impacts into their impact assessment processes, particularly at the initial stages of a project. Some companies were planning to integrate social impacts into their assessments but had not yet done so in a robust way; a few saw them as optional “add-ons” to broader due diligence processes, particularly in brownfield projects. As one interviewee pointed out, poor technical due diligence can also have important implications for social risks.

The timeframe for implementing appropriate management plans to prevent and mitigate identified social (and environmental) risks is usually dictated by other project factors. In some cases, existing legal frameworks may require that appropriate time be factored in – for example, under the consent processes in place in Canada and the Philippines for projects affecting indigenous communities. But often there is a direct tension between “social time” (the time community relations staff need to address community concerns before an activity proceeds) and “technical time” (the timeframe that construction or operations staff are working within due to technical or financial objectives). This can lead to community relationships being under-developed and activities to build trust and prevent conflict rushed in their implementation.

There was surprising variation among company approaches to including stakeholder-related risks in basic risk mapping processes. Most of the companies interviewed used formal risk registers, but not all of them include social risks (or even the business risks that can arise from social risks). One interviewee commented that while community relations staff often keep “fantastic records” of daily interactions, the information is either not used or is used only to assess immediate risks to the short-term construction or production schedule. Confidential interviews with independent enterprise risk management (ERM) experts as part of the research suggested that the collection of data on stakeholder-related risks needs to be automated for effective inclusion in ERM systems, but that the ultimate decision about their impact – on stakeholders and on the company – should be qualitative rather than quantitative and made by appropriately informed individuals. Company interviewees confirmed that internal risk processes are dependent on “good people” to implement them effectively, and noted that even where they do integrate stakeholder-related risks, they frequently suffer from a lack of “follow through.”

In merger and acquisition (M&A) situations, interviewees observed that due diligence typically consists of a desktop review of issues that would meet the traditional financial definition of materiality (discussed further below in Section C(ii)): “[I]t doesn’t take into account community dynamics and whether the project is at a tipping point with regard to the community.” In brownfield acquisitions, there can be real risk in simply accepting the social impact management plan that is already in place. For example, in one such case, an informed interviewee estimated that an oil and gas project was likely to cost US$4 billion instead of US$2.4 billion. Approximately US$750 million of that difference was attributable to the additional efforts necessary to address community conflict issues that were not appropriately identified in the original environmental and social management plan developed by the prior owner of the asset, on which the company had relied when it purchased the asset.
There was significant variation in company use of grievance and commitment registers.\(^2\) Regular use appeared limited to larger companies that were already committed to identifying the linkages between company-community conflict and costs.

An example from Luc Zandvliet and Mary Anderson’s work highlights the harm that failing to track and deliver on commitments right from the earliest stages of a project can cause, both in terms of costs to the company and damage to its relationships with local communities.\(^2\)

“One company started a new project in an area with very demanding communities. The first team on the ground was the seismic department. The community refused to allow the team to conduct a seismic survey unless they promised to build an electrification project. The seismic team agreed. They provided and installed electricity poles during the three months they needed to finish their job. When the drilling department arrived, they were met with hostility; the community felt misled by the company. Instead of an electrification project, they had ended up with poles! In order to be able to do their work, the drilling department promised to finalize the project but ended up doing only the wiring. This ensured peace during the period they were doing their part of the job. Next the pipeline contractor was forced to pay for a power plant before he could lay pipelines. By the time the operations department arrived with the intent of establishing a long-term relationship, the communities had lost confidence in the company. It took the operations department several years to regain community trust. In order to do so it had to complete the electrification project at high cost.”

The high turnover of expatriate staff in mining operations can exacerbate these problems. According to one interviewee: “You can buy the peace for two years...for example, by making promises...or at least they are perceived as promises. By the time the honeymoon is over, people are really ticked off and say ‘Okay, now we want to see some action.’ But the person who made that promise is gone.”

Some interviewees referred to the risks that can arise from the “knock-on” effects when things go wrong at other projects in the area or region, especially those physically close by, when other extractives companies fail to meet their commitments to local communities.

With regard to operational-level grievance mechanisms, some companies were in the process of instituting standardized complaints and grievance handling procedures for community-related incidents. In at least one case, the internal grievance reporting procedures included the ability to record the “cost” of the incident or complaint. Interviewees from the company predicted that it would take time to develop a corporate culture that was supportive of the new procedures, but that they should help the company identify trends in community concerns over time as well as emerging issues. Recent research has explored the potential of such mechanisms to help prevent and address disputes with local communities, when implemented as part of a broader management system for preventing and addressing the company’s negative impacts.\(^2\)
C. INCENTIVES

This section explores the effect of various incentives on increased company attention to the costs of company-community conflict, namely:

i. Internal incentives;
ii. External incentives;
iii. Perverse incentives.

i. Internal – Positive and Negative Incentive Structures

The interviews highlighted the importance of positive internal incentive structures to support the effective prevention, mitigation and remediation of adverse impacts on local communities and associated reductions in the costs of company-community conflict.

There was broad agreement among interviewees that overall responsibility for managing social impacts at the project level needed to lie with an operation’s General Manager. Closely related to this was the perceived need to better integrate social performance objectives and indicators into existing approaches.

Separate research in the extractive sector indicates that where social performance targets do exist in core business functions, they are often “fuzzy.” A few of the companies interviewed were looking to introduce social KPIs into existing “balanced scorecard” approaches that consider production and safety performance, and one company was integrating social performance into the bonus structure for all local staff at one operation. Other examples cited by interviewees included the creation of parallel reporting structures for technical and non-technical risk at the General Manager level in one operation, and tying a country Vice-President’s bonus to zero down days due to community unrest. However, interviewees commented that generally there is no clear reward for “getting it right.”

At the time of interview, one company was introducing a comprehensive ranking system to assess social performance by individual operations. It was being introduced as a self-assessment tool, but the company recognized that it would ultimately need to be backed up by internal auditing to ensure its effectiveness.

Several interviewees stressed the importance of senior level leadership on these issues. For example: “If your CEO is saying the words and just not delivering, then whether you have a bonus system or you have a penalty system, you just end up with a bunch of cynics. If it’s not truly grounded in something that the leadership of the company believes in, then the chances of really creating it are low.”

A common concern emerged around the pressures of quarterly or annual production targets: “You see crazy decisions being made in the last 3 months of the year.” Short-term production targets were seen as incentivizing negative behavior by individual managers that could potentially penalize the company in the long-term. One interviewee described the dangers of rewarding cost saving measures by the General Manager in a poorly handled resettlement process:

“How can a company that knows they’re going to shave off $200,000 on the one side but is going to pay millions in compensation on the other side [do that]? That would not have been the case if there had been incentives to look at the long-term goals of the company, not just the short-term goals of the individual.”
One interviewee commented that even if incentives are tied purely to production levels or profitability, “a smart General Manager knows if he loses his social license, his production levels are going to go down.”

Numerous examples were cited of an aggressive construction schedule contributing to heightened conflict. Lengthy legal permitting times, and a temporary halt due to the global recession, allowed one company to “sensitize” the community (and vice versa) to a project’s implications; this was unusual, and social considerations generally do not drive the company’s construction schedules. In another instance, a company’s “bullish” CEO sought to impress investors by speeding up a project’s construction schedule by 6 months. He brought in a new set of consultants to retrospectively “reevaluate” the project’s social and business risks and overrode the agreed project timetable. But by starting the project without having obtained the community’s agreement to a compensation plan that was required as part of a resettlement process, the company was risking significant conflict and associated costs, of which the market had no awareness.

Interviewees confirmed that security costs are often treated as a completely separate budget item – despite the fact that in some cases, they can comprise up to ten percent of an operation’s annual budget. In one company, the costs of security, damage to company property and resources needed for running the community relations function had been seen as entirely unrelated until quite recently. The implications of disconnected budget lines for staff incentives are neatly captured in the following example:

In one area, international company staff were kidnapped and ransom paid. These payments came from a budget line maintained in the company's headquarters in Europe. On the other hand, the country manager received his rewards for pursuing high production levels and incurring low costs. A closer look revealed that he was deeply criticized by local-hire staff for underpaying them while pushing their productivity. They, therefore, had found that they could increase their incomes by informing community-level criminal groups of the movements of international staff and where and when they could most easily be kidnapped. When ransom was paid, these local staff received a cut of the payment. If the in-country manager had paid the high ransoms from his budget, or if these events had been included in his annual performance bonus, the manager would likely have made different decisions.

**ii. External Incentives**

Interviewees cited a range of external incentives affecting company approaches to the costs of conflict with local communities.

Impacts on capital can be significant. For example, Vedanta’s share price in India dropped by around ten percent on the announcement by the Indian government that the company’s permit to develop a bauxite mine in that country was refused, largely due to the strong opposition to the project that had arisen in the community. In a separate case, one company’s senior management referred to the “[Country X] discount” arising from a particular project that suffered from high levels of company-community conflict because of an internal assessment that the company’s stock was trading at about ten percent below what it should have been as a result of the ongoing challenges with that project.

Research by the Wharton School of Management into Canadian gold mining juniors suggests that
the degree of stakeholder cooperation or conflict at a company’s mines is a critical component in calculating the financial market valuation of the publicly traded parent firms. The research showed that 63 percent of the market capitalization of these companies can be linked to the quality of their stakeholder engagement – double the percentage linked to the value of the actual gold in the ground.

Looking beyond share price, efforts to quantify impacts on reputation are notoriously difficult. There are some aspects that can readily be quantified, for example, increased public relations (PR) costs. In one case, the PR costs for one contentious mine where there was no effective community dialogue process in place exceeded the rest of the company’s PR costs put together. But capturing the true costs of reputational impact remains a challenge. Work at Harvard Business School has sought to outline a more robust approach by companies to reputational risk, including objectively assessing the company’s reputation versus the reality of its performance. There are also a growing number of media analysis tools that allow companies (including lenders) to identify and assess environmental and social issues that may pose reputational risks.

Evolving understandings of materiality may constitute a further external incentive for extractive companies to better understand their impacts on local communities – and the costs involved. In the interviews, external auditors were seen as likely to only consider company-community conflict where it rises to the level of potential litigation or regulatory action, i.e., where it becomes significant enough to require disclosure according to the most narrow, shareholder valuation-based understandings of materiality.

In financial reporting, “materiality” has typically been defined in terms of information that may affect the decisions of a “reasonable investor”. However, this has been understood in different ways – as a valuation-based approach that focuses on a shareholder’s economic decisions (eg, in the International Financial Reporting Standards) or as a broader range of potential decisions made by investors, such as exercising voting rights or bringing shareholder resolutions (eg, in the SEC’s rules in the US). In non-financial reporting, understandings of materiality incorporate the perspective of other stakeholders as well. As companies are increasingly expected – and in a growing number of jurisdictions, such as the EU, are now required – to report on their non-financial performance, the question of how best to define materiality will remain an ongoing and evolving discussion.

iii. Perverse Incentives

Experience shows that when companies persistently ignore – or are seen to ignore – community concerns about noise, dust, or other apparently “minor” issues, community members may feel driven to escalate the situation in order to draw attention to their concerns. Interviewees emphasized the need to talk to those raising concerns early on, and cited examples of cases where a lack of openness by the company led to escalating conflict. Some company interviewees queried whether embedding a costs-focused approach would incentivize “bad behavior” by external actors. In one interviewee’s view: “Increasingly… the people that are creating or are benefiting from conflict know exactly which buttons to push to get what they want.”

Where a company’s bonus structure is entirely driven by production, then as one interviewee put it: “if you interrupt production flows, you can basically ask for anything.” In one case, an oil and gas company
was experiencing US$4 million per day in lost production due to occupation of a flow station. Those responsible went to the facility manager and asked for US$300,000 for a hospital — they had calculated the daily cost to the company of the production stoppage and knew that the company would agree to build the hospital.\textsuperscript{40}

The terms of agreements with local contractors can also lead to perverse incentives. Contractors are typically unwilling to bear the risks arising from community conflict; if community unrest prevents a contractor from being able to work, the contractor may be able to activate a \textit{force majeure} clause in the agreement and claim the penalty amount. Contractors may therefore be incentivized to stir up community conflict. In one instance, the costs to a company of a local contractor activating a \textit{force majeure} clause amounted to US$29 million for a five-month project that had a budget of US$120 million. This highlights the critical importance of effective supplier/contractor engagement by extractive companies, which encourages or requires contractors to take responsibility for dispute resolution with the local community and helps build their capacity to do so.

\textbf{D. TIMELINES}

This section explores issues relating to the impact of timelines on extractive companies’ efforts to manage the costs of company-community conflict, including issues relating to liquidity, “tipping points” and the challenge of retaining community relations staff over the life of a project.

\textbf{i. Early community expectations versus late liquidity}

Interviewees pointed to the tension between the high expectations generated among local communities in advance of a project coming online and the fact that revenues often come late in the project lifecycle. Many companies calculate their community relations budget as a percentage of operational expenditure, but the need for engagement and consultation does not follow the production schedule. Community relations needs often tend to be greatest up-front, in the feasibility and construction phases. In the words of one interviewee, companies need social experts on the ground “\textit{before construction is even in the wind}.”

Yet according to company interviewees, many of the costs typically associated with preventing and addressing company-community conflict are allocated to closure or de-commissioning stages, reflecting a remediation rather than prevention-based approach, which is often driven by cash-flow concerns during the project lifecycle.

In addition, a company’s social performance spend during the exploration or construction phase is typically not recoverable from the host government under the terms of the investment agreement should the project not proceed. The same may apply under agreements with project financiers.

A failure to make the kind of front-end investment — in time as well as resources — to manage local communities’ expectations can result in a poor relationship that only becomes harder to “fix” over time. One interviewee observed that larger companies may be in a better position to address these pressures because they have positive cash-flow and can afford to implement the systems necessary to avoid conflict right from the start, including slowing down the project schedule to allow the necessary time to engage with local communities.
Interviewees acknowledged that there were costs in seeking to develop and maintain good relationships with local communities from the earliest stages of a project. But these need to be compared to, as one interviewee put it: “the different cost if things go bad and people don’t trust you and there comes a time when you almost have to buy your way back into people’s good graces…Rather than by having an agreed upon sustainable development plan [instead] you respond to short-term requests for support, for projects and so forth, [to] win your way back into the hearts of people.” Others pointed out that “buying” community support has never proven to be an effective strategy for preventing or mitigating conflict over the long term.

If tensions or conflict arise in the middle of a project, there can be a sudden “downwards pressure” from the commercial function on the community relations team, and also on the legal team, to promptly fix the problem: “What are we going to tell our financiers?” But as one company interviewee put it: “Speed is not good if you’re trying to create community consensus, social cohesion for your project, and manage expectations.” Interviewees noted that greater internal coordination at the earliest stages of a project can help the commercial team present a more accurate picture of the social risks, including the potential costs, of a project to a host government in order to help manage expectations in that relationship as well.

As one industry expert reflected, the best extractive companies are those that have the skills and systems to not only manage expectations but specifically to “manage disappointment” in processes or outcomes – whether among local community members, the government, or their own staff.

### ii. Escalation and tipping points

Interviewees stressed the need for extractive companies to understand that once a relationship has broken down, it is very hard to re-create a sense of respect through belated relationship-building efforts. As one interviewee put it: “This is not like retro-fitting in the safety context.” Dispute resolution experts drew a distinction between contexts in which conflict can be “captured and regularized” by institutions and those where it cannot; the former may increase some costs (e.g., of litigation) but can also allow for the resolution of disputes by facilitating access to information, experts and agreed-upon processes. In the latter kind of situation, resilient company-community relationships become all the more important.

One interviewee contrasted the experience in community relations with other areas like safety, and the “persuade me” attitude that prevails among management regarding social risk: “It almost takes a disaster before one sees much widening of awareness.” Such “disasters” can force companies to realize that, for example, they risk not being able to get a reasonable price for existing assets in the future. For others, it is more about tarnishing their reputation for excellence and project delivery. Some companies have used such emblematic cases in community relations staff induction programs and in presentations to senior management. Interviewees agreed that the language of quantification can be especially useful in alerting companies to the importance of these issues before they reach this kind of “tipping point.”

The interviews explored whether there were relevant differences in the reactions of mid-tier extractive companies in this regard. Generally mid-tier companies do not want to be first or last
but rather “to be right in the middle with our head below the parapet and just stay out of trouble and be invisible.” Yet several examples were cited of such companies starting to more consistently include social risks in their due diligence processes and impact management plans, suggesting that this is increasingly becoming part of accepted practice. As one interviewee put it:

“But how are companies reacting who haven’t been burned – who are just in the middle of the stream, who haven’t had an active case, who haven’t had a terrible shareholder resolution, and haven’t had these experiences? My experience is that those middle companies are changing a lot.”

iii. Valuing and retaining community relations professionals

As noted above in Section A, the interviews identified the most often overlooked cost of company-community conflict as staff time spent managing conflict. Additionally a range of other staff-related costs may be associated with conflict. Where conflict sets in, company staff can become “numb”: “Their mindset is ‘we’ll find a way through it’ or if we can’t then the government will step in and ‘sort it out.’” Company interviewees observed that community relations or social performance staff may find themselves falling into this kind of approach because of the company’s insistence on pursuing an unrealistic project schedule. The field research in Peru confirmed the toll that stress-related issues can take on community relations staff, leading not only to absenteeism but also lower retention rates – another type of conflict-related cost.

While it can be hard to put a figure on the value of good community relations, as one company interviewee stated: “Day in, day out, it would just be nicer to walk around town with people that appreciate you rather than being hostile to you.” Where this is lacking, it can take a persistent daily toll on staff – particularly for those working in remote or otherwise challenging locations.

An experienced extractive sector recruiter observed that the kind of cross-cultural communication skills that are critical in community relations roles are often not valued at the corporate level. As one company interviewee put it: “Without being skeptical, I think there are few companies that really, really truly value the expertise of their community relations people…They’re sort of at the asset protection level and…well, the asset protection guys are just security guys.” Without a change in this mindset, interviewees observed, extractive companies risk exacerbating staff-related costs associated with company-conflict – as well as the personal toll on the individuals involved.

E. MARKET DRIVERS

This section deals with some key market drivers – namely, lenders, insurers, junior extractive companies, large corporate customers, and, finally, the critical role of governments.

i. Lenders

Lenders can be an important driver of social performance standards in the extractive industry. Lenders are increasingly likely to look at the company’s track record, the specific context in which a loan is being applied, and the kinds of policies and processes that the company has in place to prevent and address conflict (often through the lens of the revised IFC Performance Standards or updated Equator Principles).
Based on the interview research, environmental or social concerns about a project often result in conditions being attached to a loan rather than a direct impact on price. Yet one lender reported rejecting roughly ten percent of transactions on environmental or social risk grounds, on the basis that companies with sound stakeholder relations tend to be sound financial performers as well.

Some lenders take the view that there can be significant costs resulting from company-community conflict, but do not seek reduce them to a dollar figure. Stakeholder-related risks tend to be addressed separately to credit risk, on a parallel path by separate staff within the financial institution. The credit risk team is focused on the borrower’s ability to repay, while the social risk team is generally focused on whether the borrower has enough funds set aside to resolve any grievances that may arise – if not, that may potentially trigger concern on the credit risk side.

Large lenders appear to be increasingly considering the risk to their own reputation of company-community conflict in the projects that they finance. For some lenders, this is translating directly into financial risk. For example, there is emerging evidence in Peru to show that banks are exposed to higher default rates on the financial support that they provide to small businesses or individuals in areas around extractive projects that are experiencing high levels of company-community conflict. This is one of the factors motivating the approach being taken by the Peruvian Superintendency of Banks, Insurers and Private Pension Funds (SBS) to incentivize better management of social conflict by companies in that country, particularly in the extractive sector.

Social conflict, resulting in part from local communities’ concerns about the impacts such projects may have on their livelihoods, welfare and human rights, is seen as having implications for the credit risk of individual Peruvian banks, the stability of the Peruvian financial system, and the reputation of Peru as an investment location. The SBS is considering regulations that would encourage improved engagement and consultation by extractive companies with local communities. This is likely to include, in higher-risk investments, an independent assessment of the quality of the company’s relationships with the local community, and thus go beyond the formal policies and processes a company may have in place.41

**ii. Insurers**

Insurers are increasingly looking at non-technical risk in the projects they underwrite, largely driven by an awareness of risk to the insurer’s own reputation. While technical risk assessors are seeing increasing linkages between technical and non-technical risks, and hence the importance of clients having good social risk management systems, they are struggling with how to consistently factor this into pricing.

Based on the interview research, insurers’ non-technical risk assessments are generally desk-based and involve researching whether the client is simply “unacceptable” (for example, because they have been involved in gross human rights abuses with no indication of a willingness to reform and improve their practices), or whether further due diligence is needed because of the sensitivity of the particular activity or context (for example, investments in tar sands operations).
One insurer requires a site visit for all extractive sector projects by both a country risk expert and an environmental and social risk expert. In the last six years, three projects have been denied coverage on environmental or social grounds following engagement with the client; the key issue from the insurer’s perspective is whether the client is willing to engage, not whether it has the up-front capacity to implement appropriate policies and processes on its own. Where financing involves this kind of “hand-holding” approach with the client on social issues, this may be reflected in the insurer’s processing fees; for example, for one institution the fee might rise to US$75,000 from a regular fee of $20-25,000 on a $300,000 premium.

There is increasing discussion among the OECD group of Export Credit Agencies (ECA) regarding improved management of social risk by their clients. Of particular note is the recent adoption of an Environmental Human Rights Policy and Due Diligence Procedure by the Norwegian ECA, GIEK.42

iii. From Juniors to Majors
Junior companies within the extractive sector often play an important role in locating resources and proving the geological and development potential of a project. The business model of many exploration juniors is dependent on the ability of the company to sell the project to a larger development partner with the skills and experience to take the project through to the feasibility, construction and eventually operational phases.

Some interviewees saw poor community relations as having the potential to reduce the value of acquisitions. For example:

“What a lot of juniors don’t seem to realize is that if at the time they’re doing that drilling, reducing the technical risk, they increase the social license risk by doing things that promote conflict, they can severely reduce the value that they could ever hope to sell a project for, or maybe not be able to sell it at all. In the case of [Project X], the junior mining company that was doing that had hopes of selling out to a big company like [Company Y]. But nobody was interested because of the conflict situation.”

iv. Seeing large corporate customers as a proxy for numerous small customers?
Compared to companies in sectors like apparel or food and beverage, companies in the extractive sector are generally less exposed to cumulative pressure from a large number of small customers to improve standards or social performance. However, this is no longer quite as clear-cut as it once was.

Beyond those oil and gas companies that have downstream or retail operations, other extractive companies are starting to find that consumer pressure further down the value chain is impacting on their own businesses. For example, civil society demands on European power companies is creating upwards pressure on some of the largest coal companies to improve their environmental and social performance – a key driver behind the “Bettercoal” initiative. Consumer pressure has also led to heightened attention to the issue of “conflict minerals” – meaning tantalum, tin, tungsten or gold from mines in conflict-affected or otherwise high-risk areas, which are often characterized by widespread or significant human rights abuses, including forced and child labor. The OECD has developed Due Diligence Guidance for Responsible Supply Chains of Minerals for Conflict-Affected and High-Risk Areas, which sets out a five-step
framework for conducting due diligence that is closely aligned with the UN Guiding Principles on Business and Human Rights. \(^{43}\)

Companies paying greater attention to the conflict minerals issue include those in the automotive, electronics and food and beverage sectors, some of whom are now seeking to map their own supply chain back to the minerals extraction stage. \(^{44}\) A range of cross-sectoral initiatives, many informed by the OECD Guidance, have emerged to support companies seeking to source responsibly from conflict-affected and high-risk contexts. For example, the World Gold Council has developed a Conflict-Free Gold Standard, intended to assure customers and investors that gold produced under the standard has not fueled, or contributed to human rights abuses associated with, armed conflict. \(^{45}\) It seeks to provide companies with an assessment framework to track gold from the mine through the refining process.

Other certification schemes that have emerged in the extractive sector include the Initiative for Responsible Mining Assurance, the Responsible Jewelry Council and Equitable Origin. These initiatives suggest that extractive companies are increasingly exposed to downstream consumer-related pressures when it comes to their social performance.

\(\textbf{v. Government}\)

Government – at the national, regional or local levels – can play a critical role in either facilitating or undermining positive company-community relations. Extractive companies may have to address “legacy issues” (problems that they did not create) in order to ensure good relationships; for example, where the land involved in a project was originally acquired by the government through a flawed acquisition process, leaving local community members lacking adequate compensation, or worse. Leading international standards increasingly recognize the need for companies to take proactive steps to investigate, and sometimes supplement, government processes in such situations. \(^{46}\) In other cases (for example in the Philippines), the relevant authorities have rejected company-community agreements presented by a company for approval on the basis of inadequate consent processes.

Some leading companies are increasingly seeking to help build government capacity to run effective consultation and consent processes. As one interviewee put it, “\textit{Who else is going to do it?}” For other companies, internal pressure to just “get the deal done” with local officials can lead to attempts to short-cut consultation and consent processes. But as one interviewee pointed out, “\textit{There are very few communities where not everything is known, so the moment you buy off the local politicians, the whole world knows about it,}” which generates the potential for serious conflict.

In some cases, project interruptions or delays arising from company-community conflict may be linked to broader issues beyond the particular company’s operations. It may be hard in these situations to disentangle political and social risk; what appear to be local community concerns can quickly escalate and become overtly “political” issues and the company’s risk exposure can suddenly change. In some cases, one company’s failure to “unlock” or address a particular conflict situation with local communities may lead to a negative political dynamic that can be problematic for the industry as a whole in that region, or even that country. Companies can experience direct costs in such situations from the increased time that has to be spent on government relations,
and from the loss of value in no longer being the
government’s business partner or investor “of
choice.” They may also lose other advantages, such
as foregoing tax concessions.
This study demonstrates that the costs of company-community conflict are both real and significant for extractive sector companies. Greater awareness of this reality should contribute to a broader paradigm shift in the sector, which recognizes the critical importance of building sustainable relationships with local communities around extractive operations.

Some areas highlighted by the research that the team believes would benefit from further investigation include:

- How can the industry move away from the perception that community relations is simply “spending other’s money” and place an appropriate value on its sustainability professionals? Are there relevant parallels from the development of a robust health and safety culture in the industry that can be drawn on here?

- The research revealed concerns among interviewees about attributing causation when it comes to community incidents, while at the same time revealing a general lack of use of root cause analysis processes. Case studies on effective tracking and incident investigation systems in the health and safety and environmental fields (where the focus is on physical conditions but the ‘people factor’ is still critical) may be helpful in moving beyond this stalemate.

- The research highlighted a number of attempts to develop and refine incentive structures that would encourage greater attention to community relationships among all relevant extractive company staff (beyond the community relations function). It could be valuable to further document these systems, and their effectiveness, in detail as they continue to evolve.

- In the period since the interview research was conducted, there have been developments among state-based lenders (such as international and regional banks, and national Export Credit Agencies and Development Finance Institutions) in terms of their understanding of how companies can better prevent and manage conflict with local communities and their expectations in this regard are increasing. Further research into these evolving expectations could help communicate the importance of this growing market incentive for company attention to these issues.

- Finally, early conversations indicate the relevance of the typology of costs developed by the team to other business sectors, as they seek to embed effective policies and processes to prevent conflict with affected stakeholders. There may be interesting comparative work to undertake in this space.
Annex A

Organizations Participating in Interviews

Allens Arthur Robinson
AngloAmerican
AngloGold Ashanti
Arcelor Mittal
Ateneo School of Government, Philippines
Barrick Gold Corporation
Berne Declaration
BG Group
Both Sides Now Consulting
BP
Centre for Sustainability in Mining, University of Witwatersrand
Chevron Corporation
Citi
Compañía Minera Antamina
Compañía Minera Doña Inés de Collahuasi
Credit Suisse
Critical Resource
De Beers
Downing Teal
Foley Hoag
Freeport-McMoRan Copper & Gold
Goldcorp
International Finance Corporation
Multilateral Investment Guarantee Agency
Newcrest Mining
Newmont Mining Corporation
Norman B Keevil Institute of Mining Engineering, University of British Columbia
Oxfam America
RESOLVE
Rio Tinto Minera Peru
Shell
Synergy
Swiss Re
Triple R Alliance
World Resources Institute
Xstrata Copper Perú (now part of GlencoreXstrata)
Yanacocha
Annex B
Case Coding Terms, including Typology of Costs

### ISSUES IN DISPUTE

1. **Social and cultural change** *(potential ‘p’ or actual/alleged ‘a’)*
   - a. Population and demographics: e.g., migration, social inclusion, growth/decline of community/town, workers camps;
   - b. Social infrastructure and services: e.g., housing; skills shortages/retention; health; education and training;
   - c. Crime and social order: e.g., corruption, domestic violence, sexual violence, substance abuse and trafficking, prostitution; change in social norms;
   - d. Community health and safety: e.g., disease; vehicle accidents; spills; controlled release; pollution; disruption of traditional food supply;
   - e. Labor issues: e.g., health and safety; remuneration; freedom of association; discrimination;
   - f. Security issues: e.g., behavior of security personnel (government, company, contractors); targeting/repression of activists; suppression of demonstrations;
   - g. Culture and customs: e.g., breakdown of traditional roles; changing production/employment base; community cohesion; effects of cash economy; ‘sense of place’; community leadership; cultural heritage;
   - h. Vulnerable and marginalized groups: e.g., disproportionate or particular effects on women, children, disabled, elderly, ethnic minorities, indigenous peoples, artisanal and small-scale miners etc.

2. **Economic change** *(potential ‘p’ or actual/alleged ‘a’)*
   - a. Distribution of benefits: e.g., employment; profit flows; royalties and taxes; training; procurement; supply chain; community development; compensation; managing expectations; equitable distribution (across state/regional/local/ethnic/class/family or other lines); effects of cash economy; technology transfer; corruption;
   - b. Inflation/deflation: e.g., housing (ownership/rents); food; access to social services;
   - c. Infrastructure: demands on/investment in roads, rail, ports etc.

3. **Socio-environmental change** *(potential ‘p’ or actual/alleged ‘a’)*
   - a. Pollution (source of or sink for): e.g., air (dust); water (acid and metaliferous drainage, cyanide, tailings seepage, riverine and submarine disposal); soil; noise; scenic amenity; vibration; radiation; traffic etc.
   - b. Resources (access to/competition over): e.g., land; water (groundwater, river, ocean); mineral resources; cultural heritage; forest resources; human; biodiversity;
   - c. Resettlement: e.g., consent and consultation in relation to resettlement; compensation; ties/relationship to land; equity; adequacy of resettlement housing and facilities; livelihoods
   - d. Disturbance: e.g., disruption (including exploration); consent and consultation in relation to land access; frequency and timing; compensation.

4. **The Process of Change** *(potential ‘p’ or actual/alleged ‘a’)*
   - a. Consultation and communication: e.g., transparency; timing; inclusiveness; clear reporting; access to decision-makers; respect for customs and traditional authority structures;
   - b. Consent: e.g., sovereign consent (indigenous/FPIC or government); community consent (non-sovereign);
   - c. Participation: e.g., development of programs; monitoring; selection of alternatives and technologies; planning operational aspects;
   - d. Redress: e.g., dispute resolution; company-level grievance mechanisms; accessibility; transparency; dialogue and engagement; third party mechanisms;
   - e. Agreements: e.g., equity; clarity of obligations; duress; capacity and governance; honoring commitments/performance; new corporate entity/transfer of obligations; cross-border projects; corruption;
   - f. Community development: e.g., participation; adequacy; appropriateness; capacity to deliver; prioritization; corruption.

*Potential ‘p’ refers to conflict over what might happen; Actual/alleged ‘a’ refers to conflict over current projects/activities/issues (alleged events are taken as actual for the purpose of this typology).*
### MANIFESTATIONS OF CONFLICT

1. **Procedure-based** (generally non-violent)
   - a. Submissions: e.g., to government (national, state, regional, local) or company (local subsidiary or parent company); petitions;
   - b. Administrative proceedings: e.g., formal complaint through state-based or IFI mechanisms; other international bodies;
   - c. Litigation: e.g., claim brought in jurisdiction where company operates; claim brought in jurisdiction where parent company/majority shareholder is domiciled; class/group action; representative proceeding; injunction; damages;
   - d. Publicity: e.g., public meetings; use of media; campaigns; involvement of NGOs;

2. **Physical protest** (may be violent or non-violent – see 3 and 4 below)
   - a. Demonstration: e.g., local/state/regional/national; involving mining personnel also or only (strike);
   - b. Blockade: e.g., entry to site; road; access route; railway line; port;

3. **Violence to property**
   - a. Private property: e.g., damage or destruction of equipment/installations/buildings; interference with private infrastructure; small/large-scale;
   - b. Public property: e.g., damage or destruction of equipment/installations/buildings; interference with public infrastructure; small/large-scale;

4. **Violence to the person**
   - a. Injuries: e.g., to community members; to company employees; involvement of company security forces; public security forces (police or military);
   - b. Deaths: e.g., of community members; of company employees; involvement of company security forces; public security forces (police or military).

### TYPES OF COSTS TO COMPANY

1. **Security**
   - a. Higher payments to state forces or company contractors;
   - b. Increased operational costs of security: fences, patrols, escorts, transport, alarm/leak monitoring systems, reduced mobility;
   - c. Increased security training and management: staff time, lost production, cost of programs;

2. **Project modification**
   - a. Design modification costs: application; redesign; legal;
   - b. Additional works

3. **Risk management**
   - a. Insurance: higher premiums and coverage; risk rating; withdrawal of coverage;
   - b. Legal and conflict expertise: specialist training for staff; additional staff;

4. **Material damage**
   - a. Damage or destruction to private property or infrastructure;
   - b. Damage or destruction to public property or infrastructure;

5. **Lost productivity**
   - a. Operations discontinued: voluntary closure or enforced through injunction;
   - b. Temporary shutdown of operations;
   - c. Lost opportunity for future expansion and/or for new projects;
   - d. Disruption to production: delays, temporary or indefinite, absenteeism;
   - e. Delays in deliveries/supplies;
   - f. Greater regulatory burden/scrutiny;

6. **Capital**
   - a. Loss of value of property: full write-off, other depreciation, sale at a loss, theft;
   - b. Inability to repay debt or default on debt;
   - c. Difficulty raising new capital;
   - d. Share price instability/loss in value (within relevant time period);
TYPES OF COSTS TO COMPANY continued

7. Personnel
   a. Staff time spent on risk and conflict management;
   b. Costs of remediation: meetings, negotiations, mediators;
   c. Hostage-taking: ransom payments, rescue operations, compensation;
   d. Arrests of staff;
   e. Injuries to staff and deaths;
   f. Low morale and stress-related effects;
   g. Retention: higher salaries, compensation packages, bonuses;
   h. Recruitment: advertising positions, screening, interviewing, induction training;

8. Reputation
   a. Higher expenditure on public relations: consultants, dissemination of information;
   b. Competitive loss/disadvantage: impact on brand, investor confidence;

9. Redress
   a. Compensation (out of court payments);
   b. Fines;
   c. Increased social and environmental obligations: health care, education and training, provision of other services, clean-up and remediation costs;
   d. Costs of administrative proceedings or litigation: costs of proceedings themselves; judgment/settlement costs.

COMPANY RESPONSES TO CONFLICT

1. Short-term response: containment and mitigation
   a. Implementation of emergency response plan;
   b. Increased use of security personnel (government, company, contractor);
   c. Legal/administrative action against claimants, e.g., injunctions, counter-claims;
   d. Immediate remediation efforts: e.g., clean-up; treatment of affected individuals;

2. Dispute resolution
   a. Participation in dialogue with claimants after dispute has arisen (employees, community members, other stakeholders); convening community/public meetings; negotiations;
   b. Providing redress: e.g., undertakings; compensation (out of court payments); changes to existing agreements/arrangements;
   c. Financing expert/independent studies or audits: e.g., water/air/soil quality assessments, medical assessments, investigation of recent conflict;
   d. Implementing recommendations of expert studies or audits: e.g., revision of internal policies;

3. Conflict management
   a. Development and implementation of a grievance mechanism;
   b. Assignment of internal responsibility and budgeting for conflict management;
   c. Development of policies, reporting, due diligence, root cause analysis and other systems to identify potential sources and impacts of conflict;
   d. Recruitment and training of community relations personnel;
   e. Training of security personnel.

STAGE OF OPERATIONS

1. Planning (including government approval of leases)
2. Exploration
3. Pre-feasibility and feasibility (including government approval of permits)
4. Construction
5. Operations
6. Expansion (under existing licence)
7. Closure
8. Post-closure

Note: at each stage if suspension (‘s’) or abandonment (‘a’) occurs.
### DISTINGUISHING FACTORS

1. Indigenous
2. Conflict zone
3. Post-conflict zone

### CASE DETAILS

1. **Country**
2. **Primary Commodity**
3. **Company type**
   - Exploration Junior
   - Operating Junior
   - Mid-tier
   - Diversified Major
   - State-owned
4. **Time Period of Analysis**
Annex C
Case Analysis Methodology

Case studies of company-community conflict around mining operations \((n=50)\) were analyzed to generate an understanding of the issues in dispute, the manifestations of conflict, as well as the geographic and project characteristics (such as the project life-cycle stage).

The cases span time periods from 1967-2012; however, the vast majority of cases had a time period of analysis that began after the year 2000 (41 of 50 cases), and in no case did the time period of analysis end prior to the year 1998. The cases represent a diverse spread of geographic locations (Figure S1), company type (Figure S2) and primary commodity (Figure S3). The criteria for selecting cases were inclusive. Cases were identified where prolonged or escalated tensions existed between local communities and extractive projects and where adequate information was publicly available to code the case. Industrial action on labor issues that did not escalate into wider community conflict was not sought for inclusion within the sample frame.

The case pool was selected based on the availability of secondary data in gray and published literature and the first-hand field experience of the authors. The coding typology was iteratively developed from existing literature interviews and case analysis (see Annex B).

Case material was identified through primary and secondary data sources, including industry journals, print media (including by search of the Factiva database), networks, academic literature, legal cases, company and civil society organization reports and websites of companies and civil society organizations. Case details were anonymized and, where possible, sources were triangulated to improve accuracy. The coding does not differentiate between alleged and actual issues in dispute, partly due to the difficulty in reaching an objective assessment in any particular case, but also in order to capture the diversity of perspectives among the parties to conflicts. Multiple issues were identified for the vast majority of case studies so that percentages correspond to the proportion of the cases in which the issue was identified.

Due to the method of data collection and the type of data sources, the case sample frame may contain biases. Media reports and civil society organizations are likely to highlight dramatic issues and cases. It would be incorrect, for example, to conclude that where an extractive sector company is subject to prolonged low level tensions that the likelihood of project abandonment is as represented in our case sample. Exploration projects may be under-represented where conflicts are local and small-scale. Furthermore, English language data sources may under-report some geographic regions or types of company (such as state-owned enterprises), particularly where the country of origin of the extractive company is the same as the project location. That said, a reasonable geographic spread is evident in the data. The case analysis therefore does not purport to represent the circumstances of the entire extractives sector but instead to draw insights from a case pool of prolonged or escalated conflict between local communities and extractive projects.
FIG. S1. CASES BY GEOGRAPHIC LOCATION (CONTINENT; \( n = 50 \)).

- Oceania 28%
- South America 26%
- Asia 20%
- Sub-Saharan Africa 18%
- Central America and the Caribbean 4%
- North America 4%

FIG. S2. CASES BY MINING COMPANY TYPE (\( n = 50 \)).

- Major 37%
- Mid-Tier 20%
- Operating Junior 27%
- Exploration Junior 12%
- State Owned 4%
- Sub-Saharan Africa 18%
FIG. S3. CASES BY PRIMARY COMMODITY (n=50).

- Gold 34%
- Copper 22%
- Shale Oil 4%
- Coal 10%
- Nickel 6%
- Iron 4%
- Zinc 2%
- Silver 4%
- Platinum 8%
- Diamonds 2%
- Uranium 4%
- Coal 10%
- Shale Oil 4%
- Copper 22%
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## Issues in Dispute

- **Potential (P)**
  - Social and Cultural Change
  - Economic Change
  - Socio-Environmental Change
- **Actual (A)**
  - Security Issues
  - Distribution of Benefits
  - Pollution or Pollution Source
  - Resource Access
  - Disturbance
  - Resettlement
  - Compensation
  - Consent
  - Participation
  - Redress
  - Agreements
  - Community Development

### Table of Dispute Issues

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- **Social and Cultural Change**
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- **Economic Change**
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- **Socio-Environmental Change**
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- **The Process of Change**
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<td>Gold</td>
<td>Operating Junior</td>
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<td>2000-2010</td>
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<td>47</td>
<td>Peru</td>
<td>South America</td>
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<td>48</td>
<td>Australia</td>
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<td>49</td>
<td>New Caledonia</td>
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<td>Peru</td>
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<td>Copper</td>
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</tbody>
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### Manifestation of Conflict
- Physical protest
- Violence to property
- Violence to person(s)

### Stage
- Demonstration
- Blockade
- Damage to private property
- Damage to public property
- Injuries to people
- Deaths

### Time Period of Analysis
- 2008-2009
- 1999-2001
- 2001-2003
- 2003-2005
- 2005-2010
- 1985-2006
- 2000-2008
- 2009-2012
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- 2012-2012


8. The authors do not assume that conflict leads always to negative outcomes; some forms of conflict offer productive pathways for resolution of issues.


15. See Rees et al, note 11 above.


17. One project that has sought to explore aspects of the value creation model through a cross-sectoral approach is EABIS, Sustainable Value: Corporate Responsibility, Market Valuation and Measuring the Financial and Non-Financial Performance of the Firm, 2009.

18. This is the figure reported in Professor John Ruggie's 2010 report to the UN Human Rights Council referenced in note 4 above.


22. For more on this example, see Zandvliet and Anderson, note 19 above, p 199.


25. From a human rights perspective, decisions about the severity of social risks need to take full account of the severity of impacts from the perspective of potentially affected stakeholders; see Office of the High Commissioner for Human Rights, The Corporate Responsibility to Respect Human Rights: An Interpretive Guide, 2011, pp 83-84. In the context of the operations of oil
and gas companies, see European Commission, Oil and Gas Sector Guide on Implementing the UN Guiding Principles on Business and Human Rights, 2013, pp 43-44.

26 Grievance registers are used to account for potential liabilities; typically, they become part of the company’s general liability register and appear in the company balance sheet. Registers of commitments made by the company to local communities can be incorporated into ongoing social performance reviews and planning.

27 Recounted in Zandvliet and Anderson, note 19 above, pp 137-138. See also Corporate Engagement Project et al, Preventing Conflict In Exploration: A Toolkit for Explorers and Developers.


31 Drawn from Zandvliet and Anderson, note 19 above, pp 194-195.


34 Henisz et al. Note 5 above.


36 See, e.g., http://www.reprisk.com. RepRisk monitors independent third party sources – all major print media, NGO reports, news sites, governmental agencies and blogs – and assesses a company and project’s environmental, social and corporate governance risk exposure on a daily basis.

37 See, e.g., the Global Reporting Initiative’s G4 Sustainability Reporting Guidelines.


39 In the dispute resolution sphere, there is a large body of work looking at models of conflict escalation that draw in new actors and/or tactics as the conflict increases; see, for example, Thomas Jordan’s English translation of Friedrich Glasl’s conflict escalation model, available at http://www.perspectus.se/tjordan/.

40 For more on this example, see Zandvliet and Anderson, note 19 above, p 193.


46 See IFC, Performance Standard 5 on resettlement, paras 30-32 and Performance Standard 7 on indigenous peoples, paras 21-22.

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