Validation of Madagascar

Final Validation Report

Adam Smith International Independent Validator

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1. EXECUTIVE SUMMARY

The Government of Madagascar announced its commitment to the EITI in 2007 and was accepted as an EITI Candidate in February 2008. Following its suspension by the EITI Board for political instability in October 2011, interrupting the country's Validation under the EITI Rules, Prime Minister Jean Omer Beriziky issued a Ministerial Order in March 2013 reactivating EITI Madagascar and establishing a permanent EITI National Committee. The EITI Board lifted Madagascar's suspension in June 2014 and the government issued Decree 2017/736 in August 2017 institutionalising the EITI under the Prime Minister's Office. The MSG is chaired by the Minister of Mines and Petroleum (currently Ying Vah Zafilahy) and consists of eight representatives each from government, industry and civil society.

On 24 October 2016, the Board agreed that Madagascar's Validation under the EITI Standard would commence on 1 September 2017. This draft validation report follows on from a quality assurance review of the International Secretariat's initial assessment. The Validator agrees with the Secretariat's preliminary assessment that requirements 1.1, 1.3, 1.4, 2.2, 2.4, 2.6, 4.1, 4.4, 4.6, 4.7, 4.9, 5.1, 5.2, 6.2 and 7.4 have not met the requirements of the EITI standard. However, we recommend that 4.9 be upgraded from inadequate to meaningful progress.

2. BACKGROUND

With a USD 391 per-capita GDP in 2016, Madagascar's population of 24m is amongst the world's ten poorest. Yet Madagascar holds extensive deposits of minerals: it accounts for roughly 4% of global ilmenite production, 2% of cobalt and 1% each of global mined nickel, rutile and zirconium. Madagascar also has a tradition of artisanal mining of gold, sapphires, rubies, aquamarines, tourmaline, topaz, amethysts and emeralds, largely exported to Sri Lanka and Thailand for processing, despite a ban on precious stone exports since 2008. The large informal economy of over half a million artisanal miners operates often in unsafe working conditions. With some 5% of the world's fauna and flaura species, 80% of which are endemic to the island-state, environmental concerns are paramount to CSOs' priorities.

From the late 1950s onwards, the French-owned SOTRASSUM[1] mined monazite, ilmenite and zircon in south-eastern Madagascar in partnership with the state. The French company COMINA has mined chromite from the west coastal region of Andriamena since 1968 and was nationalised as KRAOMA in 1975, among the largest mining projects in Madagascar to date. During the isolation following the 2009 Coup d'état, the HAT focused on promoting Asian investment, most visibly when China's third-largest steel-maker WISCO acquired the rights to the Soalala iron deposit with a USD 100m signature bonus in 2011. A series of large mining projects have provided the impetus for a rebound in economic growth since the end of the political crisis in 2013. Rio Tinto's USD 931m QIT Madagascar Minerals (QMM) ilmenite and zircon project in the southeast Anosy region, in which the state holds a 20% stake, began production in 2009. The second project, one of the world's largest nickel and cobalt mine at Ambatovy developed by Sherritt International, Sumitomo Corp. and Korea Resources Corp., represents a USD 7bn investment that started producing in 2012. While extractives contributed a modest 4.18% of GDP in 2014, the Ministry of Mines and Petroleum (MPMP) expects the sector to grow to 6%-8% by 2020. Although the value of exports covered by Madagascar's 2014 EITI Report accounted for only 6.3% of total exports, the IMF classifies Madagascar as a resource-rich country given that the value of total mining exports, including informal exports of gold and precious stones, accounting for over a quarter of total exports. However, the decline in commodity prices has meant that new large-scale mining projects have yet been confirmed.

[1] Société de traitement des sables du sud de Madagascar, a subsidiary of Groupe Pechiney Ugine Kuhlman.

While oil exploration has a long history in Madagascar, a succession of foreign companies including ELF, Chevron, Agip and Amoco never found commercially-viable deposits that warranted the relatively high cost of production. However, Madagascar is considered to be a new frontier for oil and gas prospecting, with ten international oil companies holding a total of 17 oil and gas blocks. The government has been working with data providers (TGS, BGP, Spectrum, CGG) to promote investment in 229 available blocks. Exploration work to date has identified five active oil systems, including both conventional light oil as well as heavy crude and tar sands, although onshore exploration is at a more advanced stage than offshore. The London Alternative Investments Market-listed Madagascar Oil was granted production rights for two unconventional oil blocks in April 2004. With potential reserves of up to 1.2bn barrels and 1.7bn barrels of crude oil respectively, Madagascar Oil struck a farm-out agreement with Total in 2008, selling a 60% stake in Bemolanga for USD 100m. While the 2008-2011 search for tar-sand oil at Bemolanga was unsuccessful, Total has continued its exploration for conventional types of oil since. Meanwhile, pilot heavy oil production commenced at Tsimiroro in 2015.

The Government of Madagascar's initial commitment to implement the EITI in Madagascar was made in 2007 by Former President Marc Ravalomanana. Madagascar was declared "candidate country" in February 2008 by the EITI Board. The EITI Madagascar MSG and Regional Committees were created in July 2010 under the HAT, which issued a press statement on 14 September 2011 confirming the government's commitment to EITI. Although Madagascar had been suspended since October 2011, former Prime Minister Jean Omer Beriziky signed the Ministerial Order No. 5615/2013 in June 2013 reactivating the EITI National Committee. In October 2013, former EITI Champion and Minister of Mines Rajo Daniella Randriafeno noted that the publication of the 2011 EITI Report despite five years of political instability was a sign of the government's commitment to strengthening governance in the extractive sector.

Following the lifting of Madagascar's suspension on 6 June 2014, President Hery Rajaonarimampianina opened the first International Fair on Mines, Hydrocarbons and Equipment in Madagascar on 19 June 2014 by reaffirming the government's commitment to implementing the EITI. On 21 and 22 April 2015, former EITI Chair Clare Short was welcomed by Prime Minister Jean Ravelonarivo and other high-level officials. The promulgation of the 2017 Decree on 30 August 2017 is the most recent sign of the government's public engagement by institutionalizing EITI Madagascar.

In line with the Validation Guide, the International Secretariat carried out the first phase of validation—initial data collection, stakeholder consultations, and preparation of their initial evaluation of progress against the EITI requirements (the "Initial Assessment"). Adam Smith International (ASI) was appointed as the independent Validator to evaluate whether the Secretariat's work was carried out in accordance with the Validation Guide. ASI's principal responsibilities as Validator are to review and amend the Initial Assessment, as needed, and to summarize its independent review in this Validation Report for submission to the Board through the Validation Committee.

1. Work Performed by the Independent Validator

The Secretariat's Initial Assessment was transmitted to ASI on March 13th, 2018. Our Validation Team undertook this phase of the Validation process through: (1) In-depth review and marking up of the EITI Assessment by each team member; (2) Detailed review and comments by the Multi-Stakeholder Specialist of Requirements 1 and the Civil Society Protocol; (3) Detailed review and comments by the Financial Specialist of Requirements 4, 5 and 6; (4) Consolidation of reviews and the production of this draft Validation Report, sent to the International Secretariat on the April 5th, 2018.

2. Comments on the Limitations of the Validation

The Validator carefully reviewed the Secretariat's Initial Assessment and at this stage has no comments on the limitation of the validation process.

3. Comments on the International Secretariat's Initial Assessment

The initial data collection, stakeholder consultations, and drafting of the Initial Assessment were generally undertaken by the International Secretariat in accordance with the 2016 Validation Guide. The data collection took place across three phases. Firstly, a desk review of the available documentation relating to the country's compliance with the EITI Standard, including but not limited to:

- The EITI work plan and other planning documents such as budgets and communication plans;
- The multi-stakeholder group's Terms of Reference, and minutes from multi-stakeholder group meetings;
- EITI Reports, and supplementary information such as summary reports and scoping studies;
- Communication materials;
- Annual progress reports; and
- Any other information of relevance to Validation.

Secondly, a country visit took place on 20-25 November 2017. All meetings took place in Antananarivo. The secretariat met with the MSG, the Independent Administrator and other key stakeholders, including stakeholder groups that are represented on, but not directly participating in, the multi-stakeholder group (MSG).

Finally, the International Secretariat prepared a report making an initial assessment of progress against requirements in accordance with the Validation Guide. The initial assessment did not include an overall assessment of compliance. The report was submitted to the Validator, with the National Coordinator (NC) also receiving a copy.

2. GENERAL COMMENTS

- **Progress in EITI Implementation**

The EITI Standard is highly relevant to the challenges Madagascar faces in managing its extractive industries. Madagascar presents a unique case of delicate biodiversity, with an expansive artisanal, small-scale and largely informal mining sector that accounts for an estimated 40% of the world's sapphire market, and handful of large mining, oil and gas projects. The complexities of its mining licensing system, fiscal decentralization and state participation in the extractives sector are particularly suited to the EITI's multi-stakeholder governance model. As highlighted in its 2017 EITI work plan, Madagascar has sought to address key challenges in license management, geophysical data and extractives revenue management through its EITI implementation. Overcoming funding and capacity challenges and uneven engagement of its different constituencies, EITI Madagascar has made a tangible impact on extractives governance, from providing statistics on production and exports to contributing to the launching of an online mining cadastre in 2017. EITI Madagascar has focused on key areas of public interest, for instance reviewing mining license management since the 2011 moratorium on new license awards, while EITI data on subnational payments, transfers and social expenditures has empowered mayors in communes and regions to demand their statutory share of extractives revenues.

- **Impact of EITI Implementation**

The EITI has been described by several stakeholders as a "safety net" for extractives governance during a turbulent period following Madagascar's 2009 coup, even after the lifting of its EITI suspension in 2014. With limited funding, the MSG compensated for declining secretariat support by becoming more involved in the operational oversight of EITI implementation in the 2015-2017 period. Madagascar has always had strong multi-stakeholder mechanisms in its EITI implementation, yet deviations in practice and the frequency of MSG membership renewals have affected institutional memory, particularly of government and civil society. Driven by strong industry participation, the MSG's frequent meetings saw declining engagement from the other two constituencies and were rarely quorate, reducing stakeholder buy-in to key MSG decisions. Government and civil society members of the MSG have tended not to actively represent their constituencies in the past two years. While this may have steered EITI Madagascar's focus towards issues of greatest concern for industry, such as mining licensing, it has also ensured the EITI's sustainability during extended funding gaps and lacklustre government engagement in 2015-2017. The government's institutionalisation of the EITI through a Decree in August 2017 is a welcome sign of renewed government engagement, although the quality of implementation and operational government engagement will be key to ensuring the EITI's sustainability over the longer term.

Yet EITI Madagascar's attention to detailed reconciliation has not always been matched with consideration of the non-revenue information now required under the EITI Standard, nor with efforts to improve underlying government systems and routine disclosures. The MSG's focus on the comprehensiveness of reconciliation has tended to detract from other issues of relevance to Madagascar's extractives industries, such as the structure of state participation in the mining sector and budget revenue traceability. The opportunities for increasing EITI's impact are as significant as its achievements to date, from public finance management issues involving traceability of off-budget revenues to state participation in the mining sector and the existence of transportation revenues. Key to achieving EITI objectives will be embedding EITI reporting in routine government and company systems, including for contextual information on the contribution of the sector to the economy and comprehensive data on exports from artisanal and small-scale mining of gold and precious stones. While EITI has proved sustainable by operating in a reforming silo in the past decade, linking to other ongoing reforms will be crucial to achieving the EITI's full potential in Madagascar. Thus, clarifying SOEs like KRAOMA's financial relations with the government will be key not only to fulfilling requirements of the EITI Standard, but also in meeting conditions of the IMF's 2016 extended credit facility. Providing an annual diagnostic of audit and assurance practices would support the Court of Account (CdC)'s reforms and improve transparency of companies' audited accounts. The EITI could also support the Ministry of Finance and Budget (MFB)'s efforts to streamline subnational transfers by institutionalising local governments' oversight, supported by existing innovative tools such as the IT application launched this year to improve the transfer of mining administration fees (FAM) to local communes and regions.

The Independent Validator's Assessment of Compliance

Figure 1 – Validator's assessment

EITI Requirements		LEVEL OF PROGRESS				
Categories	Requirements	No progress	Inadequate	Meaningful	Satisfactory	Beyond
MSG oversight	Government engagement (#1.1)					
	Industry engagement (#1.2)					
	Civil society engagement (#1.3)					
	MSG governance (#1.4)					
	Work plan (#1.5)					
Licenses and contracts	Legal framework (#2.1)					
	License allocations (#2.2)					
	License register (#2.3)					
	Policy on contract disclosure (#2.4)					
	Beneficial ownership (#2.5)					
	State participation (#2.6)					
Monitoring production	Exploration data (#3.1)					
	Production data (#3.2)					
	Export data (#3.3)					
Revenue collection	Comprehensiveness (#4.1)					
	In-kind revenues (#4.2)					
	Barter agreements (#4.3)					
	Transportation revenues (#4.4)					
	SOE transactions (#4.5)					
	Direct subnational payments (#4.6)					
	Disaggregation (#4.7)					
	Data timeliness (#4.8)					
	Data quality (#4.9)					
Revenue allocation	Distribution of revenues (#5.1)					
	Subnational transfers (#5.2)					
	Revenue management and expenditures (#5.3)					
Socio-economic contribution	Mandatory social expenditures (#6.1)					
	SOE quasi-fiscal expenditures (#6.2)					
	Economic contribution (#6.3)					
Outcomes and impact	Public debate (#7.1)					
	Data accessibility (#7.2)					
	Follow up on recommendations (#7.3)					
	Outcomes and impact of implementation (#7.4)					

Legend to the assessment card

	The country has made no progress in addressing the requirement. The broader objective of the requirement is in no way fulfilled.
	The country has made inadequate progress in meeting the requirement. Significant elements of the requirement are outstanding and the broader objective of the requirement is far from being fulfilled.
	The country has made progress in meeting the requirement. Significant elements of the requirement are being implemented and the broader objective of the requirement is being fulfilled.
	The country is compliant with the EITI requirement.
	The country has gone beyond the requirement.
	This requirement is only encouraged or recommended and should not be taken into account in assessing compliance.
	The MSG has demonstrated that this requirement is not applicable in the country.

3. DETAILED FINDINGS

This section highlights areas where the Validator disagrees with the findings of the Initial Assessment or requires further clarification.

With regard to Requirement 1.4 on MSG governance, the Validator notes that since the Validation took place the MSG has approved its Internal Rules. The Validator recommends the MSG publish these Internal Rules as soon as possible and would highlight that implementation of these, along with the provisions of the August 2017 Decree, will of course be essential moving forward.

4. RECOMMENDATIONS

1. In accordance with Requirement 1.1, the government must be fully, actively and effectively engaged in the EITI process. The government is required to appoint a senior individual to lead the implementation of the EITI. The appointee should have the confidence of all stakeholders, the authority and freedom to coordinate action on the EITI across relevant ministries and agencies, and be able to mobilise resources for EITI implementation. To further strengthen implementation following the institutionalisation of EITI Madagascar through the 2017 Decree, the government is encouraged to further entrench EITI funding in government budgeting to ensure the sustainability of EITI implementation over the long term. In accordance with requirement 8.3.c.i, the government constituency should develop and disclose an action plan for addressing the deficiencies in government engagement documented in the initial assessment.

2. In accordance with requirement 1.3.a, the civil society constituency should demonstrate that they are able fully, actively and effectively engaged in the EITI process. Specifically, civil society should ensure that they are able to fully contribute and provide input to the EITI process and that they have adequate capacity to participate in the EITI. In accordance with requirement 8.3.c.i, the civil society constituency should develop and disclose an action plan for addressing the deficiencies in civil society engagement documented in the initial assessment.

3. In accordance with Requirement 1.4.b.vii, the MSG should ensure that there is sufficient advance notice of meetings and timely circulation of documents prior to their debate and proposed adoption. The MSG is encouraged to ensure that deviations from their ToR are recorded and transparent. Government and company constituencies are encouraged to ensure that their representatives' attendance at MSG meetings is consistent and of sufficiently high level to allow the MSG to take decisions and follow up on them. In accordance with Requirement 1.4.b.viii, the MSG must keep written records of its discussions and decisions.

4. In accordance with Requirement 2.2, a description of the process for transferring or awarding the license and the technical and financial criteria used should be publicly available. Not least given the significant debate surrounding license movements in the mining sector, EITI Madagascar is encouraged to use EITI reporting as a diagnostic tool for non-trivial deviations from the applicable legal and regulatory framework governing license transfers and awards. In cases of competitive tender for mining, oil and gas licenses, the MSG will have to disclose the list of applicants and the bid criteria for licenses awarded through a bidding process. The MSG is encouraged to consider stakeholders calls for further analysis on the efficiency and effectiveness of licensing procedures in Madagascar.

5. In accordance with Requirement 2.4, EITI Madagascar should clarify and document the government's policy on disclosure of contracts and licenses, as well as actual practice, including any reforms that are planned or underway.

6. In accordance with Requirement 2.6, the MSG should ensure that a comprehensive list of state participation in the extractive industries, including terms associated with state equity and any changes in the year under review, be publicly accessible. The MSG must also clarify the rules and practices governing financial relations between SOEs (most notably KRAOMA) and the state. The MSG may wish to liaise with relevant government entities and development partners to assess the extent to which clarification of such issues could support progress under the IMF extended credit facility. Stakeholders are encouraged to embed reporting of such information through routine government systems, for instance in publishing extractives SOEs' statutes and audited financial statements on a regular basis.

7. In accordance with Requirement 4.1.a, the MSG should ensure that its materiality decisions related to selecting companies and revenue streams for reconciliation are clearly documented. In its approach to the materiality of revenue streams, the MSG is encouraged to strike a balance between comprehensiveness and relevance for stakeholders, to ensure that a workable approach to reconciliation is adopted and to facilitate the embedding of revenue transparency in government and company systems. In accordance with Requirement 4.1.c, the MSG should ensure that the materiality of payments from each non-reporting entity is clearly assessed to support the IA's overall assessment of the comprehensiveness of reconciliation. In accordance with Requirement 4.1.d, unless there are significant practical barriers, the government is additionally required to provide aggregate information about the amount of total revenues received from each of the benefit streams agreed in the scope of reconciliation, including revenues that fall below agreed materiality thresholds.

8. In accordance with Requirement 4.4, the MSG should assess the materiality of government revenues from the transportation of minerals, clarifying the management of port-related fees on the transportation of minerals.

9. In accordance with Requirement 4.6, the MSG should establish whether direct subnational payments, within the scope of the agreed benefit streams, are material. Where material, the MSG is required to ensure that reconciled information on company payments to subnational government entities and the receipt of these payments be publicly accessible. EITI Madagascar may wish to provide more information on the disbursement of ristournes from Ambatovy to host communes built-up since the start of production in 2012 given the materiality of such delayed payments.

10. In accordance with Requirement 4.7, the MSG is required to ensure that EITI data is presented by individual company, government entity and revenue stream. To strengthen implementation, the MSG may wish to consider the extent to which it can make progress in implementing project-level EITI reporting ahead of the deadline for all EITI Reports covering fiscal periods ending on or after 31 December 2018.

11. In accordance with Requirement 4.9.a, the EITI requires an assessment of whether the payments and revenues are subject to credible, independent audit, applying international auditing standards. In accordance with requirement 4.9.b.iii and the standard Terms of Reference for the Independent Administrator agreed by the EITI Board, the MSG and Independent Administrator should:

    a. examine the audit and assurance procedures in companies and government entities participating in the EITI reporting process, and based on this examination, agree what information participating companies and government entities are required to provide to the Independent Administrator in order to assure the credibility of the data in accordance with Requirement 4.9. The Independent Administrator should exercise judgement and apply appropriate international professional standards in developing a procedure that provide a sufficient basis for a comprehensive and reliable EITI Report. The Independent Administrator should employ his/her professional judgement to determine the extent to which reliance can be placed on the existing controls and audit frameworks of the companies and governments. The Independent Administrator's inception report should document the options considered and the rationale for the assurances to be provided.

   b. ensure that the Independent Administrator provides an assessment of comprehensiveness and reliability of the (financial) data presented, including an informative summary of the work performed by the Independent Administrator and the limitations of the assessment provided.
   c. ensure that the Independent Administrator provides an assessment of whether all companies and government entities within the agreed scope of the EITI reporting process provided the requested information. Any gaps or weaknesses in reporting to the Independent Administrator must be disclosed in the EITI Report, including naming any entities that failed to comply with the agreed procedures, and an assessment of whether this is likely to have had material impact on the comprehensiveness and reliability of the report.

12. In accordance with Requirement 5.1, EITI Madagascar should publicly clarify which extractive industry revenues, whether cash or in-kind, are recorded in the national budget. Where revenues are not recorded in the national budget, the allocation of these revenues must be explained, with links provided to relevant financial reports as applicable. To strengthen implementation, EITI Madagascar may wish to use EITI reporting to monitor the migration of government finances towards a single Treasury account system, providing a platform for public information on the management of off-budget extractives revenues.

13. In accordance with Requirement 5.2, the MSG is required to ensure that material subnational transfers of extractives revenues are publicly disclosed, when such transfers are mandated by a national constitution, statute or other revenue sharing mechanism. The MSG should also disclose any discrepancies between the transfer amount calculated in accordance with the relevant revenue sharing formula and the actual amount transferred between the central government and each relevant subnational entity. The MSG is encouraged to reconcile these transfers.

14. In accordance with Requirement 6.2, the MSG should undertake a comprehensive review of all expenditures undertaken by extractives SOEs that could be considered quasi-fiscal. The MSG should develop a reporting process for quasi-fiscal expenditures with a view to achieving a level of transparency commensurate with other payments and revenue streams.

15. In accordance with Requirement 7.4, the annual progress report should be the product of consultations with all stakeholders and include a review of the impact of EITI implementation. Civil society groups and industry involved in the EITI, particularly, but not only those serving on the MSG, should be able to provide feedback on the EITI process and have their views reflected in the APR.

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