

# Impacts of the global iron ore sector

Case Study: Altain Khuder in Mongolia



**Tim Steinweg & Anne Schuit**

December 2014

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SOMO

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Amsterdam, December 2014

## Colophon

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## Executive summary

This report provides a case study on the Mongolian mining company Altain Khuder in order to identify social and environmental impacts of the iron ore sector. The report is based on a combination of desk research and the results of a fact-finding mission in August 2014 to the communities around the Tayan Nuur mine, which is operated by Altain Khuder and has received funding from the European Bank for Reconstruction and Development (EBRD). It links sector characteristics and corporate strategies with adverse impacts on local communities.

This case study illustrates that the extent to which a company conducts meaningful stakeholder engagement and consultation, with respect for stakeholder rights as well as proper mitigation measures to address social and environmental impacts, is not only the result of a company's good intentions or the sustainable policies of its investors. It can also be explained by business factors such as the need for infrastructure, mine lifespan and production targets. If these business factors come into conflict with meaningful engagement and consultation, the rights of communities and other stakeholders could be deprioritised and their livelihoods could be threatened.

As the prime raw material for steel, iron ore is critical for all sectors of our economy and the characteristics of the global iron ore market influence the business strategies of companies that are active in this market. In turn, business strategies determine the social and environmental impacts of iron ore mines. Altain Khuder is currently the second largest iron ore producer in Mongolia. As it is located 168km from the Chinese border, it is an attractive supplier to the steel mills in Northwestern China, which face prohibitive transportation costs for seaborne iron ore supply. Altain Khuder is currently constructing a paved road from its mine to the border, which it expects will reduce its transportation costs by 25%. Since the beginning of this year, Altain Khuder has faced a significant drop in market prices for iron ore. In response, the Tayan Nuur mine is reportedly operating at 30% capacity, although the company has rapid expansion targets.

### **Transportation infrastructure impacts communities**

The roads that are used for the transportation of the ore generate dust and noise. The interviewed herders report that dust from the current road pollutes the grass and causes illnesses in their grazing animals. Herders indicated having lost up to several dozen animals, mainly goats and camels, due to dust-related illnesses. Furthermore, the herders feel that they have not been adequately consulted about the construction of the new road, despite the fact that it cuts through their pastures. Their main problem with the new road is the lack of adequate passageways for them and their herds. Livestock find it difficult to cross the elevated road, thereby losing access to pasture and facing difficulties moving from one camp to the other.

These findings show that the group of stakeholders affected by the mining operations is larger than those living at or in the vicinity of the mine itself. Infrastructure development is often presented as a benefit to surrounding communities. However, newly built infrastructure can cut through land that is already in use, and increased traffic can have significant health and safety impacts, even for communities living further afield from the actual mine.

**One-off monetary payments are not adequate compensation**

During the first phases of Altain Khuder's operations, 22 herder families were resettled by the company. Altain Khuder paid cash compensation for the resettlement directly to the herders. However, cash compensation is not appropriate when land is communally owned and livelihoods are land based. The herders were unable to use the compensation to purchase new land to resettle to, as land is democratically appointed rather than bought and sold in this part of Mongolia. This case study has identified at least one herder who was blocked from new land precisely because of the fact that she received monetary compensation. This case study illustrates how the price volatility of iron ore can have a knock-on effect on the livelihoods of local communities. As the price for iron ore is not guaranteed, companies will make use of the short window of opportunity created by higher iron ore prices to ramp up production. This can mean that there is little room for careful planning of resettlements, heightening the risk of adverse impacts for affected communities.

**Short mine lifespan means little incentive for proper stakeholder engagement**

As part of the EBRD's involvement, Altain Khuder hired a company to conduct a post-resettlement survey, in order to compare the livelihood standards of resettled families. It concluded that herders have not lost assets as a result of the mining activities. The company has also indicated that it undertook a number of social programmes to address livelihood issues. However, none of the people interviewed during the fact-finding mission were aware that such a survey had ever been conducted. At the same time, several herders who were interviewed for this study indicated that their lives have been seriously and negatively impacted since the start of the mining project. Furthermore, this report revealed a lack of transparency towards stakeholders and reports of intimidation and harassment towards its critics. The company has filed up to seven lawsuits against people who openly criticised the company and charged them with 'organized crimes of defamation'.<sup>1</sup> The company's approach to local communities might be explained by the relatively short lifespan of the mine. Given that ore reserves are estimated to dry up within 10 years, which is a relatively short lifespan for any mine, the company might not be incentivised to act as a good neighbour.

**EBRD involvement no safeguard against adverse impacts**

As a result of the financial relationship between Altain Khuder and the EBRD, the company has an obligation to comply with the Performance Requirements (PRs) of the EBRD. This report suggests that at least four PRs have not been adhered to: environmental and social management (PR1); community health and safety (PR4); resettlement and displacement (PR5); information disclosure and stakeholder engagement (PR10). The social and environmental considerations that are included in its investment strategies make the EBRD and other development banks distinctly different from mainstream investors. However, as this case study proves, the involvement of the EBRD is no safeguard against adverse social and environmental impacts. One potential factor is that the EBRD has not provided adequate disincentives to avoid ineffective resettlements or inadequate stakeholder engagement.

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1 OTWatch, Fact Finding Mission Report, Tayan Nuur (Lake Tayan) Iron Ore Project, 6-11 March 2014, unpublished.

# 1 Introduction

As the prime raw material for steel, iron ore is critical for all sectors of our economy, both for consumer products such as cars, washing machines and fridges, and for infrastructure such as buildings, bridges and roads. Steel makes up 95% of global metal production and as such, the iron ore market is directly linked to the health of the global economy.<sup>2</sup> Iron ore demand is highest in countries such as China that are experiencing rapid economic growth and where new buildings are being built at a rapid pace. Similarly, when economies slow down, housing bubbles burst and the construction of new buildings stalls, as occurred in recent years in the United States and Europe. Iron ore demand can fall steeply as a result.

For decades, iron ore was traded on the basis of a one-year benchmark price system developed by Japanese steelmakers and large Australian and Brazilian iron ore mining companies.<sup>3</sup> Prices remained relatively stable until 2010, when the benchmark system was replaced by a spot-market system, as a result of the growing demand from China. A combination of factors, including financial speculation on this spot market and the global financial crisis, has made iron ore the most volatile of all traded minerals.<sup>4</sup> It is illustrative that iron ore played a role in the recent financial scandal in China, whereby traders used iron ore stockpiles as collateral to more than one financial lender.<sup>5</sup>

Since 2013, iron ore prices are in the midst of a major downswing. Since the beginning of 2014, iron ore prices have dropped 38%, to the lowest level since October 2009.<sup>6</sup> On the one hand, this drop can be explained by new low-cost iron ore supply in Brazil and Australia. On the other hand, China's demand for steel has slowed due to credit restrictions placed on the construction sector by the Chinese government.<sup>7</sup> Analysts have labelled the steep and sudden downturn 'the end of the iron age'.<sup>8</sup>

## Iron ore mining

Iron ore is one of the most abundantly available minerals and is mined around the world, as it makes up 5% of the Earth's crust. While Australia and Brazil are home to the largest iron ore mines in the

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2 The Economist, "The lore of ore", 13 October 2012, <<http://www.economist.com/node/21564559>> (17 October 2014).

3 Ibid.

4 Bloomberg Intelligence, "The Iron Ore Market", accessed through the Bloomberg database.

5 The Sydney Morning Herald, "China scandal weighs on iron ore price", Business Day, 23 June 2014, <<http://www.smh.com.au/business/mining-and-resources/china-scandal-weighs-on-iron-ore-price-20140623-3andf.html>> (17 October 2014).

6 The Economist, "Iron ore mining; Down but not out", 9 September 2014, <<http://www.economist.com/news/business-and-finance/21616294-iron-ore>> (17 October 2014).

7 Reuters website, "UPDATE 2 – China's H1 crude steel demand lags output, mills under financing stress – CISA", 1 August 2014, <<http://in.reuters.com/article/2014/08/01/china-steel-idINL4N0Q70J720140801>> (21 October 2014).

8 Bloomberg website, "Goldman Calls End to Iron Age After 'Dramatic' Drop in Ore Price", 10 September 2014, <<http://www.bloomberg.com/news/2014-09-10/goldman-calls-end-to-iron-age-after-dramatic-drop-in-ore-price.html>> (28 November 2014).

world, large quantities of iron ore are also mined in countries such as Guinea, Congo, Sierra Leone and Liberia.<sup>9</sup>

As with the mining of all minerals, mining for iron ore often creates adverse environmental and social impacts, as well as being linked to fraud and conflict and infringing on the rights of local communities. Examples include the corruption charges against BSGR, the company of Israeli billionaire Beny Steinmetz, related to the acquisition of the Simandou iron ore mine in Guinea or the physical and economic displacement of 20,000 people in India related to the iron mine, steel plant and associated infrastructure of Korean company POSCO.<sup>10</sup>

One factor that makes base materials such as iron, copper or tin distinct from precious metals such as gold and silver is the fact that they are mined, transported and traded in much higher quantities, and that the weight of materials is therefore an important factor. The sheer volumes of iron ore bought and sold influences the way the iron ore market functions, the strategies chosen by mining companies and the impacts it has on various stakeholders.

## 1.1 Aims and target groups

The characteristics of the global iron ore market clearly influence the business strategies of companies that are active in this market. In turn, strategic corporate decisions determine the social and environmental impacts of iron ore mines. Through a series of case studies, SOMO aims to identify and explain adverse impacts at iron ore mines around the world and link them to corporate strategies and the global iron ore market. By analysing individual companies, we aim to identify and explain a number of common factors that can cause adverse impacts on workers, local communities and the environment. Such information can be used during the due diligence processes of potential financiers of new iron ore mining projects, (sustainable) investors considering investing in the iron ore or steel sectors, civil society organisations that are working with stakeholders affected by iron ore mining projects and interested media.

This briefing paper is the first in the series, and profiles Altain Khuder, a Mongolian mining company that operates the Tayan Nuur mine and has received funding from the European Bank for Reconstruction and Development (EBRD).

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9 Mining-Technology.com website, "The world's biggest iron ore mines", 19 February 2014, <<http://www.mining-technology.com/features/featurethe-worlds-11-biggest-iron-ore-mines-4180663/>> (17 October 2014); Mining Weekly website, "Miners set sights on West Africa as the next big iron-ore destination", 25 October 2013, <<http://www.miningweekly.com/article/miners-set-sights-on-west-africa-as-the-next-big-iron-ore-destination-2013-10-25>> (17 October 2014).

10 CorpWatch website, "BSGR Investigated for Corruption in Guinea Iron Ore Deal", 4 October 2013, <<http://www.corpwatch.org/article.php?id=15893>> (17 October 2014); OECDWatch website, Case Database, "Lok Shakti Abhiyan et al. vs POSCO", no date, <[http://oecdwatch.org/cases/Case\\_260](http://oecdwatch.org/cases/Case_260)> (17 October 2014).

## 1.2 Methodology

This case study is based on a combination of desk research and field research. Information about the iron ore sector in Mongolia (Chapter 1) and the company profile of Altain Khuder (Chapter 2) has been gathered through secondary research reports, analyst reports, media sources, rating agencies and non-governmental organisation (NGO) sources. Several analytical tools have been applied to analyse the company's business strategy.

The chapter about the impacts of Altain Khuder's iron ore mine is based on the outcomes of a one-week fact-finding mission by SOMO, CEE Bankwatch, Lawyers for Environment and OT Watch in August 2014, as documented in a separately published fact-finding mission report. The mission included visits to Tseel Soum, and Bayangol and Derstei Baghs in the Gobi-Altai region.<sup>11</sup> The team had meetings with the Tseel Soum's governor's office, the governors of Derstei and Bayangol Baghs, a local cooperative leader, and over 20 nomadic herders from these baghs. The team also visited project areas of the company Altain Khuder: the black top road for transportation of iron ore from the mine to the Chinese border that is currently under construction, and the site of a kindergarten in Tseel Soum. Additionally, a meeting with EBRD's Mongolia office was held in the capital Ulaanbaatar. This fact-finding mission was a follow up of an initial fact-finding mission to the area undertaken by OT Watch, Lawyers for Environment and the Council of Natives of Tseel Soum in March 2014.

A draft version of this report was sent to Altain Khuder and the EBRD as part of SOMO's review procedure. Altain Khuder provided comments and additional sources, which have been processed in this final version of the report.

## 1.3 Limitations

This case study is of an explorative nature and aims to identify relevant sustainability and human rights issues in the iron ore mining sector. As such, the following limitations are important to take into account. First, the findings on the impacts of the company are partially based on interviews with a limited number of stakeholders in Tseel Soum. The identified impacts of the Tayan Nuur mining project are therefore not necessarily representative of the experiences of the entire Tseel Soum community and these findings can therefore not be generalised. Secondly, this report is drafted on the basis of all the information available to the researchers at the time of writing. The authors are aware of the existence of a number of documents to which they did not have access, including minutes of meetings, consultancy reports and other sources. Finally, it should be noted that this case study does not intend to analyse the compliance of the company to Mongolian rules and regulations and does not imply legal offenses.<sup>12</sup>

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11 Mongolia is divided into 21 aimags (provinces). Aimags are divided into soums (districts), which in turn consist of baghs (smallest administrative units).

12 In response to a draft version of this report, Altain Khuder indicated on several occasions that it operates in accordance with Mongolian law and that its impacts do not exceed legal limits. Altain Khuder, response to a draft version of this report, email received 24 November 2014.

## 1.4 Structure of the report

Following this introduction, Chapter 2 briefly discusses the iron ore mining sector in Mongolia, including known social and environmental impacts. Chapter 3 provides a company profile of Altain Khuder, presenting basic information about the corporate and ownership structure and discussing the company's business strategies. Chapter 4 presents the findings on the impacts of Altain Khuder's iron ore mine and links them to the iron ore mining sector in Mongolia and Altain Khuder's business strategy. Chapter 5 analyses the impacts of the mine on the basis of the social and environmental standards of the EBRD. The concluding Chapter 6 discusses the overall conclusions and identifies a number of lessons that can be drawn from this case study.

## 2 The iron ore mining sector in Mongolia

This case study is set in Mongolia. As a Mongolian company, the impacts of Altain Khuder's iron ore mine that are discussed in later chapters need to be placed in the context of Mongolia and the characteristics and history of the country's mining sector.

### 2.1 The Mongolian mining sector

While the Mongolian economy traditionally centred on herding and agriculture, discoveries of its extensive mineral deposits have transformed its economy in recent years.<sup>13</sup> The country has vast deposits of copper, gold, coal and iron ore, and several large-scale mining operations have become operational over the last decade. Oyu Tolgoi, a copper and gold project in the South Gobi desert, has some of the largest reserves in the world. The mine, which became operational in 2013, is run by Rio Tinto and is considered to be the largest financial undertaking in Mongolia's history.<sup>14</sup> Tavan Tolgoi, a coal mine with reserves of 6 billion tons, has also seen massive investments over the last few years.

The developments at these two large mining projects created a large-scale commodity boom between 2009 and 2011. At its peak in 2011, Mongolia's Gross Domestic Product (GDP) grew by 17.5% on the back of mining investments, making it one of the world's fastest growing economies.<sup>15</sup> Foreign investments were soaring in 2011 and 2012, both related to the two large mining projects as well as to various other mining projects and mining related services. The benchmark index of the Mongolian stock exchange increased tenfold between 2006 and 2011, while inflation also soared.<sup>16</sup> Development banks, such as the International Finance Corporation (IFC) and the EBRD were among the largest financiers during this boom.

However, the boom slowed down significantly after 2012. Foreign investment nearly halved in 2013 compared to the year before. Conflicts between Rio Tinto and the Mongolian government over production costs and tax issues at Oyu Tolgoi, as well as changes in mining related legislation including the revoking of 106 mining licenses, caused the interest of foreign investors to fade and

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13 CIA Website, The World Factbook, "Mongolia", no date, <<https://www.cia.gov/library/publications/the-world-factbook/geos/mg.html>> (17 October 2014).

14 Invest in Mongolia website, "Gold Mine", no date, <<http://www.investinmongolia.org/index.php/invest/gold>> (17 October 2014).

15 The World Bank Group in Mongolia, Mongolia Economic Update, November 2013, <[http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2013/11/07/000442464\\_20131107125022/Rendered/PDF/826050WP0Mong00Box379865B00PUBLIC0.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2013/11/07/000442464_20131107125022/Rendered/PDF/826050WP0Mong00Box379865B00PUBLIC0.pdf)> (17 October 2014), p.11.

16 Bloomberg website, "Mongolia Delays First U.S. Dollar Bond Sale as Economy Set for 20% Growth", 27 October 2011, <<http://www.bloomberg.com/news/2011-10-27/mongolia-delays-dollar-bond-sale-as-economy-set-for-20-growth.html>> (17 October 2014).

economic growth to slow down.<sup>17</sup> Several of the mining companies that had planned to go public decided to postpone their public offerings, while the overall Mongolian economy slowed down significantly.

## 2.2 Iron ore mining in Mongolia

Mongolian iron ore is primarily attractive because of its close proximity to China. Practically all of Mongolia's iron ore is exported to the Chinese steel industry, which demands enormous quantities of iron ore. As transportation expenses are important determinants of the prices that consumers pay, Mongolia has a competitive advantage over large iron ore exporters such as Brazil and Australia. In particular, the demand for steel from the construction sector in the inland Chinese provinces of Inner Mongolia and Xinjiang is served by Mongolia, as these regions face prohibitive transportation costs for seaborne iron ore that enters through ports in eastern China.

On a global scale, Mongolia is not a large producer of iron ore. However, while copper and coal are the minerals that make the biggest contribution to Mongolia's economy, iron ore is the third most exported mineral, accounting for approximately 15% of Mongolia's exports in 2013.<sup>18</sup> Overall iron exports totalled US\$ 700 million in 2013.

The iron ore mining sector saw significant interest from investors during the mining boom of 2009-2011, with the EBRD and the China Investment Corp making multi-million investments in some of the large iron ore mining companies. As with the other commodities, when the mining boom came to an end in 2012, interest from foreign companies dwindled. The end of Mongolia's mining boom came at the same time as global iron ore prices dropping, most steeply after August 2013. Two of the smaller iron ore companies in Mongolia have already suspended their operations due to difficult market conditions.<sup>19</sup>

## 2.3 Social and environmental impacts

In its latest annual report, the National Human Rights Commission of Mongolia discusses the environmental impacts of mining in Mongolia, and recognises that the environment is degraded because of the large number of mining licenses issued.<sup>20</sup> It also reports how the transportation of natural resources is one of the major reasons for this environmental degradation, and that the deterioration

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17 Bloomberg website, "Mongolia Prepares to Restore Mining Licenses in Investment Boost", 28 April 2014, <<http://www.bloomberg.com/news/2014-04-28/mongolia-prepares-to-restore-mining-licenses-in-investment-boost.html>> (17 October 2014); Reuters website, "Special report: In tax case, Mongolia is the mouse that roared", 16 July 2013, <<http://www.reuters.com/article/2013/07/16/us-dutch-mongolia-tax-idUSBRE96F0B620130716>> (21 October 2014).

18 Mongolian Mining Journal, "An Economic Impact Assessment of the Iron Ore Sector in Mongolia", March 2014, <[eri.mn/research/ERI/Iron\\_Ore.pdf](http://eri.mn/research/ERI/Iron_Ore.pdf)>, (17 October 2014), p.2.

19 Ibid.

20 National Human Rights Commission of Mongolia, 12th Report on Human Rights and Freedoms in Mongolia, Ulaanbaatar, 2013, <<http://www.asiapacificforum.net/members/full-members/mongolia/downloads/annual-reports/2013>> (17 October 2014) p.9.

of soil and pasture lands creates respiratory diseases and makes it more difficult to sustain livelihoods in areas where coal and other minerals are transported. According to the French newspaper *Le Monde*, mining also destabilises ecosystems and contributes to the desertification of the Mongolian countryside.<sup>21</sup> The high demands of water for mining operations reroutes major rivers and endangers United Nations Educational, Scientific and Cultural Organization (UNESCO) world heritage sites such as the Orkhon Valley. Wildlife populations are affected by the noise of mining sites and the roads that cut through their habitat. When mines cease their operations, sites are often not restored to their natural state and the environment remains scarred from the previous mining activities.

Mining also has an impact on the livelihoods of the rural population. According to the National Human Rights Commission, the population of nomadic herders has decreased by 56% in some areas, as it has become more difficult to sustain a nomadic lifestyle due to shrinking pastureland. *Le Monde* also reports on the increased rates of birth deformations seen in animals kept by nomadic herders near the Areva uranium mine.<sup>22</sup> In the Gobi desert, mining and its related infrastructure create immense amounts of dust, destroying pasture land and creating respiratory illnesses for the farmers and their herds. As a consequence, the majority of nomads in those areas have moved from their homeland in search of more fertile pastures to the north.

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21 *Le Monde* website, "Mongolia ; L'eldorado n'existe pas", no date, <[http://www.lemonde.fr/a-la-une/visuel/2014/09/06/mongolie-l-eldorado-n-existe-pas\\_4464498\\_3208.html](http://www.lemonde.fr/a-la-une/visuel/2014/09/06/mongolie-l-eldorado-n-existe-pas_4464498_3208.html)> (17 October 2014).

22 *Ibid.*

## 3 Altain Khuder company profile

This chapter provides a general overview of the Mongolian iron ore mining company Altain Khuder. It describes some of the general information regarding the company structure, ownership and finances, before discussing the company's business strategy in the second part of this chapter. The strategy analysis aims to identify a number of factors that influence the company's operations and that provide the context for the social and environmental impacts discussed in Chapter 4.

Altain Khuder is the second largest iron ore mining and exploration company in Mongolia.<sup>23</sup> It has owned and operated the Tayan Nuur iron ore mine since 2006.<sup>24</sup> Tayan Nuur is located approximately 1,300 kilometres south west of Ulaanbaatar, Mongolia's capital, and approximately 168 kilometres from the Chinese border. The company sells, stores, transports and exports iron ore products to steel mills located in western China.<sup>25</sup> According to a company presentation, the Tayan Nuur project has an annual production capacity of 2.3 million tons, a six-fold increase over the past five years, and total reserves of 91.7 million tons with a content of 38% iron ore.<sup>26</sup> Its iron ore exports account for 33% of the total exports of Mongolia.

### 3.1 Corporate and ownership structure

Altain Khuder is a private company, ultimately owned by Mr. Bazar Radnaabazar, a Mongolian businessman.<sup>27</sup> The EBRD, which also issued debt to the company, controls a 5% minority stake.<sup>28</sup>

Altain Khuder's corporate and ownership structure appear to be in a constant state of flux in recent years. The most recent publicly available information about Altain Khuder's corporate structure stems from a corporate presentation from March 2014.<sup>29</sup> However, in their response to a draft version of the current report in November 2014, the company indicated that this information was already outdated.<sup>30</sup> It remains unclear what the current corporate structure actually is.

23 CRU Group, "Iron Ore: Assessing Mongolia's potential", Ulaanbaatar, 3-5 September 2012, Frontier Invest Mongolia 2012, By John Johnson, CEO, CRU China. <<http://www.frontier.mn/index.php/research/full-reports/category/5-expert-series-2012?download=57:assessing-mongolia-s-iron-ore-potential>> (24 November 2014), p.13.

24 Altain Khuder website, About Us, "Altain Khuder LLC", no date, <<http://www.altainkhuder.mn/content/24.html>> (17 October 2014).

25 Idem.

26 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

27 Reuters website, "TEXT-S&P rates Mongolian Resources Corp. 'B-'; outlook stable", 8 October 2012, <<http://www.reuters.com/article/2012/10/08/idUSWLA441720121008>>, 21 October 2014.

28 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

29 Idem.

30 Altain Khuder, response to a draft version of this report, email received 24 November 2014.

The corporate structure that was presented in March 2014 showed that the business entity Altain Khuder Inc. was wholly owned by Mongolian Resources Corporation Sarl, based in Luxembourg. The ultimate holding company of the group was Cayman Island-based MRC (Mongolian Resources Corporation), which also controlled the Million Vision Group Limited, based on the British Virgin Islands. Luxembourg, the Caymans Islands and the British Virgin Islands are often considered as secrecy jurisdictions.<sup>31</sup>

According to the company, this structure was chosen in preparation for an international stock listing at the recommendation of external advisors.<sup>32</sup> In 2012, Altain Khuder had appointed Australia's Macquarie Group and Bank of America as joint global coordinators for an Initial Public Offering (IPO) at the Hong Kong stock exchange.<sup>33</sup> The IPO was targeted for the fourth quarter of 2012, but has not taken place to date. Altain Khuder has indicated that the offering has been delayed indefinitely, and that the corporate structure is therefore no longer applicable.<sup>34</sup>

Prior to the preparations for the IPO, Altain Khuder had already undergone several changes as the result of the divestment of Deutsche Bank from the company. Deutsche Bank held shares in Euro 7 Investment, MRC's major shareholder, until 2011.<sup>35</sup> According to its 2010 annual report, Deutsche Bank controlled 21.2% of the company at the time.<sup>36</sup> In 2011, these shares were transferred through a debt-funded buy-out to business partners of Mr. Bazar Radnaabazar. This resulted in an organisational restructuring, whereby Euro 7 Investment, Eastern Metals LLC, the Trade and Development Bank of Mongolia and TDB Capital LLC sold their shares in Mongolian Resources Corporation Sarl (the Luxembourg entity) to MRC (the Cayman Islands entity).<sup>37</sup>

### EBRD financing

In 2012, the board of the EBRD approved a term loan of US\$ 30 million to Altain Khuder to develop the Tayan Nuur mine and an equity investment to Altain Khuder LLC totalling US\$ 25 million.<sup>38</sup> The equity investment consisted of a US\$ 15 million tranche for the purchase of a minority stake in the company's yet to be listed parent company and a US\$ 10 million tranche to avoid potential dilution of the EBRD's stake.

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- 31 Financial Secrecy Index website, "Financial Secrecy Index – 2013 Results", no date, <<http://www.financialsecrecyindex.com/introduction/fsi-2013-results>> (21 October 2014).
- 32 Altain Khuder, response to a draft version of this report, email received 24 November 2014.
- 33 The Wall Street Journal Blog, "Macquarie Lands Lead Role on Mongolia IPO", Deal Journal Australia, 23 May 2012, <<http://blogs.wsj.com/dealjournalaustralia/2012/05/23/macquarie-lands-lead-role-on-1-billion-mongolia-ipo/>> (27 November 2014).
- 34 Altain Khuder, response to a draft version of this report, email received 24 November 2014.
- 35 Reuters website, "TEXT-S&P rates Mongolian Resources Corp. 'B-'; outlook stable", 8 October 2012, <<http://www.reuters.com/article/2012/10/08/idUSWLA441720121008>>, 21 October 2014.
- 36 Deutsche Bank, Annual Financial Statements and Management Report of Deutsche Bank AG 2010, <[https://www.deutsche-bank.de/ir/en/download/Annual\\_Financial\\_Statements\\_and\\_Management\\_Report\\_of\\_Deutsche\\_Bank\\_AG\\_2010.pdf](https://www.deutsche-bank.de/ir/en/download/Annual_Financial_Statements_and_Management_Report_of_Deutsche_Bank_AG_2010.pdf)> (24 November 2014).
- 37 Service Central de Législation Luxembourg, Recueil des Sociétés et Associations, Memorial Journal Officiel du Grand-Duché de Luxembourg, 18 July 2013.
- 38 EBRD, Minutes of the Board Meeting of 31 January 2012, <<http://www.ebrd.com/downloads/board/BDSM1202w.pdf>> (27 November 2014).

The investment is part of the bank's strategy to foster the transition of Central and Eastern European and Central Asian countries to market-based economies.<sup>39</sup> As outlined in its Mining Policy, the EBRD aims to address so-called 'transition challenges' by investing in mining operations. Such challenges include; state ownership of strategic minerals; market concentration; trade barriers; poor infrastructure; use of outdated technologies; weak institutions and lack of transparency; and lack of alignment between legal and regulatory frameworks and international standards.

The EBRD supports the extraction of iron ore and coking coal because in its countries of operations '*steel is important to the overall economy, being a key supplier of raw input to a number of manufacturing industries*'.<sup>40</sup> The EBRD also aims to contribute to sustainability in the mining sector and to the development of a responsible mining sector that applies the best international standards.

The project also fits in with the EBRD's strategy on Mongolia, where it financed a total of 52 projects between 2006 and 2012.<sup>41</sup> Among other objectives, the EBRD also aimed to '*support the sustainable development of the natural resource sector through providing debt and equity finance to privately owned mining companies and requiring adherence to the highest environmental, transparency and corporate governance standards*'.<sup>42</sup>

## 3.2 Finances

Neither Altain Khuder nor its parent company MRC has published any annual reports or financial accounts.

In 2012, while preparing for a bond issue that never materialised, the company received a B3 and a B- rating by rating agencies Moody's and Standard & Poor (S&P) respectively.<sup>43</sup> In their argumentation, Moody's points to the fact that the company is heavily indebted, with most of the debt owed to shareholders and related parties such as the EBRD.<sup>44</sup>

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39 EBRD, Mining Operations Policy, approved by the Board of Directors on 17 October 2012, <<http://www.ebrd.com/downloads/policies/sector/mining-operations-policy.pdf>> (21 October 2014).

40 Idem., p.6.

41 EBRD, Strategy for Mongolia, approved by the Board of Directors on 25 June 2013, <<http://www.ebrd.com/downloads/country/strategy/mongolia.pdf>> (21 October 2014).

42 Idem, p.5-6.

43 Moody's website, "Ration Action: Moody's assigns first-time B3 to Mongolian Resources; outlook stable", 8 October 2012, <[https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR\\_256966](https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR_256966)> (21 October 2014); Reuters website, "TEXT-S&P rates Mongolian Resources Corp. 'B-'; outlook stable", 8 October 2012, <<http://www.reuters.com/article/2012/10/08/idUSWLA441720121008>> (21 October 2014).

44 Moody's website, "Ration Action: Moody's assigns first-time B3 to Mongolian Resources; outlook stable", 8 October 2012, <[https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR\\_256966](https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR_256966)> (21 October 2014).

S&P describes how, as of June 2012, more than 50% of the company's debt stemmed from the buy-out of shares held by Deutsche Bank.<sup>45</sup> Also, MRC failed to repay debt to Golomt Bank of Mongolia in time in March and May 2012. S&P concluded that there were limitations in the company's internal controls and financial discipline.

In early 2013, Moody's downgraded MRC's rating because of concerns that MRC would be unable to refinance its debt due to the company's weak financial position and low iron ore prices.<sup>46</sup> It later withdrew the rating because it believed it had insufficient or otherwise inadequate information to support the maintenance of the rating.

### 3.3 Business strategy

According to its website, Altain Khuder's objective is to 'become the leading iron ore mining and processing company in Mongolia and in the region furthermore in terms of production quality and export volume'.<sup>47</sup>

#### 3.3.1 Competitive environment

Within Mongolia, there are nine iron ore projects with an estimated total resource base of 1,250 million tons.<sup>48</sup> Altain Khuder is currently the second largest iron ore producer in Mongolia, after Eruu Gol, which had a market share of over 50% in 2011 but which is expected to stop operating in 2023.<sup>49</sup> Altain Khuder currently claims to have a market share of 33%.<sup>50</sup> In addition, there are a handful of other companies with market shares of less than 5%. Internationally, the largest iron ore producers are Vale, based in Brazil and Rio Tinto in Australia.

#### Transportation costs

As an iron ore mining and exporting company based in Mongolia, Altain Khuder is servicing the demand for iron ore by the Chinese steel industry. Transportation makes up a significant share of the costs for iron ore mining companies, and Mongolia's proximity to China means that the shipping costs are lower than for companies based in other large iron ore producing countries,

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45 Reuters website, "TEXT-S&P rates Mongolian Resources Corp. 'B-'; outlook stable", 8 October 2012, <<http://www.reuters.com/article/2012/10/08/idUSWLA441720121008>> 21 October 2014.

46 Moody's website, "Rating Action: Moody's downgrades Mongolian Resources; rating to be withdrawn", 30 August 2013, <[https://www.moody.com/research/Moodys-downgrades-Mongolian-Resources-rating-to-be-withdrawn--PR\\_281307](https://www.moody.com/research/Moodys-downgrades-Mongolian-Resources-rating-to-be-withdrawn--PR_281307)> 21 October 2014.

47 Altain Khuder website, About Us, "Company's Mission", no date, <<http://www.altainkhuder.mn/content/25.html>> (21 October 2014).

48 Mongolian Mining Journal, "An Economic Impact Assessment of the Iron Ore Sector in Mongolia", March 2014, [eri.mn/researchERI/ERI\\_Iron\\_Ore.pdf](http://eri.mn/researchERI/ERI_Iron_Ore.pdf), 17 October 2014), p.1.

49 Idem, p.9.

50 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

such as Australia and Brazil. According to an article in the Wall Street Journal, shipping costs of iron ore concentrate from Mongolia are less than half the shipping costs from Australia.<sup>51</sup>

According to an undated interview with the sales manager of Altain Khuder, the market for iron ore in Northwestern China is less competitive, and pricing power lies in the hands of a select group of large Chinese steel manufacturers.<sup>52</sup> The customers that the company lists in a recent presentation mostly appear to be large Chinese steel mills.<sup>53</sup> Altain Khuder indicates that these large firms cooperate to force iron ore suppliers to lower their prices and to keep small and medium size steel mills out of the market.<sup>54</sup>

### Steep drop in market prices

Since the beginning of 2014, Altain Khuder has been faced with a significant drop in market prices for iron ore. Market prices in China have dropped some 33% since August 2013, mostly due to a slowdown in the real estate sector.<sup>55</sup> According to Bloomberg, completions and sales of new buildings in China have dropped 18%, leaving a lower demand for steel and the raw materials for steel production. Two of the smaller Mongolian iron ore operations have already suspended operations, due to the low prices of iron ore in China.<sup>56</sup> It remains unclear how Altain Khuder has been affected by this drop in iron ore prices, but it is likely that this has had an impact on the company's production volumes, capital structure and profitability. Reportedly, the Tayan Nuur mine was operating at 30% capacity in August 2014 in response to the low iron ore prices.<sup>57</sup>

The drop in Chinese iron ore demand is linked to the dire financial situation of many Chinese steel firms, who are reported to have alarming debt-to-asset ratios.<sup>58</sup> Bayi Iron & Steel Co, Altain Khuder's largest customer, is reported to have a debt-to-asset ratio of 86.46% and analysts report that it and many other Chinese steelmakers might have to cut or suspend their steel production in response to their financial troubles.

In addition to the decrease in Chinese demand, iron ore prices are also affected by the increase in iron ore production in Australia and Brazil, the two largest producing countries in the world. For example, BHP Billiton recently announced an increase in its iron ore production in an effort

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- 51 The Wall Street Journal website, "Minegolia Struggles With IPOs", Blog, 22 May 2012, <<http://blogs.wsj.com/deals/2012/05/22/minegolia-struggles-with-ipos/>> 21 October 2014.
- 52 Asian Metal website, "Interview with Khulan, International sales department minister of Mongolian Altain Khuder LLC.", no date, [http://www.asianmetal.com/metal\\_cron/index\\_lunshi\\_khulan\\_en.shtml](http://www.asianmetal.com/metal_cron/index_lunshi_khulan_en.shtml) (21 October 2014).
- 53 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).
- 54 Asian Metal website, "Interview with Khulan, International sales department Minister of Mongolian Altain Khuder LLC." no date, <[http://www.asianmetal.com/metal\\_cron/index\\_lunshi\\_khulan\\_en.shtml](http://www.asianmetal.com/metal_cron/index_lunshi_khulan_en.shtml)> (21 October 2014).
- 55 Bloomberg Intelligence, Iron Ore's Paper Market, accessed through the Bloomberg database.
- 56 Mongolian Mining Journal, "An Economic Impact Assessment of the Iron Ore Sector in Mongolia", March 2014, <[eri.mn/researchERI/ERI\\_Iron\\_Ore.pdf](http://eri.mn/researchERI/ERI_Iron_Ore.pdf)> (17 October 2014), p.2.
- 57 Interview with the Governor of Tseel Soum, 13 August 2014.
- 58 People Daily website, "Debts pile up, weighing on steelmakers", 7 September 2014, <<http://english.peopledaily.com.cn/business/n/2014/0907/c90778-8779605.html>> (21 October 2014).

to gain more market share as high-cost producers in China would be forced to shut down mines due to the low iron ore prices.<sup>59</sup> Estimation models show that iron ore supply may increase 45% by 2018.<sup>60</sup>

### Price volatility and speculation

Global iron ore prices have been very volatile in recent years. The trade in iron ore contracts that are not backed by physical deliveries has increased greatly over the last years and speculation in futures, derivatives and other financial products have made iron ore the most volatile of all traded metals. The recent scandal concerning the use of non-existing commodities as collateral for loans to Chinese firms has also affected global iron ore prices.<sup>61</sup>

### 3.3.2 Competitive positioning

As for all iron ore mining companies, the location of the mine and the volumes of its iron ore reserve largely determine Altain Khuder's competitive positioning.

#### Proximity to customers means competitive transport costs

The single most important competitive advantage that Altain Khuder has over its competitors is the geographical location of its mine. As it is located only 168 kilometres from the Chinese border, it is an attractive supplier to the steel mills in Northwestern China, which face prohibitive transportation costs for seaborne iron ore supply. Within Mongolia, Altain Khuder's mine is located closer to its market than any of its competitors, and is therefore faced with lower transportation costs.<sup>62</sup> This geographical location is one of the factors that allow Altain Khuder to be a low-cost supplier of iron ore. According to Moody's, the production costs for its iron ore concentrates stood at US\$ 45/ton in 2011.<sup>63</sup>

In order to profit from this competitive advantage, the company needs to ensure that both its production and transportation costs are kept to a minimum. Altain Khuder is currently constructing a paved road from its mine to the border, which it expects will reduce its transportation costs by another 25%.<sup>64</sup> A number of the environmental and health impacts described in the subsequent chapter are related to the construction and the use of this road.

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59 ABC website, "BHP posts increase in iron ore output", 22 October 2014, <<http://www.abc.net.au/news/2014-10-22/bhp-posts-increase-in-iron-ore-output/5832198>> (25 October 2014).

60 Bloomberg Intelligence, The Iron Ore Market, accessed through the Bloomberg database.

61 CNBC website, "China plans crackdown on iron ore import loans", 30 April 2014, <<http://www.cnbc.com/id/101630942>> (21 October 2014).

62 Mongolian Mining Journal, "An Economic Impact Assessment of the Iron Ore Sector in Mongolia", March 2014, <[eri.mn/researchERI/ERI\\_Iron\\_Ore.pdf](http://eri.mn/researchERI/ERI_Iron_Ore.pdf)> (17 October 2014), p.2.

63 Moody's website, "Ration Action: Moody's assigns first-time B3 to Mongolian Resources; outlook stable", 8 October 2012, <[https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR\\_256966](https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR_256966)> (21 October 2014). In response to a draft version of this report, Altain Khuder indicated that the figure of US\$ 45/ton is outdated. However, no more recent information about the company's production costs were available.

64 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

Compared to its competitors, Altain Khuder supplies relatively high-quality iron ore. The company reports that its total reserves have an iron grade of 38.0% and that its concentrate is between 60-64%.<sup>65</sup> Such percentages are average on the global market, but Moody's reports that these figures represent relatively high purity levels of iron in the company's deposits compared to those of its Asian competitors.<sup>66</sup> Furthermore, the company indicates that it stands out as it supplies iron ore concentrate while most of its Mongolian competitors supply iron ore lumps.<sup>67</sup> The company has several processing plants at the mining site that produce this iron ore concentrate. As also discussed in Chapter 4, these processing plants are identified by government officials as one of the sources of the dust pollution around Tseel Soum.

### Rapid expansion plans, short lifespan

Finally, the company aims to rapidly expand its production of iron ore over the coming years. It targets a production volume of 3.5 million tons in 2014, up from 2.2 million tons in 2013.<sup>68</sup> However, S&P indicated in 2012 that there was a high risk associated with this expansion, as the company's targeted volumes were seen as 'aggressive' and 'untested'.<sup>69</sup> The company depends on increasing production and sales of iron ore in order to repay its debts, but S&P projected that the company would continue to face high debts despite higher sales volumes. It can be expected that higher iron ore production, requiring more mining activities, would increase dust, water use, transportation of the ore and an expansion of the mining area. In turn, this could further affect the livelihoods of the nomadic herders.

If iron ore prices do recover in the near future, it can be expected that Altain Khuder would intensify its iron ore production, in order to meet its sales targets and service its debts.

Given the company's projected production rates over the coming years, Moody's expects that the Tayan Nuur mine has a lifespan of no more than 10 years before reserves run dry.<sup>70</sup> As a comparison, nearly all of the largest iron ore mines in the world have an expected mine life of more than 30 years (see Table 1).<sup>71</sup> The combination of the limited iron ore reserves and the company's strategy of increased production suggest that its operations in Tseel Soum will not be maintained for an

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65 Ibid.

66 Seeking Alpha website, "The Important Factors to Consider When Investing in Iron Ore", 10 April 2011, <<http://seekingalpha.com/article/262764-the-important-factors-to-consider-when-investing-in-iron-ore>> 21 October 2014; Moody's website, "Ration Action: Moody's assigns first-time B3 to Mongolian Resources; outlook stable", 8 October 2012, <[https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR\\_256966](https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR_256966)> (21 October 2014).

67 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

68 Ibid.

69 Reuters website, "TEXT-S&P rates Mongolian Resources Corp. 'B-'; outlook stable", 8 October 2012, <<http://www.reuters.com/article/2012/10/08/idUSWLA441720121008>> 21 October 2014.

70 Moody's website, "Ration Action: Moody's assigns first-time B3 to Mongolian Resources; outlook stable", 8 October 2012, <[https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR\\_256966](https://www.moody.com/research/Moodys-assigns-first-time-B3-to-Mongolian-Resources-outlook-stable--PR_256966)> (21 October 2014).

71 Mining-Technology.com website, "The world's biggest iron ore mines", 19 February 2014, <<http://www.mining-technology.com/features/featurethe-worlds-11-biggest-iron-ore-mines-4180663/>> (21 October 2014).

extended period of time. This could reduce the incentive for meaningful stakeholder engagement and relation building with the local community.

**Table 1: Expected remaining mine life of Tayan Nuur and a selection of the world's largest iron ore mines**

| Mine             | Country           | Expected (remaining) mine life (in years) |
|------------------|-------------------|---|
| Tayan Nuur       | Mongolia          | 10  |
| Carajas          | Brazil            | 51  |
| Samarco Alegria  | Brazil            | 39  |
| Minas Itabiritos | Brazil            | 33  |
| Vargem Grande    | Brazil            | 44  |
| Zanaga           | Republic of Congo | 30  |
| Simandou         | Guinea            | 30  |
| Sishen           | South Africa      | 18+                                       |

Source: Mining-Technology.com<sup>72</sup>

72 Mining-Technology.com website, "The world's biggest iron ore mines", 19 February 2014, <<http://www.mining-technology.com/features/featurethe-worlds-11-biggest-iron-ore-mines-4180663/>> (21 October 2014).

## 4 Impacts at the Tayan Nuur mine

This chapter is based on excerpts from the report of the Fact Finding Mission drafted by CEE Bankwatch, SOMO and OT Watch. This report describes the findings of an August 2014 mission to Tseel Soum and surrounding communities. Each of the impacts that were identified during this mission are discussed in the context of the characteristics of the iron ore mining sector in Mongolia (as described in Chapter 2) and the business strategies of Altain Khuder (as described in Chapter 3).

Among the key findings of this mission were:

- ❑ issues related to the use and construction of the road from the mine to the Chinese border, which is linked to the company's strategy of being a low-cost supplier of iron ore;
- ❑ issues related to the involuntary resettlement of herders at the mine impact area, which might be exacerbated by the company's aggressive expansion plans; and
- ❑ inadequate stakeholder engagement, which can be partially explained by the relatively short lifespan of the mine.

A number of the impacts described in this chapter had been identified in earlier assessments. In 2011, Altain Khuder commissioned the consultancy firm ERM to conduct an Environmental and Social Review & Action Plan for the Tayan Nuur mine.<sup>73</sup> This Action Plan outlined a number of steps that needed to be taken in order to mitigate adverse impacts of the mine and work towards bringing the Tayan Nuur project in compliance with the Performance Requirements of the EBRD's Environmental and Social Policy. The fact-finding mission of August 2014 also assessed whether some of these steps had indeed been taken.

### 4.1 Impact of the road: dust pollution and animal and human health impacts

Altain Khuder exports iron ore from its mine in Tseel Soum to China via the Burgastai border post, a distance of approximately 168 kilometres.<sup>74</sup> The roads that are used for the transportation of the ore are dust and gravel roads, and the heavy trucks transporting ore generate dust and noise. The company is currently constructing a paved road, which will allow it to export iron ore to China faster and at a lower cost. As mentioned in the previous chapter, Altain Khuder expects that the paved road will reduce its transportation costs by 25%.<sup>75</sup>

73 ERM, Environmental and Social Review & Action Plan; Tayan Nuur Iron Ore Mine, Gobi Altai, Mongolia, 13 December 2011.

74 MRC Mongolian Resources Corporation, Powerpoint Presentation presented at Mines and Money Hong Kong 2014, 25-27 March 2014, <[http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar\\_S2\\_1230\\_Javkhlanbazar-Radnaabazar\\_Mongolian-Resource-Corp.pdf](http://www.minesandmoney.com/hongkong/wp-content/uploads/2014/04/26Mar_S2_1230_Javkhlanbazar-Radnaabazar_Mongolian-Resource-Corp.pdf)> (21 October 2014).

75 Idem.

A paved road is also expected to reduce the dust and noise pollution, and is said to have a development impact for local communities by improving the transport infrastructure in the area. The governor of Tseel Soum confirmed that 30 kilometres of the black top road has been constructed and 59 kilometres of it are expected to pass through the Soum.

The summary below outlines the identified impacts of transportation of iron ore on the existing road and the construction of the new paved road in the Tseel Soum area, as reported by the nomadic herders who were interviewed during the fact-finding mission. The testimonies of the interviewed herders are in line with the general findings by the National Human Rights Commission of Mongolia, as described in Chapter 2, regarding the health impacts of the dust pollution created by roads used by mining companies.<sup>76</sup>

### **Dust pollution and animal health impacts**

A major issue pointed out by all interviewed herders and by the Tseel Soum administration is the dust pollution created by three main sources: the heavy trucks transporting ore on the dirt and gravel roads from the mine to the Chinese border, explosions during the mining of ore, and the 'dry' techniques used to process the ore to concentrate. The transportation of ore to the border appears to affect the nomadic herders the most, as the road covers a large stretch of land (from the mine to the Chinese border post) and cuts through animal pastures. While definitive numbers of affected herders are unknown, it is likely that they constitute a much larger group than the herders affected directly by the mining operations.

In 2011, ERM's Environmental and Social Review & Action Plan identified ore stockpiles, the mine pit, ore processing and the road between the mine and the Chinese border as significant sources of 'fugitive dust', while noting that existing controls include speed limits (20 km/h) for trucks travelling to the border.<sup>77</sup> Visual inspection of the fact-finding team found that these speed limits are not always observed. An inspection report by the National Inspection Office of Mongolia, a translation of which was shared by Altain Khuder, indicates that dust levels at various points around the road were within approved limits of 0.5mg/m<sup>3</sup>.<sup>78</sup> Despite the results of these measurements, which were taken in 2013, herders continued to report the negative effects of the dust pollution in 2014.

The interviewed herders report that dust from the road and the mine pollutes the grass and water sources and causes illnesses to their grazing animals. Herders whose camps are near the transportation route or in the mine impact area reported that since the Tayan Nuur mine started its operations, their animals are increasingly getting sick. Animals suffer from mucus and diarrhea, and slaughtered animals have reportedly had dark spots on their lungs. Birth defects, congenital disorders and animals returning from grazing with black mouths from the dust that sticks to vegetation were also reported. Herders indicated having lost up to several dozen animals, mainly goats and camels, due

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76 National Human Rights Commission of Mongolia, 12th Report on Human Rights and Freedoms in Mongolia, Ulaanbaatar, 2013, <<http://www.asiapacificforum.net/members/full-members/mongolia/downloads/annual-reports/2013>> (17 October 2014).

77 ERM, Environmental and Social Review & Action Plan; Tayan Nuur Iron Ore Mine, Gobi Altai, Mongolia, 13 December 2011, p. 16.

78 Conclusion of the State Senior Inspector for National Inspection Office of Mongolia, translation provided by Altain Khuder, 24 November 2014.

to dust-related illnesses. Although the Tseel Soum authorities indicated that they had not detected rising levels of fatally sick animals, they also recognised the increased risk of lung diseases, if dust pollution is not reduced.

In response to complaints from the herders about the health impacts of the ore transportation on their animals, a series of veterinary and laboratory tests were administered to the animals, with mixed outcomes. Several herders from Derstei Bagh reported that their animals were tested on multiple occasions – once on the initiative of the Council of Natives and at least twice on the initiative of Altain Khuder.<sup>79</sup> According to them, Altain Khuder agreed to compensate them for any animal losses if it was proven that this was caused by the company's actions. The results from the first test were published in a newspaper and confirmed that lung diseases were caused by the dust pollution. The company seems to have challenged these findings and requested a review of the legitimacy of the laboratory assessment process, which resulted in a letter from the Research Institute of Veterinary Medicine noting several mistakes and errors.<sup>80</sup>

Tests initiated by the company, undertaken by the Veterinary Institution in Ulaanbaatar on sheep and goats in Bayanghol Bagh in 2013, indicated that no fatal disease or illness originated from negative dust impacts.<sup>81</sup>

According to the herders, results from the company tests were never communicated back to them. One herder reported that a lab officer informally confirmed that dust pollution was in fact the reason for the sickness of his animals. Altain Khuder has never proactively discussed the results of the tests they administered, nor has it paid compensation for any animal losses. In response to a draft version of this report, the company indicated that the environmental inspection reports are shared on a quarterly basis with local authorities, but that it never received any requests from herders for these results.

Despite being concerned about the health impacts of the dust on their animals, the nomadic herders indicated that they continue to use their pastures. Finding alternative pastures is difficult in desert areas like the Gobi Altai region; there are no vacant fertile pastures with adequate water resources and migrating to occupied pastures has implications for the herders and their livestock already inhabiting the area. Land areas not in use are of inferior grazing quality, and migrating to those areas would result in loss of herds and reduced quality of animal products, which are at the basis of the herders' livelihoods. In addition, herders are attached to their seasonal camps and corresponding pastures because of their strategic location and favourable climate conditions, and because of the fact that they have used these camps for generations. Herders also report that the type of pastures they require depend on the animals they breed. For instance, one herder noted that camel breeding requires a specific type of vegetation, which grows only in a particular valley that has been a traditional camel pasture for generations.

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79 The Council of Natives is a representative body for Tseel Soum inhabitants and is located in Ulaanbatar.

80 Research Institute of Veterinary Medicine, letter to Altain Khuder, 27 September 2013, translation provided by Altain Khuder, 24 November 2014.

81 A translated version of the results of these tests was provided by Altain Khuder.

Interviewed herders also report that they and their families have experienced skin rashes, chronic sneezing and sinus infections. The high cost of seeking medical assistance prevents them from consulting a doctor.

### **Impacts from the construction of the new road**

Both the herders and the Tseel Soum government consider the construction of the black top road as a potential solution to the dust pollution problem. However, the herders feel that they have not been adequately consulted about the construction of the road, despite the fact that the road cuts through their pastures, and their needs have not been taken into account. Their main problem with the new road is the lack of adequate passageways. The new road is slightly elevated and without accessible and safe passageways, the animals are obstructed from grazing the entire pasture as they normally would, which disturbs the grazing process. Altain Khuder has constructed several slopes for animals, but these are reportedly too steep for safe passage. In addition, the herders are blocked from crossing the road when they migrate to their seasonal camps with their herds. They are forced to make detours of several miles in order to bypass the road, which costs them additional fuel and time and creates stress for the animals. The herders regard this as highly problematic, especially during harsh weather conditions.

The construction of the road requires significant volumes of gravel. The raw materials for this gravel are retrieved from a number of stone, gravel and sand quarries alongside the road. The company has also created a gravel production site. Interviewed herders have indicated that these quarries not only create a lot of dust, but are also located at what used to be fertile grazing land. The size and quantity of these quarries have had an impact on the amount of grazing land that is available for their herds, further affecting the health of their animals and the quality of their products.

### **Loss of income due to dust pollution**

Twelve interviewed herder families from the Derstei Bagh area complained that, as a result of the dust pollution, the quality of wool and cashmere from their animals, which is the main source of income for many, has decreased. The local cooperative leader, who mediates the sale of animal products for a community of 200 herders, reported lower quality of cashmere and reduced market demand for their cashmere since the mine started operating. Reportedly, Chinese merchants recognise that the cashmere comes from a mining area and offer reduced prices or refuse to buy the product altogether.

## **4.2 Involuntary resettlement at the mine's impact area**

During the first phases of Altain Khuder's operations, between 2007 and 2011, 22 herder families who had land use rights to their winter camps at the site of the proposed mine were resettled by the company. Winter camps are the only type that herders have a land title to, and consist of 0.7 hectares of land on which herders set up their traditional nomadic tents and permanent structures to protect their animals from the harsh winters. The land title does not include the pasture surrounding the camp. The size of pasture needed to herd livestock varies from 5 square kilometres to 30 square kilometres, depending on the type of animal and weather conditions. At least one herder indicated that displacements continue to take place to this day to make way for the mine's planned expansion. In addition to the resettled herders, there were an unknown number of displaced

herders with grazing land in the area where the mine is now located. Altain Khuder's resettlement programme includes cash compensation, but does not include the allocation of new land.

While the company maintains that it does not have the authority to allocate new land, the Environmental and Social Review & Action Plan from December 2011 did identify several key shortcomings in relation to the acquisition of land and the related resettlements, and proposed various corrective actions;<sup>82</sup>

- ❑ to identify the number of physically and economically displaced households at each of the project sites (mine, camp, road, etc.) for past and future displacement;
- ❑ to demonstrate through a post-resettlement survey of displaced households that livelihoods of displaced households are equal to or higher than pre-displacement levels; and
- ❑ to undertake a survey and demonstrate that compensation paid for loss of assets was at full replacement value.

These actions were to be completed by May 2012 and were the responsibility of Altain Khuder's public relations officer and the Environmental, Social and Health Impact Assessment (ESHIA) contractor. While the company indicated that all corrective actions had been completed, none of the interviewed stakeholders were aware of any surveys being conducted (see below).

Given the company's heavy debt burden and strategy of rapid expansion (see Chapter 3), it can be expected that the mine impact area will continue to expand over the coming years, which might result in additional resettlements. If and when the current downswing in iron ore prices comes to an end, the company will be forced to further increase the speed of its expansion in order to meet its production targets. This could lead to significant impacts for herders and other local stakeholders, making it more important that the corrective actions outlined above are implemented.

### **Resettlement negotiated with individual herders**

Altain Khuder paid cash compensation for the resettlement directly to the herders in addition to a number of other support measures. According to the Environmental and Social Review & Action Plan, "All land attachments (i.e., human and animal shelters) were compensated for on the basis of negotiated settlement, with compensation at market price for lost assets being used as the principle for the negotiation".<sup>83</sup> According to the interviewed stakeholders, such negotiations took place on an individual basis, without involvement of local officials, although the company maintains that land officials and governors were in fact present. The Tseel Soum Governor stated that the administration was unsure of their role in the negotiation process as they had never faced issues of resettlement and compensation before. The Governor argued that the Soum administration cannot interfere in bilateral agreements between Altain Khuder and the herders. Rather, they see a role for the Soum government in ensuring that agreements between the company and herders are respected, yet remain unsure how to do so.

With negotiations conducted on an individual basis, herders were unable to negotiate on an equal and informed basis. One resettled herder indicated that she was not fully aware of her property

82 ERM, Environmental and Social Review & Action Plan; Tayan Nuur Iron Ore Mine, Gobi Altai, Mongolia, 13 December 2011.

83 ERM, Environmental and Social Review & Action Plan; Tayan Nuur Iron Ore Mine, Gobi Altai, Mongolia, 13 December 2011, p. 22.

rights and the value of her land when the company started the negotiation. She thought she had no other option but to hand over her property rights, and was unaware of the exact implications of this act. The mining operation would proceed regardless of her decision, and she felt she only had a choice between accepting the proposed compensation or receiving nothing at all. She did not realise that the agreement with the company meant that she would have to vacate her land, as she was under the impression that the company would only want to make use of it. The herder was asked by the company to bring her permit and received a cash payment in exchange. Given the remoteness of the area and the fact that land is democratically awarded rather than bought, the herder had no means to assess whether the compensation had been fair. Later, she was told by a relative who works in the local administration that the value of her property was 14 times higher than the compensation she received.

Some herders reported that the compensation payment was delayed or was not transferred. The Soum governor reported that a number of herders had to travel to Ulaanbaatar in order to complain that the compensation had not been paid and in order to receive their cash payment.

### **Cash payments not effective compensation**

Regardless of whether the compensation amounts reflected the true value of the herders' camps, a separate issue is that cash payments are not an effective means of compensating and resettling herders. As explained by the Bayangol Bagh Governor, available land in the Bagh is democratically appointed to herders at quarterly meetings and cannot be purchased, meaning that herders cannot use the compensation to purchase new land to construct alternative winter camps. Cash compensation thus does not enable resettled herders to find new land, and since Altain Khuder's resettlement programme did not include allocation of land, resettled herders have not found new locations for their winter camps. One interviewed herder indicated that her applications for new land have been rejected by the other herders at Bagh meetings, who regarded her acceptance of compensation as wrongfully selling community owned land to the company.

According to Altain Khuder, herders have complained to them that the local authorities are unwilling to issue new land permits and it has requested the Tseel Soum Governor to provide new land to the displaced herders. The Tseel Soum government however does not consider itself responsible for providing alternative land specifically to the resettled herders. The Soum has a general procedure for issuing new land permits every year and the local government stated that there is enough land available to relocate the herders. Interviewed herders disagree with this statement explaining that land with sufficient pasture to sustain their animals is already occupied. Vacant land often remains unused because it is not suitable for grazing animals.

This leaves displaced herders in a position where they cannot use the monetary compensation to buy new land for their winter camps, and are unable to obtain new land as the other herders refuse to grant them access. As neither the Soum government, nor the company is taking any effective action to relocate these herders, they have nowhere to go. As a consequence, several of the herder families have tried to return to the winter camps they handed over to the company. According to the Soum governor, Altain Khuder has requested his assistance in removing herders who moved into the mining site, disrupting mining operations and exposing themselves to health and safety risks. These were all families who had been displaced before.

### **Stakeholders unaware of post-resettlement survey**

As part of the agreement to undertake a post-resettlement survey, Altain Khuder hired a company specialised in such surveys, which concluded that herders have not lost assets as a result of the mining activities. This company also conducted a comparative analysis of the livelihoods of households before and after the resettlement, and Altain Khuder reports that a number of its social programmes were based on the outcomes of this analysis. However, none of the people interviewed during the fact-finding mission were aware that such a survey had ever been conducted. Neither the Tseel Soum Governor nor the herders had been contacted by the company that had undertaken the survey.

At the same time, several interviewed herders indicated that, since the start of the mining project, their lives have been seriously and negatively impacted. One resettled herder indicated that her herd is now half the size compared to before resettlement, and that she has become dependent on relatives for survival. She is now sharing their land, while her herd grazes on their pasture. At the time of the fact-finding mission, she stayed at the summer camp of her relatives, and planned to go to the winter camp of her son-in-law later in the year. However, the winter camp of her son-in-law is also located in the mining area, and he reportedly was also going to be resettled. The herder was unsure whether she would still be able to access the camp during the coming winter. If access to this camp was denied, she reported to have no other options.

## **4.3 Inadequate stakeholder engagement**

As discussed in Chapter 3, the company aims to rapidly expand its mining operations, while the expected lifespan of the mine is limited to 10 years. Arguably, such a relatively short operational lifespan reduces the incentive to meaningfully engage with local stakeholders, while fully respecting their rights.

According to the company, engagement with the community in Tseel Soum was initiated from the early stages of the project. The company also committed to developing a stakeholder engagement plan, undertaking dust deposition monitoring, disclosing information on dust pollution and water use to Tseel Soum communities, and establishing an effective grievance mechanism. The company also asserts that representatives of local herders, Tseel Soum authorities and Bagh governors have been involved in the relocation programme. However, the fact-finding mission revealed a lack of transparency towards stakeholders and reports of intimidation and harassment towards its critics.

### **Lack of transparency**

Based on the interviews with affected individuals and local government bodies, the fact-finding mission concluded that stakeholders are lacking information about Altain Khuder and the Tayan Nuur mining project and its impacts. Interviewed herders and authorities reported that they have not been consulted prior to the start of the mining project, either by the company, the EBRD or contracted consultants. They also are unaware of assessments or surveys on the impact of the mine on their livelihoods. The Soum and Nagh governing structures admit that they lack knowledge and capacity to effectively protect the rights of the people impacted by the mine, and are uncertain about the company's and the government's respective responsibilities as the Tayan Nuur mine is the first mining

project in the area. All interviewed herders reported that the company never disclosed information about dust pollution or water use.

The herders from Bayanghol and Derstei Baghs also reported that they had no knowledge about the involvement of the EBRD in financing the mining project, and are unaware of the responsibilities that arise from the EBRD's investment. One group of herders stated that they regard the mining project as a unilateral project of a wealthy individual who pushed them off their land, grabbed their resources and destroyed their environment and means of livelihood.

### **Intimidation and harassment**

Among the interviewed people in Tseel Soum, Altain Khuder has become notorious for intimidating those who criticise its activities. The company has filed up to seven lawsuits against people who openly criticised the company or expressed their grievances, and charged them with '*organized crimes of defamation*'.<sup>84</sup> This is a serious crime in Mongolia, which can result in up to 22 years of imprisonment. Bagh Governors, healthcare workers and citizens' representatives were sued and had to appear in front of the Gobi Altai court. When the charges were dropped on the grounds of lack of substance, the company continued to pursue the case at higher instance courts in Ulaanbaatar, leading to high travel expenses and reputational damage for the people involved. In May 2014, the final stage court acquitted the case. The seven defendants are currently preparing to file a counter-claim for costs incurred and reputational damages.

Several of the interviewed herders reported that, when they approach the mining site to talk to representatives about their grievances, they are intimidated by the mine's security personnel and prevented from entering the site. While there are legitimate security reasons to block people from entering mining sites, such incidents do suggest that these herders face difficulties getting in contact with company representatives. The Council of Natives also reported intimidating treatment by the company, including one experience where their camera equipment and mobile phones were seized and never returned.

### **Ineffective company level grievance mechanism**

Altain Khuder has placed a suggestion and complaint box in the administrative building of the Soum government, in accordance with its commitment to establish a company level grievance mechanism.<sup>85</sup> The company also appointed a contact person responsible for communication with the local communities. However, only one of the interviewed herders reported being aware of the complaint box. This herder once submitted a complaint in the box, but never received a response.

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84 OTWatch, Fact Finding Mission Report, Tayan Nuur (Lake Tayan) Iron Ore Project, 6-11 March 2014, unpublished.

85 Idem, p. 25.

## 5. Violations of environmental and social standards

As a result of the financial relationship between Altain Khuder and the EBRD, the company has an obligation to comply with the Performance Requirements (PRs) of the EBRD. This chapter discusses those key impacts of Altain Khuder's mining operations that are discussed in the previous chapter in relation to these environmental and social standards.<sup>86</sup> As outlined in the EBRD's Environmental and Social Policy, PRs stipulate responsibilities of the bank's clients in ensuring the project's environmental and social sustainability. In short, the PRs outline standards that Altain Khuder is expected to meet in relation to areas including environmental and social management (PR1), community health and safety (PR4), resettlement and displacement (PR5), information disclosure and stakeholder engagement (PR10).

### 5.1 PR 1: Environmental and Social Appraisal and Management

PR 1 has the objective of ensuring a systematic approach to managing environmental and social impacts and monitoring on an ongoing basis, and emphasises the importance of engaging with stakeholders. In order to comply with this standard, Altain Khuder should conduct appraisal activities such as an environmental and social impact assessments, in consultation with relevant stakeholders. This includes a due diligence process whereby the company should *'identify and assess any potential future impacts associated with the proposed project, identify potential improvement opportunities, and recommend any measures needed to avoid, or where avoidance is not possible, minimize, and mitigate adverse impacts'*.<sup>87</sup> Based on the environmental and social appraisal, an Environmental and Social Action Plan (ESAP) should be developed and implemented.

The appraisal process was found to be inadequate by an external consultant commissioned by Altain Khuder to conduct an environmental and social review and to prepare an action plan to bridge gaps between the company's operations and the PRs. According to the consultant, Altain Khuder's impact assessment did not meet the PRs with respect to ecological impact assessment, disclosure of information, documentation of consultation, impacts of project's water use, and social impacts.

Interviewed herders impacted by the mine and local authorities furthermore reported a lack of consultation about the impacts of the mining project on their lives, both prior to the start of the project as well as during its operations. The herders' accounts point to a serious lack of action

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<sup>86</sup> This chapter only includes an assessment of the responsibilities of the company under the Performance Requirements in relation to the specific impacts that are the focus of this report. The fact-finding mission also found other negative impacts, and the assessment thereof and the corresponding PRs can be found in the fact-finding report. "For this case study, the 2008 Environmental and Social Policy was used since this policy applies to Altain Khuder and the Tayan Nuur mine, and was the policy in force during the documentation and analysis of the adverse impacts. On 7 November 2014, the EBRD's new Environmental and Social Policy entered into force. This Policy applies to projects initiated after 7 November 2014.

<sup>87</sup> EBRD, Environmental and Social Policy, May 2008, <<http://www.ebrd.com/downloads/research/policies/2008policy.pdf>> (21 October 2014), para. 10, p.18. The Tayan Nuur mining project has been identified as a category B project by the EBRD.

to collect information about the mine's impacts, as well as failure to act on the feedback of stakeholders and improve its performance. Instead, herders have been confronted with intimidation and harassment when they voice their concerns or try to have the company address their grievances.

## 5.2 PR 3: Pollution Prevention and Abatement

PR 3 has the objective of avoiding or minimising adverse impacts on human health and the environment, by avoiding or minimising pollution arising from the project. According to the EBRD, '*pollution prevention and abatement are key ingredients of a sustainable development agenda and EBRD-financed projects must meet good international practice in this regard*'.<sup>88</sup> To meet the requirements of this PR, Altain Khuder should address any adverse impacts on the environment by avoiding or, when this is not feasible, minimising or reducing the release of pollutants, including addressing impacts of the mining project on the surrounding environment and taking into account cumulative impacts with uncertain consequences.

According to the available test results provided by Altain Khuder, the dust levels in Tseel Soum are within acceptable levels. Nonetheless, as reported in Chapter 4, interviewed stakeholders reported significant dust pollution caused by the mining project, which negatively affects air, soil and vegetation and impacts animal and human health. Some herders reported that, in response to their concerns about the impacts of the dust pollution on their livestock, the company initiated tests on their animals, but that the results were never disclosed to them. While herders fear for their health and that of their animals, they continue to use affected grazing lands. Considering the fact that this is a semi-desert area, dust pollution of this environment and its vegetation can have severe consequences, including desertification.

## 5.3 PR 5: Land Acquisition, Involuntary Resettlement and Economic Displacement

PR 5 aims to mitigate the impacts of involuntary resettlement as a result of land acquisition and restrictions on use of and access to land. This includes demonstrated decreases in livestock resulting from project-related disturbance or pollution. Involuntary resettlement is defined as both:

- ❑ physical displacement related to relocation or loss of shelter; and
- ❑ economic displacement related to loss of assets resulting in loss of income sources or livelihoods. 'Displacement' applies both to those who have legally recognisable rights or claims to land, as well as those with customary claims to land, users of land with no title or claim, and seasonal resource users such as herders.

In order to meet the requirements of PR 5, Altain Khuder should take actions including consulting with affected persons (including host communities), and facilitate informed participation in decision-making regarding displacement and resettlement. Affected people should have the opportunity to

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<sup>88</sup> Idem, para 1, p. 26.

participate in the negotiation of compensation packages, resettlement assistance and suitability of the proposed resettlement sites. For those herders without titles to land, Altain Khuder should have offered a suitable alternative site with security of tenure. Altain Khuder should also have developed a Resettlement Action Plan to mitigate, monitor and evaluate the impacts of resettlement on both resettled herders and on communities at the site where herders are resettled to, as well as a Livelihoods Restoration Framework for economically displaced herders.

Regarding the type of compensation, PR 5 specifically states that monetary compensation is only appropriate in contexts where livelihoods are not land-based, or when the land taken for the project is a small fraction of their land and the residual land is economically viable.<sup>89</sup> Where livelihoods are land-based, compensation should also be land-based.<sup>90</sup>

As documented in the previous chapter, the company has not provided the herders with any options for a suitable resettlement site, nor have the herders been adequately consulted about the process. Rather than the required land-based compensation, displaced herders received cash compensation, which is not an appropriate form of compensation when livelihoods are land-based and ineffective in the context of the Mongolian land tenure system where land cannot be purchased. No information is available about the existence of a Resettlement Action Plan and the Livelihoods Restoration Framework.

## 5.4 PR 10: Information Disclosure and Stakeholder Engagement

PR 10 emphasises the importance of information disclosure and stakeholder engagement in order to successfully manage environmental and social impacts on communities. Stakeholder engagement is regarded as an ongoing process of information disclosure, consultation with affected parties and the establishment of a grievance mechanism.

In order to meet this PR, Altain Khuder should provide information about the project and the implementation of the Environmental and Social Action Plan, and receive feedback on how it is implementing this, among other things. As is also evident from the previous chapter, and the above assessment of the other PRs, the company is breaching this PR in several ways. All the interviewed individuals stressed the complete lack of information about the company, its financiers and the mining project. The possible and actual environmental and social impacts of the mine and its associated facilities were not known to interviewees, nor had they engaged with the company or been consulted about how to manage impacts and find an acceptable way for all parties involved to reconcile various interests. In fact, at least seven people who complained about the mining project were faced with criminal cases against them. An effective grievance mechanism has not been established, violating the requirement that the company should establish a grievance mechanism process to receive and facilitate resolution of concerns and grievances, which the

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89 EBRD, Environmental and Social Policy, May 2008, <<http://www.ebrd.com/downloads/research/policies/esp-english.pdf>> (21 October 2014), para. 30 and 35, p.40-41."

90 Idem, para 30, p. 40.

mechanism should address promptly and without retribution. Based on the EBRD guidance on implementing the PRs, an independent and objective appeal mechanism should also have been established. As mentioned in the previous chapter, the company has placed a suggestion box at the Tseel Soum centre, but only one of the interviewed herders knew about this, and his complaint was never followed up by the company.

## 6. Conclusions

A number of overall conclusions can be drawn from the findings discussed in the previous chapters that are relevant for the iron ore sector as a whole. This chapter analyses a number of these findings and concludes that:

- ❑ local communities can be negatively affected by transportation infrastructure associated with the mine;
- ❑ one-off monetary payments are an ineffective and counterproductive means of compensation; and
- ❑ short mine lifespan and high production targets can reduce the incentive for meaningful stakeholder engagement.
- ❑ The involvement of a development finance institution is no safeguard against adverse impacts.

### 6.1 Transportation infrastructure impacts communities

This case study illustrates how stakeholders can be affected not only by the mining operations but also by the infrastructure associated with the mine. This is particularly relevant for the iron ore industry, as transportation of ore is a determining factor in the business model of any iron ore mining company, and roads and railways are an integral part of its business.

In the case of Altain Khuder, the construction of the paved road from the mine to the Chinese border provides the company with the advantage of reduced transportation costs. However, the use of the current road, as well as the construction of the new road, has adverse impacts on the nomadic herders that use the land. Herders report that both the dust created by the large trucks as well as the quarries dug to provide gravel for the new road impacts the grazing and health of their animals. Herds have difficulties crossing the elevated road that lacks passage ways, thereby losing access to pasture and facing difficulties moving from one camp to the other, while the quarries have destroyed fertile grazing land, thereby impacting the health of the herd.

These findings show that the group of stakeholders affected by the mining operations is larger than those living at or in the vicinity of the mine itself. Infrastructure development is often presented as a benefit to surrounding communities, as it might be in many cases. However, newly built infrastructure can cut through land that is already in use, and increased traffic linked to a mine can have significant health and safety impacts, even for communities living further removed from the actual mine.

Transportation costs are a significant element of iron ore prices and determine the competitiveness of iron ore mining companies. New iron ore mines are likely to be located in more and more remote areas, as deposits located near export ports are likely to be mined already, and will have longer transportation routes. Therefore, it becomes increasingly important to recognise the risk of adverse environmental or social impacts related to roads, railways and other forms of transportation infrastructure associated with the mine. This case study shows that it is incorrect to assume that improved infrastructure is solely to the benefit of local communities. Their livelihoods and health can in fact also be negatively impacted.

## 6.2 One-off monetary payments are not adequate compensation

Another lesson that can be drawn from this case study is that the appropriate form of compensation for resettlement of local communities is dependent on local contexts. While land tenure systems in Mongolia have developed towards individual land tenure since the end of Communist times, in many places pastureland continues to be held and managed as common property. For Mongolian herders, mobile and flexible grazing arrangements and strategies are exactly fitted to cope with the harsh conditions in the areas they live in, and therefore are key to their survival.<sup>91</sup> Altain Khuder's method of making cash payments to compensate herders for the loss of their winter camps has proven to be ineffective and counterproductive. These herders were unable to use the compensation to purchase new land to resettle to, as land is democratically appointed rather than bought and sold. In fact, this case study has identified at least one herder who was blocked from new land precisely because she received monetary compensation.

This illustrates how cash payments do not mitigate the adverse economic and social impacts for involuntary resettlement and economic displacement of communities, but might in fact create more hardships among vulnerable groups. Incomes are not restored or improved, and resettled herders have experienced great difficulties in maintaining their livelihoods. An additional factor in this case study is that, as well as the company, local and regional governments also refused to accept responsibility for a proper resettlement programme, partially because of their lack of experience and know-how of properly dealing with mining operations in their area. This leaves displaced herders with little to no options.

While environmental and social standards such as the EBRD Performance Standards recognise the need for a resettlement plan that includes assistance in restoring livelihoods and standards of living, as well as placing responsibility on the company to offer suitable resettlement sites, and emphasising the importance of compensation in kind when livelihoods are land-based, such standards are not always adhered to. In the case of Altain Khuder, the company agreed in their Environmental and Social Review and Action Plan to conduct a post-resettlement survey to assess the need for any assistance, but never honoured this commitment. The EBRD, with its leverage over the company through its loan and equity investment, has not been able to guarantee adherence to its own policies.

The volatile and current low iron ore prices pose a challenge to Altain Khuder, which needs increasing revenues to pay off its debts. If Altain Khuder is to meet its production targets it will have to expand its mining area and additional involuntary resettlements are likely to take place in the future. Given the current low prices for iron ore, such expansion is more likely to take place at a time when iron ore prices have recovered and might then take place in a hurried fashion. This further heightens the risk that herders might be 'bought off' with one-off cash payments, and do not receive the assistance they need to restore or improve their standards of living. There is a significant risk that future resettlements might not take place in a careful and well planned manner in compliance with the applicable environmental and social standards.

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91 Fernandez-Gimenez, M., Land use and land tenure in Mongolia: a brief history and current issues. USDA Forest Service, 2006, p.1, <[http://www.fs.fed.us/rm/pubs/rmrs\\_p039/rmrs\\_p039\\_030\\_036.pdf](http://www.fs.fed.us/rm/pubs/rmrs_p039/rmrs_p039_030_036.pdf)> (30 November 2014).

This case study illustrates how the price volatility of iron ore can have a knock-on effect on the livelihoods of local communities. As the price for iron ore is not guaranteed, companies will make use of the short window of opportunity created by higher iron ore prices to ramp up production. Rapid expansion of iron ore production can mean that there is little room for careful planning of resettlements, heightening the risk of adverse impacts for affected communities.

### **6.3 Short mine lifespan means little incentive for proper stakeholder engagement**

Thirdly, Altain Khuder did not engage in proper stakeholder engagement. On the one hand, the company appears to apply a tick-box mentality for its engagement efforts. The company has put in place a suggestion box, as a sort of company-level grievance mechanism. However, this mechanism does not appear to function effectively, as most of the interviewed herders were not aware of its existence. As already discussed above, the one herder that did make use of this suggestion box indicated that his complaint was never followed up.

On the other hand, the company has taken an overly aggressive approach towards its critics. Herders, local political representatives and other stakeholders who raised the issue of the adverse impacts by the company's operations have been taken to court and have been threatened with excessively long prison sentences as the company charged them with the 'aggrieved organized crime of defamation'. When lower courts threw out the case, the company persisted by going to national courts, only to have these courts reject the claims as well. However, the proceedings resulted in extensive travel costs for the critics of the company, who have interpreted the company's actions as a form of intimidation and an effort to silence them.

The company's approach to local communities might be explained by the relatively short lifespan of the mine. Given that ore reserves are estimated to dry up within 10 years, which is a relatively short lifespan for any mine, the company might not be incentivised to act as a good neighbour. Rather, the company's business model appears to be based on a year-to-year increase in production of iron, and meaningful engagement with local communities might result in delays that are in conflict with this business model. Criticism of the company will only have to be neutralised for a few years before the company wraps up its operations and leaves the area.

### **6.4 EBRD involvement no safeguard against adverse impacts**

Finally, a notable characteristic of this case study is the involvement of a development bank in the project. The EBRD's investment in Altain Khuder is part of its strategy to finance mining-related operations in Central and Eastern Europe, Central Asia and the Mediterranean in order to foster transition towards market-based economies. This strategy, as outlined in EBRD's Mining Policy, focuses both on the so-called 'transition challenges', such as state ownership, trade barriers, poor

infrastructure and the use of outdated technologies, as well as on promoting responsible mining and the application of the best international standards.<sup>92</sup>

The social and environmental considerations that are included in its investment strategies make the EBRD and other development banks distinctly different from mainstream investors. One could expect that the involvement of the EBRD in the Tayan Nuur project would positively contribute to the social and environmental management of the mine and reduce the adverse impacts experienced by the herders and other local stakeholders, given the EBRD's emphasis on responsible mining. However, as this case study proves, the involvement of the EBRD is no safeguard against such adverse social and environmental impacts for local stakeholders.

One potential factor is that the EBRD has not provided adequate disincentives to avoid ineffective resettlements or inadequate stakeholder engagement. The review identified several points where the company was not in line with the PRs in 2011, while this case study shows that the company is still not in adherence with several of these PRs three years later. To illustrate, the lack of involvement, or even awareness, of stakeholders in the post-resettlement survey has not appeared to have had any consequences for the company.

This case study has illustrated that meaningful stakeholder engagement, with respect for community and herders' rights as well as proper mitigation measures that address social and environmental impacts and that are to the actual benefit of communities, are not only the result of good intentions of a company's decision-makers or sustainable policies of its investors. They can also be explained by business factors such as the need for infrastructure, mine lifespan and production targets. If such business factors come into conflict with engagement and resettlement processes, the rights of herders, communities and other stakeholders could be deprioritised and their livelihoods could be endangered.

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92 EBRD, Mining Operations Policy, approved by the Board of Directors on 17 October 2012, <http://www.ebrd.com/downloads/policies/sector/mining-operations-policy.pdf> (21 October 2014).

## Annex: EBRD's Performance Requirements

The list below provides the hyperlinks to the descriptions of each of EBRD's 10 Performance Requirements (PRs).<sup>93</sup>

PR 1: Environmental and Social Appraisal and Management

PR 2: Labour and Working Conditions

PR 3: Pollution Prevention and Abatement

PR 4: Community Health, Safety and Security

PR 5: Land Acquisition, Involuntary Resettlement and Economic Displacement

PR 6: Biodiversity Conservation and Sustainable Management of Living Natural Resources

PR 7: Indigenous Peoples

PR 8: Cultural Heritage

PR 9: Financial Intermediaries

PR 10: Information Disclosure and Stakeholder Engagement

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<sup>93</sup> EBRD website, "EBRD Performance Requirements", no date, <<http://www.ebrd.com/environment/e-manual/e31ebrd-performance-requirements.html>> (21 October 2014).

## Impacts of the global iron ore sector

### Case Study: Altain Khuder in Mongolia

This report provides a case study on the Mongolian mining company Altain Khuder, which receives financing from the European Bank for Reconstruction and Development. The case study intends to identify social and environmental impacts of the iron ore sector. It links sector characteristics and corporate strategies with adverse impacts on local communities. Business factors such as the need for infrastructure, mine lifespan and production targets can come into conflict with meaningful stakeholder engagement. In such cases, the rights of communities are deprioritized and livelihoods threatened. The involvement of a development finance institution is no safeguard against such adverse impacts.

