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ENCLAVE PROJECTS

What Are They and What Can Be Done?

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This document was prepared by a Bank wide Working Group integrated by: Virginia Alzina (SDS/ENV), Elizabeth Davidsen (EVP), Anne Deruyttere (SDS/IND), Rodolfo Huici (RE3), Javier Jiménez (LEG), Juan Antonio Ketterer (RE1), Robert Montgomery (PRI), Gijs Nolet (PRE), and Ana Cristina Torres, Loreto Biehl, Francesco Lanzafame, and Mayra Buvinic from SDS/SOC who coordinated the report. Juan M. Benavides (SDS/IFM), Elizabeth Brito (PRI/ESU), Marie Clotilde Charlot (ROS/PMP), Eduardo Rojas (SDS/SOC), María da Cunha (SDS/IND), Joseph Christopher Milewski (SDS/ENV), Priscilla Phelps (RE2/EN2) and the participants to the CRG also contributed to the report.

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Executive Summary

This report addresses the IDB Board of Directors' request for an issues paper on the advantages and disadvantages of including positive social programs in enclave projects, *after* appropriate mitigation and compensation measures are in place. For this report, enclave projects are large, productive oriented public or private sector investment projects that import technologically sophisticated production and/or marketing systems into the local economy, operate with a high degree of autonomy and export the goods produced. A defining feature of these projects is that the direct benefits flow outside the community where the project operates. Enclave investments can become problematic when they result in present or future losses to the community, some of which may be difficult to fully assess and compensate, and/or unrealized community expectations of increases in wellbeing.

Positive social programs are investments that seek to enhance the human and social capital of individuals and communities. Including positive social actions in enclave projects can have many benefits and few risks, if the actions are well thought out and are not confused with "hand outs" or charity. Effective social programs would benefit the community, help reduce territorial inequality, and help reduce the emergence of conflicts between the project and the community, among others. A desk review of the project experience of the international financial institutions (IFIs), including the IDB, and the private sector catalogues social actions into those that are directly related to the enclave investment (promoting supply chain linkages and other actions) and those that are not, including human resources development, SME development, etc. The former actions seem to have greater likelihood of project success than the latter. Unlike mitigation and compensation, which are mandatory and included in project costs, social enhancement actions are not mandatory but highly desirable. However, because there is no clear separation between social mitigation and social enhancement, because some losses may never be fully compensated, and because of the unique opportunity that these projects present for fostering balanced economic and social development in a territory, the IFIs, including the IDB, are well positioned to take the lead in promoting effective positive social actions in enclave operations.

Specific project circumstances determine who --the public sector, the private sector, the IFI-- should underwrite social actions in enclave operations. But all actors, including the community and its resources, have key roles to play in insuring that effective social actions take place in enclave projects, and coordination among them is essential. Specifically, the IFI, in this case the IDB, should continue to ensure that environmental and social safeguards are strictly complied with; use its leverage and resources to advice and assist the public and private sectors in including social actions in enclave operations; promote and disseminate good practices to reduce enclave risks; and coordinate and facilitate negotiations between all parties involved in the project. It has a key opportunity to enhance coordination and minimize enclave risks in ongoing country dialogue and programming.

1. Introduction

1.1 In October of 2002 the IDB Board of Directors appointed an independent panel to investigate if complaints filed by individuals and groups against the Termoeléctrica del Golfo (TEG) project, financed by an IDB private sector loan (loan 1223/OC-ME), had merit in terms of compliance with IDB policies. The main complaints centered on the negative environmental impacts of the construction of two thermoelectric plants (one financed by the IDB) in Tamuín, San Luis de Potosí, built to generate electricity for 13 cement producing plants in the central and northern regions of Mexico. In their final report of March 2003 (PR-2444-15), the panel concluded that the environmental issues raised in the complaints were unfounded and that the Bank had complied with all applicable operational policies, except for parts of the Information Disclosure Policy (OP-102). The panel also agreed that the project complied with safeguards governing the environmental, social, health and safety aspects of PRI projects, and included an environmental and social management plan as well as a workplace safety and health plan.

1.2 However, the independent panel also noted that the increasing energy supply would benefit Mexico as a whole, while there likely would be no long-term direct benefits to the local population in Tamuín. It therefore recommended that in future "enclave" projects of this nature, "particularly when carried out by the private sector, it is essential to include a positive social program agreed upon by the IDB and the national or local government in the country where the project is to be built to cover at least some of the unmet basic needs in the project area, especially in poor regions" (PR-2444-15 p.14).

1.3 In response, in July of 2003 the IDB Board of Directors requested that Management prepare an issues paper on the advantages and disadvantages of including positive social programs in enclave projects (PR-2444-20). Since the intention of these social programs is not to replace the required safeguards of mitigation and compensation but to add "development value," the Board made it clear that this issues paper should focus on analyzing the advantages and disadvantages of social enhancements that occur *after* appropriate mitigation and compensation policies are in place. In addition to this analysis of advantages and disadvantages, questions of interest to the IDB Board were: should positive social programs be mandatory or optional features in Bank operations; who should pay for them; and whose responsibility should it be to include these programs in enclave operations (the government, the private sector, the IDB)?

1.4 This report addresses the above request. That is, it analyzes the advantages and disadvantages of including positive social actions in enclave projects *after* appropriate mitigation and compensation policies are in place, and addresses both the question of the mandatory or optional nature of these actions and the question of the responsible executing and financing agent or agents. The report defines enclave projects, reviews the experience of international financial institutions, the private sector and the IDB with including positive social programs in enclave operations, and presents review findings and conclusions. It is based on a desk review of project experience, covers enclave projects undertaken by both the public and private sectors, and emphasizes reviewing good practices to offer project suggestions for IDB staff.

2. Enclave Projects

What are they?

2.1 The term enclave has been used in various ways in the development literature and the Bank's project experience. The independent investigation panel used it to describe a project that "is inserted in a community for reasons that have nothing to do with the community's demands or needs and has no immediate, significant and permanent positive impact on its standard of living" (Llach et al., 2003 p.13). Early on, and perhaps most famously, Cardoso and Faletto (1969) used enclaves to explain industrial development and capitalist expansion in Latin America in the dawn of the 20th century, during one of the world's earliest globalization waves. Enclave stood for inserting production controlled by external agents with heavy capital investments and highly specialized technology and marketing systems in a local economy, where domestic producers lost significance.

2.2 According to these authors, mining and plantation enclaves led to concentration of income in the enclave sector, increased income inequality, and political subordination of workers and peasants to dominant classes. But enclave economies and enclave projects do not necessarily have to have the negative attributes just mentioned. IDB documents, for instance, use the term enclave to describe export-oriented commercial projects expected to generate foreign exchange (in Panama) and mention the creation of "enclaves of excellence" (by providing training or employing consultants, in Trinidad and Tobago)[1]. The African Development Bank defines an enclave project as "a commercially viable, self-sustaining, export oriented project, operating through a legally autonomous entity incorporated in a regional member country" (AFDB circa 2000). And the investigation panel similarly stated that enclave projects are not necessarily negative in and of themselves. See Box 1 for different usages of the term enclave.

2.3 While there is no agreement on an operational definition of enclave projects or their inherent development value or "goodness," there is some common understanding of their basic elements. First, in physical terms, an enclave project or an enclave economy is a structure enclosed within another structure. It is an autonomous entity that is significantly different from its surroundings. Second, in economic terms, an enclave project imports large capital investment and more advanced, technologically sophisticated production and marketing systems into the local economy while it exports the goods produced to generate foreign exchange and/or meet national needs. Generally, the goods produced have positive macroeconomic impacts but no lasting direct benefits to the local economy. Enclave projects can have short-term benefits to the local community

[1] "Panamá. Desarrollo Empresarial de la Micro, Pequeña y Mediana Empresa" (TC-0006035), IDB, September 2000. Mimeo; "Country Program Evaluation. Trinidad and Tobago: 1985-1999," IDB August 2001. Mimeo.

(through, for instance, employment generation during construction) but no sustainable impacts. And third, enclave projects do not (and are not meant to) generate sustainable social development in the locality where the project takes place.

2.4 When can enclaves become problematic? According to the Chair of the independent panel for the TEG project, conditions that trigger complaints, despite adequate mitigation and compensation actions, include high community expectations of potential benefits when a large outside investment takes place that may be met in the short term but are frustrated in the medium term. In enclave projects, the expected negative environmental consequences may be adequately mitigated, but the positive expectations of increases in wellbeing may not materialize, resulting in unmet community expectations and community perceptions of unfairness in the allocation of benefits (Llach 2004). While this characterization of when enclaves become problematic may be questionable (instead, narrow political interests may take advantage of and nurture community complaints), it underscores both the disconnect that may exist between favorable outside evaluations and negative community assessments of project impacts on local conditions as well as the role of community expectations in shaping complaints.

2.5 A more fundamental reason for the problematic nature of some enclave projects is the possible competition for the use of limited resources between the state, outside sponsors and local interests, which may result in the loss of local control over community resources. Even when conflicts are well managed, and communities participate in the decision making process and receive appropriate mitigation and compensation, sometimes negative impacts (particularly in the cultural and symbolic realms) may not be adequately mitigated and can become a source of conflict. Another possible source of complaints is the community's identification of real future risks that are not perceived by outside parties. In this situation, the objection of the community is not rent seeking but a form of risk management against future costs, which project mitigation analyses should but often do not or are not able to identify as costs.

2.6 Based on the above, for the purpose of this report, enclave projects are defined as large productive oriented investment projects that import technologically sophisticated production and/or marketing systems into the local economy, operate with a high degree of autonomy and export the goods produced. A defining feature of these projects is that the direct benefits flow outside the community where the project operates. Problematic enclaves may occur when interventions result in losses or future costs which are not fully compensated or appropriately consulted with the community and/or when they give rise to but do not meet community expectations of future benefits.

Box 1: Some Definitions of Enclave Projects

US State Department [1]

- …loans to export-oriented commercial projects that generate foreign exchange…..

The United Kingdom Parliament [2]

- … "enclave projects" (with) very few backward, vertical and horizontal linkages which will produce lasting broad-based benefits …
- …new external investments barely touched the average citizen….

The European Bank for Reconstruction and Development [3]

- …" enclave projects" that may have positive effects within the confines of the project but that lead neither to significant knowledge spillovers nor to the building of capacity for the future.

The African Development Bank [4]

- …an enclave project is defined as a commercially viable, self-sustaining, export-oriented project, *operating through a legally autonomous entity (the project company), incorporated* in a regional member country…….. Projects in manufacturing, mining, agriculture, agro-industry, as well as infrastructure, such as power generation, gas pipeline, telecommunications, transportation, which are undertaken by private investors in partnership with the government, could be considered as enclave projects, subject to their being able to generate sufficient foreign exchange and to meet the above conditions.

UNDP [5]

- Enclave projects with a narrow focus in terms of area of intervention and duration are becoming increasingly discredited. Often they leave little behind other than locally cultivated success: there is little or no effort to create an institutional memory. And spots don't necessarily spread spontaneously.

The World Bank [6]

- …Enclave projects whose benefits bypass local people...

- There are numbers of different types of International Development (ID) Projects as follows:

"Hard " versus "Soft". Originally most ID Projects were civil work construction projects like railroads, ports, dams and power plants. These had clear goals and could be contracted to large experienced international firms. They were called "enclave" projects. Over the last three decades the mix of projects has changed drastically to "soft' or projects aimed to human development like education, health and institutional development.

IMF [7]

In addition to borrowing to finance poverty spending and other (generally non-commercial) investment, some governments, at times, borrow to finance government equity in commercial activities with private (foreign) partners and identified export markets. Oil exploitation, pipelines, and hydroelectric dams are examples of such projects. These projects (known as enclave projects) are expected to become self-financing once brought on stream, as the associated export earnings are likely to be more than sufficient to service any debts incurred during the construction phase. A natural question when discussing debt sustainability in low-income countries is, therefore, the degree to which enclave project should be included or excluded from government borrowing limits…. In light of their prospected commercial viability, one should be reasonably argue that enclave projects should be excluded from borrowing limits. However such a judgment would have to be made with great care.

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1 U.S. Department of State. *Fact Sheet: State Department on HIPC Debt Relief Initiative*. November 2000.

2 U.K. Parliament. *Selected Committee on Trade and Industry – Third Report*. Memorandum submitted by Save the Children Fund (On a project in Mongolia), October 1998.

3 Stern, Nicholas. *Investments on Poverty: The Role of international Financial Institutions,* April 2001.

4 African Development Bank. *Bank policy on financing enclave projects,* circa 2000.

5 United Nations Development Program. *Innovation, Farmers and Land Husbandry: An Overview of Methodology and Issues, 2002.*

6 World Bank. *Development Extractive Industries,* 2004; Youker, Robert. *The Nature of International Development Projects*. World Bank, 2004.

7 IMF. *Debt Sustainability in Low Income Countries – Toward a Forward Looking Strategy,* May 2003.

2.7 In this context, a broad range of productive investment projects can have potential enclave consequences. They typically include investments in extractive industries (oil, gas and mining), other energy industries, such as power plants, and both export manufacturing and export agricultural projects. Potential enclaves include as well processing plants of primary products for national or export markets, ports and airports linked to industrial production, and tourism projects that build separate, highly autonomous tourism infrastructure within relatively deprived communities. In all these projects direct benefits flow outside the community and there is the potential that project actions may result in environmental and/or social disruptions.

2.8 As it is implied in the examples above, enclave projects are not necessarily restricted to the private sector. Both the public and private sectors can finance and execute these operations, although they have different competencies and responsibilities regarding the economic and social development of the locality where the enclave takes place. In contrast to the more restricted role of the private sector, in the economic realm, the public sector has the function of and is accountable for enabling both local economic and social development. Furthermore, because enclaves are large productive investments with a significant impact on the economy, the latter sector has a regulatory role to play even in projects financed by the private sector. But increasingly these differences in competencies and roles are becoming more nuanced: the private sector, through greater corporate social responsibility, is assuming or sharing responsibility for the social development of the localities where it operates. The public and private sector are seeking increased partnerships under which, for instance, the public sector may subcontract large projects to private sector firms.

<u>The case for positive social action</u>

2.9 Positive social programs are investments in the human and social capital of individuals and communities. There are good reasons to include positive social programs in enclave projects. First, there is ample evidence in the development project literature of negative social and environmental consequences of enclaves, some of which go beyond those that are subject to compensation and mitigation (see, for instance, EIR 2003; World Commission on Dams 2000). They include losses in present or future income sources, as when the community has to stop growing traditional crops and loses revenues (and often times nutritional status), or when it anticipates the loss of future employment income with the closing of the project plant; increased poverty due to rise in the cost of living at the local level; risk of environmental contamination; human rights problems as a result of badly supervised construction operations; social conflicts, including increases in levels of alcoholism, violence and the exploitation of women, rise in the incidence of HIV/AIDS and other contagious diseases; cultural and customary losses and dislocations; and increased demand for local water sources, housing, etc., among others. Second, community complaints in the case of enclave projects, many resulting from faulty consultation processes, can increase project costs and severely disrupt project execution. See Box 2 for examples of disruptions in project execution. Third, enclaves can increase inequality in a territory, intensifying this recalcitrant development problem in Latin America-- which records the highest income inequality among world regions. And fourth, paradoxically, negative impacts can emerge from sudden and massive money inflows (including those of compensation) creating incentives for corruption. Many of these negative project consequences and project conflicts can be avoided by having appropriate consultation processes, compensation and mitigation policies, but because of the continuum that exists between mitigation and enhancement (see 2.10 below) as well as the difficulty of forecasting in advance some of these negative consequences, they also provide the rationale for positive social programs.

Box 2: Examples of Social Conflicts in the Exploitation of Natural Resources

Environmental and indigenous organizations, both in the region and in industrialized countries, often protest against oil and gas exploration activities perceived as having important negative effects in the environment and in local communities that have not been adequately consulted prior to taking action. These protests manage to delay and in some cases to cancel projects. Examples of recent conflicts originated in the Andean Region include:

- Opposition to the Cuiaba natural gas pipeline that cut through a primary tropical forest, by environment groups and indigenous communities, in Bolivia.
- Protests, legal actions and violent conflicts in Colombia due to the opposition of the U'wa people to oil exploration by Occidental Petroleum in U'wa territory.
- Lawsuit against Texaco (for $1 billion) by indigenous communities in the Oriente region in Ecuador for contamination with toxic waste and crude oil.
- Suspension of the construction of a high power electric grid in Venezuela in 1999, as a consequence of the protests undertaken by the Pemón indigenous group.

Source: Donahue, M and M. Dixon, "Concept Paper for Bank Support to Pre-Qualification of Oil and Gas Exploration/Production Blocks Andean/Amazon Basin Countries," Washington, D.C., IDB November 2000. Mimeo.

The mitigation-additionality continuum

2.10 The IDB has built safeguard policies and guidelines and established loan committee reviews, including the Committee of Environmental and Social Impact (CESI) mechanism, to mitigate potentially negative direct and indirect environmental and social impacts of the projects it finances. They mandate the Bank to compensate populations directly negatively affected by Bank interventions and mitigate negative environmental and social consequences. (See Box 3 for definitions of these terms.) The independent panel's recommendation to include socially positive actions in enclave projects (see 1.1 - 1.2) goes beyond the required safeguards of compensation and mitigation to wider socially sustainable development activities that add value and improve social conditions in the communities where the projects operate. The recommendation moves beyond making people whole again-- from mitigating negative impacts to enhancing social development, building and giving added value to Bank productive oriented interventions and, as such, falls outside the current mandatory review of the CESI. There is, however, a continuum between mitigation and enhancement and it is difficult to trace a clear line in terms of where compensation and mitigation end and enhancements begin. According to good mitigation practices, the same principles should apply to programs designed to mitigate negative impacts and those designed to promote development. That is to say, they should be appropriate, effective and sustainable and should allow the people that are affected by a project to develop their capacity rather than, as it often happens, simply establishing new ties of dependency (Renshaw et al. 2001). Well-designed mitigation actions, therefore, also should enhance social development.

Box 3. Definitions of Mitigation and Compensation Measures

Mitigation
Referred as the action "to relieve" or "make amends for." It refers to minor impacts (or impacts that cannot realistically be compensated), such as loss of habitat, ways of life, cultural sites, memories and sentimental value (Renshaw et al. 2001). Mitigation measures avoid, minimize or offset significant negative impacts that a project may generate in the human and natural environment. The purpose of mitigation is to generate actions oriented to bring to acceptable levels the environmental impact of human actions, ensuring that environmental conditions will be restored at least to the initial levels that existed prior to the project. (Espinoza 2002).

Compensation
Refers to the reproduction –or improvement, of the former conditions, and covers the replacement of lost assets, lost income or production, and access to community infrastructure and social services (Renshaw et al. 2001). Compensation measures look to generate alternative positive effects that are equivalent to the adverse effects caused by the project. Compensation can be understood as an extreme mitigation applicable in particular conditions. (Espinoza 2002).

Sources: Espinoza, Guillermo. "Gestión y Fundamentos de Evaluación de Impacto Ambiental," In *Plan de Manejo Ambiental* Chapter VIII. IDB, Chile 2002. Mimeo; Renshaw, Jonathan, M. Sant'ana and V. Von Bremen. "Guidelines for Socio-Cultural Analysis." IDB, October 2001. Mimeo.

2.11 As it was mentioned before (see 2.5), sometimes negative project impacts in enclave type operations that should become the subject of compensation or mitigation policies, such as the opportunity costs of using community land and other resources, take place in the future and are hard to forecast and quantify. As a result, they are not included in project costs and become conflated with the need for social enhancements, further blurring the line between mitigation and enhancement.

2.12 The multiple reasons that can give rise to enclave project complaints, from losses which may be not fully compensated to unrealized community expectations of anticipated benefits, add complexity to the analysis of enclave projects. The inability to conceptually clearly separate mitigation on the one hand from enhancements on the other, further complicates the analysis of what can and should be done about enclave projects and who should be the responsible agent.

An optional good practice feature

2.13 The Bank's mission is to promote economic and socially sustainable development in the borrowing member countries but many projects cannot capably integrate the provision of economic and social infrastructure and services in one design. As long as they do no harm (in social and environmental terms), projects that finance economic activities (such as infrastructure) are not mandated to include specific social infrastructure and services components as well. It follows that the Bank is mandated to mitigate (direct and indirect) negative impacts but that social development objectives (that is, investments in human and social capital for advancing people's well-being, including actions in health, nutrition, education, housing and others) are not necessarily best achieved in the short term at least through these types of economic development operations. Positive social interventions in enclave projects, therefore, should be desirable but not mandatory. As mentioned above, a challenge, however, is the conceptual difficulty in separating what is mitigation, especially resulting from indirect negative impacts of projects that may be difficult to anticipate, from what are social enhancements. Therefore, because of this conceptual difficulty that may lead to unattended negative impacts, the IDB has a unique opportunity to go beyond what is mandatory and add development value through social actions.

Advantages and disadvantages of positive social actions

2.14 By including effective social programs, enclave projects may present a unique opportunity for the government and the IDB to foster synergies between economic and social actions in a territory, and promote balanced development. The introduction of effective social programs in enclave projects should benefit the local community and government, the central government, the executing agency (the government or private sector company), and the financing institution - in this case, the IDB. By fostering social progress, effective social programs would benefit communities and governments and help reduce inequality within a territory. They should reduce the emergence of conflicts between the project agency and the community and community complaints and, therefore, prevent the possible disruption of operations. They could improve the private sector company's bottom line by enhancing its business reputation and the marketability of its products, and they would both fulfill the basic development mandates and enhance the effectiveness and reputation of the IDB.

2.15 Among potential costs or disadvantages are that social actions add complexity to the design and implementation of already large, complex economic development projects; carry a reputation risk for both the financing and executing agencies if the social actions are poorly executed, cut short from lack of funding, or converted into "hand outs;" and add costs (to underwrite the social actions) to total project costs. Although these may be a relatively minor proportion of overall project costs, the government or the private sector company may not be in a position to increase project costs, and the use of grant monies or non-reimbursable funds especially in the context of a private for-profit venture may not be available.

2.16 In addition, the social action in response to community demands, especially when it involves benefit-sharing schemes, may be unwarranted or create regional imbalances in the distribution of fiscal revenues. Instead, it may be in the country's best interest for the government to distribute the macroeconomic benefits of enclave investments (obtained through revenues, taxation or royalties) on a national rather than a local basis.

3. International Experience

The international development institutions

3.1 There is growing interest among the international development institutions in examining enclave projects and drawing guidelines for their performance. The IMF, the AFDB, and the World Bank Group (WBG) have all analyzed and made statements regarding enclave projects (see Box 1). In general, it can be said that these IFIs support financing enclave projects, but only when there is a strong poverty reduction rationale. Nevertheless, an emphasis is also made on the need to design complementary project actions, not only to mitigate negative social and environmental impacts but to also take advantage of all the positive elements so that the project will contribute to sustainable local development. In the case of projects that are executed by private companies, these actions are built into the theme of corporate social responsibility. In all cases, the government has an important role in generating optimum conditions so that private firms can implement social programs and guarantee their benefits.

3.2 Among IFIs, the WBG has done most extensive work on enclaves. As a follow up to a World Commission on Dams Report (2000), it defined a dams planning and management action plan that called for some form of revenue sharing with the local community to avoid the enclave consequences of dams, where benefits flow outside the communities where these projects are built. Box 4 outlines various forms of revenue sharing that, along with non-monetary benefits (such as skills transfer, social infrastructure, and income generation), are two general options to avoid enclave risks in development programs.

3.3 More recently, the WB commissioned an independent extractive industries review (EIR) of worldwide oil, mining and gas investments, including an intensive, two-year consultation process. The review reinforced the enclave feature of these projects: it concluded that they did not alleviate poverty at the local level and recommended that "extractive industries development should take place in a socially acceptable manner, where industries lay the basis for long term development rather than promote enclave projects operating in extreme isolation from the surrounding communities" (EIR 2003). The EIR stressed that sustainable extractive industries development required pro-poor governance, more effective social and environmental policies, and respect for human rights. It recommended managing the social risks of extractive industries by identifying clear and appropriate policies on social impacts; incorporating these policies into laws, regulations and obligations; undertaking local consultations and social impact assessments; making provisions for compensation when appropriate as well as community participation in project benefits and sharing of fiscal revenues; and promoting corporate social responsibility. Because of their mandates and unique institutional features, and their power in convening and operating the interface between government, investors and local groups, the EIR called the IFIs to give advice and assistance to help enhance the local economic impact of extractive industries development, providing the additionality of development impact beyond pure finance.

Box 4: Revenue Sharing Mechanisms in Dam Projects

Revenue Sharing

In the case of revenue sharing mechanisms, part of the revenues are redistributed to local or regional authorities in the form of royalties tied to power generation or to water charges. Such mechanisms may be the result of negotiations between local or regional authorities and the promoter or may be defined in the legislation. In the latter case, the percentages of revenues which must be transferred to regional or local beneficiaries, and the destination of the proceeds, are generally specified.

Development Funds

Developments funds financed from power sales, water charges or government may be established to provide seed money for fostering economic development in the project-affected area. As for revenue sharing mechanisms, the objectives, structure and duration of development funds may be the result of negotiations between local or regional authorities and the promoter or may be defined in the legislation. Projects to be financed by the development funds may be specified or not. They may include for instance community facilities, training programs or job creation in industrial or commercial projects.

Equity Sharing or Full Ownership

A variety of mechanisms may allow local or regional authorities to partly or fully own a dam project. Local authorities thus share the risks of the venture but also its profits, if any. Moreover, they may in certain cases gain a degree of control over the design and operation of the project.

Taxes Paid to Regional and Local Authorities

Two main types of taxes paid to regional and local authorities can be considered. In some countries, the State allows local or regional authorities to directly tax dam owners (e.g. hydropower corporations) on the dam's property value or other basis. This mechanism is not linked to revenues since the tax applies whatever the level of power generated or water supplied by the dam operator. However, it represents a fixed charge for the producer, which has a direct impact on profits. Taxes to be paid to regional and local authorities can also be defined in State legislation, sometimes as a percentage of project sales or net income. In the latter case, this mechanism is similar to revenue sharing.

Preferential Electricity Rates and Other Water-Related Fees

Local or regional authorities may negotiate free energy or preferential electricity rates with the hydropower producer, which benefits all electricity consumers in their constituency and contributes to local and regional economic development. Similarly, water for irrigation or water used for domestic or industrial purposes can be supplied to adversely impacted communities at subsidized rates or for free. This mechanism is a form of revenue sharing since it results in less revenue for the dam owner and in avoided costs for beneficiaries.

Source: Palmieri, Alessandro. *Benefit Sharing from Dam Projects. Phase 1: Desk Study*. World Bank, 2002.

Private sector initiatives

3.4 The International Finance Corporation (IFC), the private arm of the WBG, promotes social and community development programs in the extractive industry loans that the IFC finances because they make business sense. They do not mandate private sector firms to undertake these activities, but rather respond to demands from those clients who are motivated to undertake them to stay profitable. The IFC promotes supply chain linkages to break from enclaves (as a condition of business with large clients), emphasizing SME development, and attempts to transfer labor and health standards to subcontractors. The IFC acknowledges, however, that supply chain linkages often are difficult to implement, especially when local resources and capacity is poor – which tends to be the norm rather than the exception

3.5 In addition, the IFC has targeted facilities from donor trust funds (the corporate citizenship facility) that it uses to make grants to clients to implement social and community development programs. For instance, it gave a $ 100,000 donation to a banana company in Ecuador to insure land tenure for its workers (see Box 5 for details). It also works on governance issues, including revenue management and distribution through taxes and/or royalties, only when the projects have sufficiently large anticipated revenues that this is worth doing. For instance, in the Inti Raymi mine project in Bolivia, financed by an IFC loan (of $ 40 million), local governments receive an increased portion of tax revenues. And in the Chad Cameroon pipeline, 10% of the revenues will be held in trust for future generations (Kyte 2004).

3.6 Private sector companies worldwide increasingly finance welfare, social and community development programs in the localities where they operate, under corporate social responsibility tenets. One important rationale for these actions is to increase the competitiveness of the firm in international markets. Action priorities tend to vary by region. In Asia social issues, such as child labor and worker benefits, stand out. In India, for example, large firms offer their employees benefits for themselves and their communities that, comparatively speaking, are far above those offered in developed countries. This boosts the firm's reputation with consumers. In Europe, on the other hand, priority is given to environmental actions and in sub Saharan Africa to health (HIV/AIDS) and community development. In LAC, firms emphasize good management of human resources to increase the firm's legitimacy in local communities where often there is mistrust of government agencies. A recent survey found that while only 8 percent of consumers in Asia had penalized private companies for their lack of social responsibility, 23 percent had done so in LAC and 42 percent in North America (Globe Scan/Environics International 2004). Box 5 gives examples of social and community actions that firms in LAC undertake to reduce the enclave risk of their investments.

Box 5: Social and Community Actions in Private Sector Projects in LAC: A Sample

Country	Project	Sponsor	Action	Description
Perú	Yanacocha, Cajamarca	Newmont Mining Co. & IFC 2003	Development of small and medium enterprises	A program has been developed to support regional SMEs in their ability to better compete when it comes to obtain contracts linked to the Yanacocha Mine. With the objective of diversifying the activities of local SME, the program is also bringing technical assistance, access to capital and capacity building to develop other sectors of activities not related to mining.
Perú	Gloria S.A.	Gloria S.A. 1982	Supply Chaín	With the objective to increase the local milk chain supply for the company, Gloria S.A. developed a project to identify and promote target interventions to improve productivity, output quality, household income for each producer type. The project also provides small-scale loans to all actors along the supply chain, from producer and transportation, to milk collection.
Ecuador	Favorita	Favorita & IFC 2001-2	Community Development	(i) Assists independent banana suppliers in their efforts to achieve ECO-OK certification (a program existing in various countries in North, South and Central America to certify the social and environmental sustainable management of rural enterprises). (ii) Develops educational programs to improve labor and environmental practices among independent banana producers. (iii) Supports primary and secondary level technical schools that represent an attractive option for minors between the age of 12 and 15 and complements the national efforts to eradicate child labor in the banana industry. (iv) Finances housing programs.
Bolivia	Aguas del Illimani	Aguas del Illimani 2001	Sales / Clients	The company maintained revenues and achieved concession objectives through the 1997-2001 period with one of the lowest water tariffs in Bolivia, despite an average 22% decrease in per-capita water consumption, through expanding the availability of water and sewerage services. This was achieved through innovative social marketing strategies, the introduction of financing plans for water connections and the adoption of appropriate reduced-cost solutions such as condominium sewerage. Proactive stakeholder engagement resulted in a reduced risk profile, and a successful tariff renegotiation for the 2002-2006 period which concluded in December 2001
Dominican Republic	Grupo M	Grupo M 1998	Supply chain	Grupo M supplies companies like Levi Strauss and Polo that required the accomplishment of minimum labor standards. Grupo M offered subsidized services of transportation, kinder garden and health for its employees and their families, such as training courses at different levels. In this way Grupo M increased its productivity and obtained new contracts with other international companies for its quality and social responsibility.
Chile	Henkel Chile	Henkel Chile 1995	Sales / Clients	Henkel Chile is an example of responsible marketing. The company substituted one of the components of an industrial adhesive, the toluene, toxic and addictive if used inappropriately. This was inhalated by street children becoming a major social and health problem. The increase in the cost was compensated by the increment of market quotas and by the reputation of social responsibility.
Bolivia	Gas Trans–Boliviano	Gas Trans–Boliviano 2001	Community Development	Gas Trans-Boliviano S.A. (GTB) is a Bolivian Company that was formed within the bi-national agreement between Bolivia and Brazil to execute the GSA. GTB owns and operates the Bolivia-Brazil natural gas pipeline in the Bolivian section, which is 557 kilometers long. In this territory there are 111 indigenous communities from three different ethnic groups. The natural gas pipeline deforested 1.500 has, and is in the process of deforesting 750 has. 87% of the people are very poor. GTB had to address long time of indigenous mistrust through direct contact, communication, transparency and time. Open relationships with two way dialogue were established. Trust in GTB' s people then became trust in the company. Two plans were designed and implemented: 1) The Ichepe Usaka Plan, with the indigenous people, which include: (i) Communication and training; (ii) Environmental coo-management; (iii) Community development, and 2) The Corporate Citizenship Plan with municipalities and non indigenous communities including: (i) Direct social action; (ii) Employment creation; (iii) Environmental co-management. GTB is also developing programs to create public value in order to avoid the wrong perception that a private company. can replace the state. Moreover every GTB manager and employee must spend one week a year in these communities, helping coordinate activities and deepen these relationship. By involving the local community GTB has built trust and gained valuable partners.
Brasil	Volkswagen do Brasil	Volkswagen do Brasil 1996	Health	In 1996 Volkswagen do Brasil established a program of attention of HIV/AIDS for its employees, their families and the local community, utilizing the radio-phonic services of the company, local magazines, internal newsletters and special publications. The program achieved a better understanding of the local community about the problem. The program also provides access to health care specialists, social assistance, specialists in nutrition, psychologists and in some case finances specialized hospitals treatments, access to analysis and drugs and domestic care.

4. IDB Experience

4.1 As is the case with the other development banks, in the IDB the opening of Latin American economies to globalization and foreign investment, the growing role of the private sector in the region and in the Bank, the strengthening of democracy and social and environmental activism, and the Bank's commitment to reduce poverty and promote sustainable economic growth all have focused attention on potential enclave investments and ways to address enclave risks. The issue is especially important because of growing energy and other large infrastructure operations in the IDB portfolio. For instance, the Bank has 28 energy projects in execution[2] and 80 additional in the 2004-2006 pipeline. Energy projects in execution add to a total of $1,814 million. Of this amount $ 956 million is private sector lending and $ 858 is public sector lending.

4.2 The IDB's loan portfolio in recent years has dealt with enclave risks in various ways. It includes large investment projects with few or no social actions along with projects at the other extreme of the continuum, where the infrastructure investment becomes one more component of a comprehensive regional development intervention package, including intensive community consultations and social actions (see Box 7). The tendency is for the IDB's public and private sector lending to increasingly incorporate social development activities in the enclave type operations it finances. Currently, approximately 50% of the energy loans in execution include some social actions in the project report. This same proportion explicitly mentions community participation as an important aspect in project design. Community consultation and social mitigation measures are higher in private sector (65%)[3] that in public sector (27%) energy investments. Measures that are specifically addressed in the above project documents are: expanded public consultation; development and implementation of funds, financed by royalties and company participation to assist in local economic development; a social strategy that explicitly states that local population and all affected parties must be informed about the company's policies, activities and safety standards; integral strategy to promote a long-term relationship with different project stakeholders; continuous presence of specialized community relation coordinators, among others. Unfortunately, there are yet no available impact evaluations of the effectiveness of these measures.

[2] According to the IDB's data analyzer system (OPS) on April, 2004.
[3] Some private sector loans do not specifically describe social mitigation measures but refer to the need of including them in the Environmental Impact Assessment. These projects were included in the calculation of the percentage of projects that include social mitigation measures.

Box 7. Darien Sustainable Development Program

The renovation of the Bayano-Yaviza highway in Darien, Panama, is considered among the best practices of sustainable development projects undertaken by the Bank and the Government of Panama (GOP). Not only was it a participatory development project aimed at creating the conditions for land use planning and for improving the living conditions of the population of the province, but also served to mitigate the impacts of the highway renovation project.

The highway had been previously financed by the IDB in 1973 but the negative impacts of increased migration to the area were not anticipated at that time. In 1996, however, when the GOP began conversations with the IDB to obtain financing for paving and renovating the highway, the Bank acknowledged the importance of creating a sustainable framework for the protection and management of natural resources, improving the quality of life of Darien communities, and strengthening public and civil society institutions and organizations.

The program's design took into consideration results from a wide-ranging process of community consultation as well as those from studies of land use planning, land tenure, regulatory structure, productive activities, infrastructure, basic services and multimodal transportation.

The five components of the program were: (1) land-use planning, titling, environmental management and protection; (2) institutional strengthening; (3) support for sustainable production; (4) improvement of the transportation infrastructure; and (5) improvement of basic services. The community consultation focused on fostering a proactive process of reflection on the part of the stakeholders concerning the problematic issues under consideration, and referred to the possibility of stakeholder participation in the sustainable development of the project within a process that establishes a series of rights and obligations and offers an opportunity to provide feedback to the project designers. Persons consulted expressed their willingness to assume, individually and collectively, forms of self-regulation for land-use planning and management if the program undertook to solve strategic problems. Communities presented program proposals for six areas: environmental protection, forest management, animal husbandry, farming, fishing and urban uses.

Although the ultimate objectives of the program have not been fully attained, a positive result attained thus far in the program is the community's interest in participating. This interest is likely the result of the lack of established land tenure and the limits on sustainable development, which those affected believed could be resolved by the program.

Source: Perafán, Carlos, and Helí Nessim. *Community Consultation. The case of Darién, Panama*. Inter-American Development Bank. Sustainable Development Department. Indigenous Peoples and Community Development Unit. 2002.

4.3 Many recent IDB infrastructure projects include social components that go beyond the mitigation of social impacts. The Camisea project, for example, includes the development and implementation of a Camisea fund, financed by the government of Peru's (GOP) royalties and private sector participation, to assist in local economic development as well as environmental and social development in project areas.

4.4 Various other private sector (PRI) projects have implemented community development and environmental and social programs; they have been described in a survey of PRI projects. For example, Consorcio del Este, the concessionaire for the Montevideo - Punta del Este Toll Road in Uruguay has supported various local social actions, including educational programs for needy children via "Crianças Unidas," medical, food and educational programs via "Maria Del Pilar," and contributions to the Maldonado Municipal Hospital. In the Energía Mayakan Pipeline Project in Mexico, the company's social responsibility actions have included assistance to local social capacity and infrastructure in the areas of health, education and poverty reduction.

4.5 In addition the Bank has developed policies, tools and mechanisms to design infrastructure and private sector operations and compensate and mitigate negative environmental and social impacts that can be helpful in averting enclave risks in projects. A review of Bank's policies and procedures points to existing instruments that are relevant to mitigate and enhance socially sustainable development in enclave operations. They include the Committee on Environment and Social Impact (CESI) (see Box 8), and a package of IDB sector strategies for increasing the Bank's effectiveness in achieving its twin overarching goals -- sustainable economic growth and poverty reduction and promotion of social equity. As part of this package, in particular, the *Social Development Strategy* gives guidance on the design of both human development (health, education and housing) and integrated programs to promote local development in a territory. Similarly, the *Competitiveness Strategy* charts actions to develop the entrepreneurial activities of the poor through microfinance and worker training programs as well as to promote corporate social responsibility.

Box 8: Committee on Environment and Social Impact

The CESI Procedures aim to enhance the quality of Bank operations, by promoting cost effective integration of environmental and social impact considerations into the design of the Bank's operational strategy, at the national and regional levels; by minimizing negative environmental and social impacts, and enhancing future opportunities and options to promote positive impacts, in all phases of Bank operations; by providing relevant information to enable Bank decision makers to effectively evaluate environmental quality and social impact factors in project analysis and approval; and by overseeing that the Bank's analysis and decision making processes regarding environmental and social impact are transparent and participatory.

Source: Inter-American Development Bank. *Procedures of the Committee on Environment and Social Impact (CESI)*. 2002.

4.6 The IDB also has initiated internal discussions regarding corporate social responsibility. They are reflected in "*The Role of Multilateral Development Institutions in Fostering Corporate Social Responsibility" (Vives 2004)*. The paper argues that multilateral development institutions have a broad role to play in fostering corporate social responsibility through promotion and advocacy, development of a conducive policy environment, provision of financial support and by promoting compliance, reporting and accountability.

IDB's private sector experience

4.7 The IDB's Private Sector Development Strategy (GN-2270-4) provides overall guidance to the Bank's Private Sector Department (PRI) on enclave type operations. It underscores the private sector's role in poverty reduction and emphasizes that the IDB group will promote responsible corporate behavior and deepen the dialogue between the public and private sectors through its lending and convening powers. A main premise is that good corporate governance and social responsibility allow firms to tap financial markets and earn the goodwill of consumers and other stakeholders, therefore contributing to the firm's development as well as its capacity to contribute to economic and social development and stability. When civil society and the private sector work together they can promote good business behavior and seek ways to improve how companies behave and govern themselves.

4.8 PRI has developed and implemented guidelines to provide an overview of the requirements and processes related to environmental, social, health and safety, and labor aspects of private sector projects PRI finances. "Environmental and Social Aspects" (see Box 9), first released in January 2000, states that the Bank is interested not only in preventing and mitigating the negative impacts of projects, but also in attempting to maximize positive benefits and impacts. This is done through both direct project benefits (e.g., increased employment, economic development, etc.) and the implementation of specific project programs (components) that provide "positive environmental and social benefits" (e.g., community investment programs).

Box 9: Environmental and Social Aspects (PRI)

PRI states the following fundamental principles for PRI projects related to environmental, social, health and safety, and labor aspects are:

- Comply with all applicable in-country and IDB environmental, social, health and safety, and labor legal requirements;
- Promote sustainable development projects that maximize to the extent possible the positive project-associated benefits while adequately mitigating project-related negative impacts and risks;
- Promote information disclosure, stakeholder involvement, and transparency;
- Promote use of sound environmental, social, health and safety, and labor practices and management systems; and
- Promote local, national, and regional economic and social development by utilizing the human, financial and material resources of member countries.

Source: Inter-American Development Bank. *Environmental and Social Aspects*. PRI Environmental and Social Guideline. Private Sector Department. March, 2004.

4.9 PRI works with private sector companies to help select the types of positive environmental and social programs companies can undertake to maximize their positive effect on local populations. "*Community Investment Programs: A Guideline for Enhancing the Environmental and Social Benefits of Infrastructure Projects*," a PRI document, encourages private partners to go beyond mitigating the negative social and environmental impacts of their projects, and support community investment programs. While a higher standard of social responsibility is demanded from private companies, in fact it is in these companies' best interests to seize the opportunity to develop mutually beneficial relationships with local communities. The objective of community investment programs is to improve the living conditions of residents, raise their earning capacity and income levels, ameliorate health issues and address threats to their environment or safety.

4.10 Possible community investment programs fall in two groups. First, socio-economic programs, which include program ideas that may not fall within the company's business strengths, and typically refer to the areas of environment, health, poverty reduction, community empowerment, education and indigenous people. Companies interested in implementing these programs are encouraged to form partnerships with specialized public agencies or non-profit organizations in order to ensure their successful implementation and long-term sustainability. Second, project-specific programs which fall within the company's business strength and are implemented in order to increase beneficial impacts in the communities in which private sector companies operate; they mostly refer to transportation, energy, water and sanitation and telecommunications programs. By directly assisting and participating in the improvement and development of local communities, IDB's private sector partners can be socially responsible neighbours and good corporate citizens.

5. Summary and Options

What they are

5.1 Summarizing, for this report enclave projects are large productive oriented investment projects from either the public or private sectors that import technologically sophisticated production and/or marketing systems into the local economy, operate with a high degree of autonomy, export the goods produced, and where the direct benefits flow outside the local economy. The positive macroeconomic impacts of these projects do not trickle down to the local level in the short or medium term while they may result in present or future losses/costs to the community, some of which may be difficult to fully assess and compensate. This and/or unrealized community expectations of project benefits can result in problematic enclaves, even after appropriate mitigation and compensation policies are in place, and help to explain the disconnect that sometimes exist between favorable outside and negative community assessments of the project impacts on local conditions.

5.2 The costs of these projects should incorporate adequate mitigation and compensation actions to minimize potential negative environmental and social impacts. Currently, the Bank does not require that these projects incorporate wider socially sustainable development activities that add social development value to the project and the local community, although increasingly it has implemented actions to promote them. Therefore, unlike mandatory compensation and mitigation policies, positive social interventions in enclave investments are highly desirable but not mandatory actions for the IDB.

5.3 This fairly straightforward statement, however, is complicated both because potential negative social impacts (including the opportunity costs of the project using local resources, such as land) may be difficult to forecast in advance and because there is a continuum between mitigation and enhancement, with no clear dividing line between them. As a result, often there will be potential for confusion between "must" and "highly desirable but optional" social actions. Expanded social impact evaluation knowledge should help the IDB to better assess the range of actions that should fall under mitigation and to better separate mitigation from enhancement. The suggestions below in this report address highly desirable but optional social actions. By including them, enclave projects may present a unique opportunity for the governments and the IDB to foster synergies between economic and social actions in a territory, and promote balanced development.

<u>What can be done</u>

5.4 From the review of project experience, in addition to adequate mitigation and compensation, five different types of actions can help avert or reduce the risk of enclaves in large productive oriented investments: (1) effective consultations with the local community where the enclave project will be located, beginning with the project's preparation phase. Since enclaves can result from unmet community expectations, thorough consultation and briefing of communities, and a fair negotiation process with them, no easy tasks by any means, should avoid or reduce the enclave problem significantly. Projects should strive to go further, and engage the community and its resources proactively, making the community part of the solution to future problems; (2) training in needed skills and the promotion of microenterprises and SMEs in the local economy, including access to credit and technology, to create supply chain linkages with the more advanced production and marketing introduced by the project; (3) social actions unrelated or only indirectly related to the productive project, including community development, health promotion, and provision or improvement of social infrastructure and services in the local community (electricity, garbage collection, health clinics etc.) financed by either the private sector firm through its corporate social responsibility program, the IFI through its grant mechanisms, or the government through reallocation of existing public revenues or a loan with the IFI; (4) local capacity strengthening to effectively manage the opportunities and impacts of projects ensuring participatory community involvement in monitoring environmental and social impacts and adequate implementation of mitigation, compensation and benefit sharing plans, and (5) revenue sharing schemes channeling to the local economy increased government tax revenues or royalties from the operation.

5.5 Box 10 below lists options for positive social programs in enclave projects that emerge from reviewing the international development, including the IDB, and private sector experience. They can be grouped into those that are directly related to the enclave's productive oriented investment (promoting supply chain linkages and other actions) and those that are unrelated to the main project investment. The latter grouping includes human resource development, provision of social infrastructure, technical assistance for SME development unrelated to the firm's products, etc. While there are no known evaluations of the impact of these different options on reducing risks associated with enclave operations, the common observation is that activities directly related to the main project investment have greater likelihood of project success than unrelated activities.

Box 10: Options for Positive Social Programs in Enclaves

Project related		**Project unrelated**
Construction	***Operation***	
Sales / Clients Provision of credit. Training in money management and banking services. Provision of credit and training to assist local people with development of rental housing or other services to cater to a large workforce.	Sales / Clients Facilitation of local employment	Health Development of social programs Education and information campaign on social ills, drugs, HIV/AIDS, prostitution, etc.
Providers Development of small/medium enterprises related to the project. Facilitating the local supply chain of goods and services required for project construction	Providers Development of small/medium enterprises related to the project. Facilitating the local supply chain of goods and services Environment protection services.	Service Provision Services improvement (telephones, electricity, waste recollection, health centers, etc.)
Human resources development Provision of training or skills enhancement for local people (in advance of construction) to allow them to benefits from higher wages during construction and improve their potential for similar work in future Training the local community for a good use of the income and benefits obtained during this phase of temporary jobs (savings, investments, use of temporary income to improve existing local micro enterprise or for the creation of new).	Human resources development Improvement of labor conditions and quality of life for employees and their families Health assistance, housing subsidies, etc.) - promoting the extension of these benefits to the local community.	Community development Financing of Scholl/education and other social services required by the community Recreational activities for children and adolescents. Micro-credit programs for the local community

5.6 Options can also be divided into those that provide a monetary benefit to the community and those that do not. Options for revenue sharing include: (a) the government or the private sector company sets up development funds from the royalties or revenues received to finance social or economic projects in the local communities; (b) the local or regional government assumes equity sharing or full ownership of the project investment, which implies transfer of the profits as well as the risks involved in the venture; (c) the government transfers the tax generated revenue to the regional or local authorities; and (d) the project gives the local community the goods or outputs produced at preferential or subsidized rates.

5.7 But the benefit-sharing scheme may be unwarranted or create regional imbalances in the distribution of the government's fiscal revenues. The IDB's *Sub National Development Strategy* (2125) provides the fiscal context for revenue sharing schemes and alerts to the importance of considering the fiscal arrangements between local and national governments, determined by constitutional restrictions, political realities and institutional capacities, in the design of these revenue schemes.

5.8 It is important to underscore that the IDB has useful instruments and considerable experience to support the five types of actions listed above. Among the former, it is worth highlighting the Bank's ongoing policy and programming dialogue with the country, which provide a singular opportunity to identify and minimize potential enclave risks and boost coordination between the relevant actors. Among the latter, it is worth mentioning the Bank's extensive experience with microfinancing and SMEs, skills training programs, social investment funds (SIFs), fiscal management of central and subnational governments, and, more recently, integrated community development projects, community consultation and participation, corporate social responsibility, and health and safety in the workplace. Lastly, the Bank has a long track record of giving grants for social issues, including financing SIFs.

The danger of charitable social actions

5.9 Social actions that are unrelated to the productive project often are visible (winning good-will), comparatively easy to execute, and preferred by firms following corporate social responsibility mandates. However, there is sufficient evidence in the development literature that questions the success and sustainability of perhaps well-intentioned social action – because the donation runs out, the implementers lack technical competence, the beneficiaries lack the time to participate, among others[4]. While they may be more difficult to implement, actions that generate supply chain linkages should be preferred. They will often seek to increase the economic opportunities of local residents through employment or subcontracting with the firm. Social and community actions unrelated to the project are worthy as well, if done well. Doing them well means some degree of assurance of their development sustainability. Many of the public health and safety interventions (such as HIV/AIDS prevention efforts) as well as those seeking to improve labor conditions should be included under social mitigation and become mandatory in projects funded by the IFI.

6. Conclusion

6.1 Including positive social actions in enclave projects could have many benefits and few risks, if (and only if) the actions are well thought out. This report has identified preferred actions and has warned of the risks of confusing social development initiatives with "hand outs" or charity. It has clarified that, unlike mitigation and compensation, which are mandatory and included in project costs, social enhancement actions are not mandatory but highly desirable. However, it has also pointed out that what is mandatory and what is desirable is often difficult to define precisely because of the lack of a clear separation between social mitigation and social enhancement, and that some present or future cost may be difficult to fully compensate. Given these ambiguities, and the unique opportunity that enclave projects may present for fostering balanced economic and social development in a territory, the IFIs, including the Bank, are well positioned to take the lead in motivating both the public and the private sectors to include effective positive social actions in their enclave operations.

[4] See, for instance, Tendler, J. "Turning Private Voluntary Organizations into Development Agencies: Questions for Evaluation," *AID Program Evaluation Paper* No. 12 USAID 1982; Buvinic, M. "Projects for Women in the Third World: Explaining their Misbehavior," *World Development*, Vol. 14, No. 5, May 1986.

6.2 In terms of who should foot the bill for the social actions in enclave projects, this depends on the specific project circumstances. The public sector should pay if the enclave project is a public sector intervention. If it is a private sector venture, who should do so depends on government fiscal policies and regulations over private sector investments, and the specific arrangement between the government and the private sector. In theory, the responsibility of private sector companies is discharged through the taxes they pay or other financial obligations they have with the government. Increasingly, however, the private sector is underwriting social development actions in the localities it works, and this is good for the locality and the company. But financial as well as technical support from the IFI may be needed to pilot both public and private sector programs and provide incentives to the government to expand its social development role in enclave operations, and to the private sector to spur corporate social responsibility.

6.3 Lastly, on the third question of interest to the Board –whose responsibility is it—the report argues that all actors have a role to play and that coordination between them is essential: the *private sector* needs to follow corporate social responsibility tenets; the *government* needs to guarantee the appropriate economic and fiscal framework for private sector investments, provide appropriate fiscal and labor regulations, coordinate actions with the private sector and among private sector firms, and provide incentives for private sector firms to invest in social development; the *international financing institution,* in this case the IDB, needs to first, make sure that the environmental and social safeguards are strictly complied with; second, use its leverage and resources to advice and assist the public and private sectors in including effective social actions in enclave projects; third, promote and disseminate good practices and knowledge needed to reduce enclave risks; and fourth, foster coordination and facilitate negotiations between all actors involved, including the affected community. The *community* is the last key actor, and projects should strive to engage the community and its resources in contributing to common local development objectives.

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