

UNDERSTANDING OF THE LOCAL CONTENT COMPLIANCE LAW FROM THE EXTRACTIVE INDUSTRY'S PERSPECTIVE

Written by *Theresia Charles Numbi*

PhD Candidate, St Augustine University of Tanzania, Tanzania

ABSTRACT

This paper discusses on the context to which local content compliance law applies in the extractive industries namely oil, gas and minerals. The author starts by discussing the concept of local content as a concept. Second, discusses the context in which local content compliance applies from an extractive industry perspective. The author planned to continue the knowledge since local content paradigms is vital concept to most resourceful rich countries. It is a qualitative research paper and the author used a doctrine-based legal research method. The paper gives a clear sense of the context in which local content complaints are based.

Keywords: Local Content, Compliance, Extractive Industry, Oil, Gas and Mining

INTRODUCTION

Local content is a strategy for deepening the domestication or localization of minerals value chains (MVCs). It aims to ensure that MVCs are substantively linked with the domestic economy and that more significant and more tangible benefits flow into the local economy through multipliersⁱ.

In the extractive industry, local content is allied with jobs, preference schemes for local businesses, skills, or value-addition generated anywhere in the domestic economy by mining companies, contractors, sub-contractors and service providersⁱⁱ. It can also be referred to as jobs created in the neighbourhood of mining sites. Moreover, local content can provide infrastructures such as schools, water supply, medical facilities, and roads that are not inputted into the mining economic operators but intended to benefit the local populationⁱⁱⁱ. Local content may be viewed as local ownership, control, and participation by citizens and the government.

Logically, local content measures the extent to which the extractive industry's economic operators extend, expand or distil the benefits to the local and national economy. The immediate effect of local content compliance is to influence foreign companies to cooperate closely with local initiatives in their procurement, set up a subsidiary, or engage in local production. The country adopting such measures hopes to develop its industry by forcing foreign companies to buy from the local industry or even invest in it.^{iv} It is significant to differentiate between local content and local participation as described in the level of equity ownership by local citizens.^v

Likewise, the local content paradigm is the contractual commitment between the State and investors, provided in the contracts (licenses or lease licenses in some jurisdictions). Oil, Gas and Mining companies must procure a minimum percentage of the local suppliers' services. The government establishes pre-conditions for a preference on using local goods and services that such companies must focus on to be issued with licenses and legally exist and operate.

The rationale behind applying the local content paradigm in a specific sector, is to promote the local economy. Moreover, local content initiatives ensure that natural wealth resources such as

oil, gas, and mining value chain is promoting the domestic economy through employment, local participation, technology transfer, and knowledge acquisition.^{vi}

In action, the concept of local content finds its origin in the Local Content Requirements (LCRs) policy tools used by the government to generate economic benefits for the local community and value addition for the nation^{vii}. It is a policy that where there are minerals, oil, and gas, there must be a portion of benefits that remain at host country (resource-rich country), which is beyond fiscal benefits. Thus, local content comprehends the local value-added to the national economy by purchasing local-made goods and services to realize socio-economic development.

There are several ways that LCRs in mining project(s) can be met. For example, workforce development such as local recruitment and training; investment in local suppliers; developing businesses and services locally; procuring equipment and chemical suppliers; and securing consultancy, exploration, extraction, transport, and processing services in the country; beneficiation and local linkages^{viii}.

It is important to note that history suggests that both developed and developing countries have used local content in extractive industries. Local content is often formulated either as a provision within a hydrocarbon agreement such as a Production- Sharing Agreement or license or legislative instruments, such as Acts and regulations. Sometimes countries implement local content without having in place contracts or legislation. For instance, in Norway, the government provides preference to Norwegian bidders when proved to be competent and skilled in the extractive industry. History shows Norway did not have an explicit law or had not made a specific legislative requirement to share the local content compared to a country like Brazil^{ix}.

The Context within which the Local Content Applies in Extractive Industry

A) Local Content and Protection of Human Rights

Economic operators in the extractive industry can profoundly impact the human rights of employees, consumers, and communities where they operate. The impact may be complimentary, such as increased access to employment or improved public services, or damaging, such as polluting the environment, underpaying workers, or forcibly evicting

communities. These caused local communities and international institutions to debate the responsibilities of companies in handling these adverse impacts and the government's role.^x

In 2008, the United Nations endorsed the Protect, Respect, and Remedy Framework' for business and human rights.^{xi} It recognized that States and business enterprises have a duty under international human rights law to protect human rights abuses within their territory. States are required to take appropriate steps to prevent, investigate, punish, and redress such violations through effective policies, legislation, regulations, and adjudication.^{xii} The guiding principles being that States have obligations to respect, protect and fulfil rights and fundamental freedoms; business enterprises as specialized organs of society performing technical functions are required to comply with all applicable laws and to respect human rights; there is a need for fairness and obligations to be matched to appropriate effective remedies when breached.^{xiii}

On the other hand, business enterprises are also required by the guiding principles to respect human rights wherever they operate.^{xiv} In the view of local content advocates, once multinational companies respect human rights, they become more acceptable by local communities within their operational jurisdictions hence quickly obtaining a social license to operate.^{xv} These Guiding Principles align with other international obligations that set standards for State and businesses, such as the human rights-based approach principles, including development, participation, accountability, equality, non-discrimination, transparency, among others.^{xvi}

In the contemporary globalized world, human rights are the dominant normative priority. For example, it is common to struggle for national self-determination, class-based and labor empowerment, and property rights protection under economic globalisation. Due to the need to eradicate poverty, human rights have gained new insight and accommodate "development" to fit the semantic of human rights and related concepts, such as fundamental human capabilities and multidimensional poverty.^{xvii}

Development, as a concept, local content first entered human rights as the idea of the right to development. The idea establishes a legal and moral authority to developing countries' requests

for the international redistribution of resources to upgrade their development and transfer development from the realm of charity to the realm of rights. It also assumes actions to realize human rights, civil and political, economic, social, and cultural. The human rights-based approach to development (HRBAD) is an international human rights framework that integrates international human rights principles into development work. The HRBAD confirms that development is on a par with realizing human rights without marking whether development is or is not a human right.^{xviii}

The right to development was recognized legally in Article 22 of the 1981 African Charter on Human and Peoples' Rights. It was later incorporated into the global human rights framework through 1986 of the Declaration on the Right to Development by the United Nations General Assembly. The 1993 Vienna Declaration and Programme of Action, the 2000 Millennium Declaration, and the Durban Declaration and Programme of Action reconfirmed development as a universal and inalienable human right. Moreover, Article 1 of the Declaration on the Right to Development defines the right to development.^{xix}

Therefore, local content is a development strategy used by governments to promote the national economy. It ensures that people's rights and interests are upheld; local communities get a reasonable share in every business activity within the extractive area. Once a national government performs its duty to protect, respect, and remedy and the economic operators respect human rights, it is easy to gain local community confidence. Businesses around the extractive industry will also flourish because unnecessary conflicts will be reduced or avoided.

B) Local Content and Resource Nationalism

For many resource-abundant countries, the debate is what role should natural resources play in the economy and what policies should the country apply to maximize natural wealth to contribute to the economic development of the Government and the citizens.^{xx}As a result, resource nationalism becomes a top deliberation worth pursuing.

The term resource nationalism comprises a set of policies and practices that intensely highlight the maximization of public revenue, the assertion of strategic state control in a specific sector, and the enhancement of developmental spill overs from extractive activities. The said policy reduces the autonomy of the operator in the extractive industry and provides for mandatory

obligations that every private entity must comply with while doing business.^{xxi} Further, governments are actively seeking to maximize the contribution of a foreign firm to government revenue and economic development.

Resource nationalists consider the home nation should be the primary beneficiary of natural resource extraction. They also insist that the natural resource sector be self-industrialized, meaning exports like natural gas would be further processed locally before export. Additionally, they have demanded an increased flow of rents to “the people.” Resource nationalism is not a new idea, and it has been applied in Latin America, the Middle East, and Northern Africa.^{xxii}

To date, local content policies are perhaps the most prevalent form of resource nationalism, and they may be the single most innovative initiative in the energy policy. When properly implemented and supported by relevant stakeholders, it has the potential of transforming natural resources into workable profit desired by the Government and the citizen.^{xxiii}

One of the primary reasons countries use local Content in the extractive industries is the need to apply resource nationalism. A motivation behind resource nationalism is a public outcry to demand access to maximum wealth benefits realized from the natural resource’s wealth. The Government has an absolute duty to fulfil this demand and ensure benefits last beyond fiscal incentives that natural wealth can bring.

However, it has been suggested government opt for appropriate measures that reflect current global standards and practices to achieve this economic goal in implementing resource nationalism. It has been contended that resource nationalistic experiments or imposing strict local content regulation, especially to developing countries, may risk losing investors.^{xxiv} Furthermore, no country can expect to be an “island unto itself” shut off from and indifferent to the external economic environment in the twenty-first century.^{xxv} The government ought to be keen enough to set functional and appropriate economic measures in place. Considering that economic operators want to nourish now, one day will flourish and want to expand their business operations. They might be exposed to similar positions to other countries, and their government won’t have a say simply because they will be judged by history.

This Author believes that resource nationalism is critical in promoting and ensuring countries endowed with minerals maximize benefits from their wealth. However, in choosing to adopt the resource nationalism approach, countries may conduct a baseline survey on the existing legal setups if they accommodate such developments. As well as consider the presence of different stakeholders such as companies operating in the industry since their legislative approach do affect their business decision. Worth noting, if resource nationalism creates a barrier for the business community to flourish reasonably, the country may not reap as much from their mineral's endowments.

C) Local Content and Corporate Social Responsibility

At its core, Corporate Social Responsibility (CSR) concerns how companies manage their relations with society. Moon suggested that the definition of CSR captures the following features^{xxvi}

- i. Business responsibilities *to* society meaning being accountable;
- ii. Business responsibility *for* society, among others, embrace compensating for negative impacts and contributing to societal welfare;
- iii. Business responsible *conduct* that is the business needs to be operated ethically, responsibly, and sustainably;
- iv. Business responsibility *to* and *for* society in broad terms;
- v. The management by the business of relationships with society.

The concept of CSR also refers to the general belief held by the citizens that modern business has responsibilities to society that extend beyond their obligation to the shareholders or investors in the firm. Furthermore, CSR encompasses the economic, legal, ethical and discretionary or philanthropic expectations that society has of every company at a given point in time.^{xxvii}

In the extractive industry, CSR does not differ from the above definition since it's also linked to expectations from the citizens and government that there must be benefits generated in connection to economic operations in the mining areas. However, it must be differentiated from local content requirements since CSR economic operators are duty-bound by business ethics to add value to the community of mining operations. In Tanzania, the concept of CSR

compliance is an item on its own. The Mining Act compel a mineral holder to prepare and submit a CSR plan jointly agreed by the relevant local government authority or local government authority in consultation with the Minister responsible for finance.^{xxviii} Countries have CSR in their legislation; in Tanzania for instance the law states an extractive company shall submit to the Committee annual reports containing information on local content and CSR.^{xxix}

Therefore, CSR mainly focuses on the economic operators' contributions to the community where their operations occur. Their implementation will rely on what the local community government will require or demand or what the company think it's best to do such activities. For instance, the mining company or service provider may implement education or infrastructure projects in mining areas. When it comes to local content and CSR are not the same because the first advocates for the involvement of nationals in every mining operation that is taking place. While the latter deals on to what extent the companies involved in oil, gas and minerals operations give back to the community where extractions occur.

D) Local Content and Sovereignty over Mineral Resources

History suggests that sovereigns developed a mechanism that ensures control and ownership over available mineral resources in different territories. For instance, sovereignty over mineral resources was developed under Roman law in the legal framework governing the land. In the developed framework, the ownership was vested in the state. Thus, a mineral holder could only enjoy the right of possession over that land, but an obligation to pay royalties surfaced when it comes to extracting minerals.^{xxx}

Other instance includes Britain colonies such as America and Australia, rights to minerals and mine were given by the British Crown. Then Miners were obliged to pay for a portion of minerals extracted. This implies control over mineral resources in British colonies was in the hands of the British government. Therefore, sovereignty over mineral resources helped develop mining law and cemented in the development of the principle of Permanent sovereignty over Natural Resources (PSNR).^{xxxi} The international community in the 1950s set the PSNR principle to address matters of exploitation of natural resources in the world. The principle is enshrined with rights and duties. Such rights include the right to assert the ownership of natural

resources, the right to manage and control the exploitation of natural resources, freedom of a country to exploit its natural resources, and the right to benefit from the exploitation of its natural resources.^{xxxii}

On the side of duties associated with the PSNR include the commitment to practice the right of PSNR in the interest of national development to ensure that the population benefits from their natural resources; the duty to refrain from actions that would likely jeopardize the rights and interests of the people in the exploitation of state over its natural resources; the duty to pay a fair compensation promptly in case of nationalization, expropriation or requisition; the duty to observe international agreements and to accomplish international obligations in good faith in the practice of PSNR mention in a few.^{xxxiii}

Due to the development of the doctrine of PSNR, countries such as Tanzania may have a valid justification for implementing local content in the mining industry. It is significant that when opting for such a path, the country should always consider the general duties associated with that right over natural resources. Doing so will enable resourceful countries to maximize benefits beyond fiscal regime while complying with existing duties and obligations attached to mineral sovereignty over mineral resources.

CONCLUSION

Local content compliance law is one of the tools that rich countries can use to maximize the benefits of their natural wealth. This paper has provided information that complements local content paradigm in the oil, gas and minerals. The author is of the view that as a concept local content had a legitimate existence. The country should employ such policy tools while maintaining existing legal standards and standards for extractive industries.

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