

Natural Resource Contracts: A Practical Guide



LAW

Environmental Law Alliance Worldwide

Natural Resource Contracts: A Practical Guide

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Acknowledgments

Natural Resource Contracts: A Practical Guide was authored by Liz Mitchell, a Staff Attorney at the Environmental Law Alliance Worldwide (ELAW). ELAW helps communities speak out for clean air, clean water, and a healthy planet. We are a global alliance of attorneys, scientists, and other advocates collaborating across borders to promote grassroots efforts to build a sustainable, just future. ELAW has global reach and supports public interest environmental lawyers in countries where assistance is most needed and can achieve the greatest impact. Through the ELAW network, advocates around the world provide legal and scientific support to their colleagues and build global capacity to protect the environment and advance environmental justice through law.

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Introduction

Why has ELAW written a guide to natural resource contracts?

In response to rapidly growing global demand for natural resources and rising prices for agricultural commodities, many private companies are looking for untapped supplies of oil and minerals or large swaths of agricultural land to exploit. Resource extraction and large-scale agriculture projects are primarily governed by long-term contracts between natural resource companies and the governments of the countries in which they seek to operate - known as “host countries.” The contracts are almost always negotiated without involving the public or lawmakers.

Through the advocacy efforts of transparency and anti-corruption organizations, a growing number of governments are disclosing natural resource contracts to the public. As these contracts come to light, citizens are finally gaining the opportunity to understand how their resources are being managed and at what cost. The implications of natural resource contracts can be significant, not just in terms of revenue for the host country, but also in relation to land rights, access to water and housing, food security, and public health.

Over the last decade, ELAW has worked closely with public-interest advocates around the world to review dozens of natural resource contracts. From our perspective, it is apparent that host countries are not doing enough to protect communities and maximize benefits that can be derived from resource extraction and large-scale land leases. Time after time, host governments waive social and environmental protections, neglect opportunities to bring education, technical know-how, and employment opportunities to citizens, and forego vital sources of tax revenue.

Contract transparency is changing that dynamic. Citizens and civil society organizations are demanding accountability when their governments fail to negotiate

fair deals or neglect to enforce contract terms. Access to natural resource contracts allows local communities to monitor whether resource extraction companies are fulfilling their commitments and acting sustainably.

ELAW published this Guide to help public-interest advocates understand natural resource contracts. These agreements are complex and difficult to read, requiring knowledge of many areas of law and policy. Contracts vary greatly among countries and industries, and it is virtually impossible to identify “best practices” because what might be beneficial in one country may not work well in another. For that reason, it can be difficult to tell whether a particular contract represents a good deal for a host country and its citizens. The goal of this Guide is to explain common topics that are addressed in natural resource contracts and to provide suggestions for improving contracts that are vague or unfavorable to host countries. The Guide also includes references to additional resources that will be useful for advocates who want to learn more about particular topics and issues.

In most cases, a natural resource contract does not include all of the terms that apply to a particular project. The contract must be read in conjunction with applicable national and international laws that govern tax and financial issues, resource exploitation (e.g., mining, forestry, petroleum), land tenure, environmental protection, social and human rights obligations, and contracts. In many countries, there will also be customary laws to consider - particularly those governing land rights. Issues not addressed in a natural resource contract may be regulated in a host country’s laws and vice versa.

Drafting, interpreting, and negotiating natural resource contracts requires considerable expertise. This Guide is not a substitute for, nor is it intended to provide, professional legal advice.

A note on terminology:

There are many titles used to identify the contracts that govern exploitation of natural resources and long-term agricultural land use, including: “investment agreement,” “concession contract,” “production sharing agreement,” “stability agreement,” and “lease agreement.” For the purposes of this Guide, we chose to use the broad term “natural resource contract.” What these documents all have in common is that they regulate the activities of an entity (sometimes called an “investor”) that is proposing to extract a natural resource or use a large tract of land. The entity may be a private company, a consortium of companies, and might even include state-owned (domestic or foreign) companies. We refer to the investor in this Guide as “resource company,” recognizing this is not a perfect or all-encompassing term.

A note on contract excerpts:

Throughout this Guide, we include excerpts from actual natural resource contracts to illustrate certain points in the text. We have edited these excerpts for length and clarity, but have made all efforts to maintain the meaning expressed in the original contract. A list of the contracts that have been excerpted or referenced is provided in the bibliography.

Contract Negotiation

Before delving into what natural resource contracts say, it is appropriate to include a brief discussion of contract negotiation. Negotiations play a significant role in the content and quality of natural resource contracts. Many of the problems with contracts that are identified in this Guide could be avoided through better negotiation at the outset.

There is tremendous secrecy surrounding contract negotiations. Natural resource contracts are typically discussed and drafted by teams representing the host country and the resource company. Without close public and civil society oversight, the process is susceptible to mismanagement and corruption. Add to this the imbalance of power in situations when host country negotiating teams, particularly in developing countries, lack the technical capacity, experience, and funding to participate effectively. There may be power struggles within the host country itself among ministries that are vying for control of a particular project. In countries with weak governance and inadequate laws, government negotiators wield considerable discretion to set terms and conditions that are far from optimal. Any one of these factors is enough to contribute to poorly drafted contracts that will generate long-term consequences for the host country and its citizens.

Botswana is held out as an example of a developing country that successfully negotiated mining agreements with several foreign resource companies. The government of Botswana achieved this by: deploying a well-qualified and interdisciplinary negotiating team; maintaining a consistent roster of negotiators through multiple contract negotiations to build greater capacity and expertise; engaging with outside experts when necessary; and taking the lead in drafting documents.¹ Similarly, the government of Cameroon enlisted support when it undertook negotiations with an Australian mining company over a large-scale iron ore mining project, as did the government of Liberia during renegotiation of two concessions governing mining and agricultural production.

The governments of resource-rich countries have a responsibility to be knowledgeable and well-prepared in contract negotiations over natural resource extraction and long-term land leases - not just for the sake of securing a good financial deal, but to promote high standards in labor and human rights, environmental protection, health, safety, transparency, and fiscal management. It is incumbent on public-interest advocates to demand that their governments assemble competent and experienced contract negotiating teams and, if internal capacity is limited, to seek outside guidance and support. Some countries have moved to a model contract system and codified key regulatory and fiscal provisions in law, which narrows the scope of issues that must be negotiated for a particular project. There is also an important role for lawmakers to play in reviewing and ratifying proposed natural resource contracts. All of these elements contribute to a more robust and transparent process for managing natural resources on a commercial scale.

Contract Term

A natural resource contract will state how long the agreement is valid, which is known as the “term.” Contract terms can range from a few years to several decades from the date the agreement becomes effective.

Determining the term of a contract can be complicated and requires cross-referencing with other parts of the agreement. A good place to start is by identifying the initial term (usually described near the beginning of the contract) and the effective date. The effective date may be explained in the definitions section of the contract. Some contracts take effect on the date they are signed by the host country and natural resource company, while others do not take effect until certain conditions have been met, such as legislative approval or acquisition of permits or land leases.

The contract term will be further modified by provisions addressing renewal or extension. A contract might require the resource company to meet certain investment benchmarks or work obligations during the course of a project. If the company fails to meet these deadlines, it might trigger provisions that automatically terminate the agreement or allow the host country to take over implementation of the project. Alternatively, there may be a provision allowing the resource company and host country to extend the contract for a period of years, provided certain goals are achieved.

With mining and petroleum projects, the contract term might be divided into consecutive phases reflecting the anticipated lifespan of the project, such as “exploration” (or “prospecting”), “appraisal,” “production,” and “decommissioning” (or “abandonment”). Typically, the contract will assign a relatively short timeline to the early phases of a project in order to discourage the resource company from sitting on its exploration rights. As the project progresses, the company may be required to seek permission from regulators and demonstrate that it has met financial and technical benchmarks before moving on to the next phase of development. Social and environmental projects, such as community infrastructure or health programs, may be incorporated into those benchmarks.

LIBERIA - OIL PALM PLANTATION

“The term of this Agreement . . . shall commence on the Effective Date and continue for a period of sixty five (65) years unless otherwise extended . . . or sooner terminated in accordance with the other provisions of this Agreement.”

Contract terms are not always straightforward. Be sure to check provisions governing contract extensions and termination.

AFGHANISTAN - GOLD ORE MINING

“Effective Date’ of this Contract is the date that this Contract is signed by both parties.”

Contracts may take effect upon signing or after later events occur.

LIBERIA - OIL PALM PLANTATION

“Effective Date - The later of (i) the date on which this Agreement is signed by all of the Parties, attested to by the Minister of Justice of Liberia, ratified by the Liberian legislature, signed by the President and becomes Law in accordance with the Laws of the Republic of Liberia and (ii) the date on which Investor enters into one or more leases, each with a term of at least 65 years, of approximately one hundred hectares (100) of land suitable to the Investor at each of the ports of Greenville and Harper . . . for its operations . . .”

It will be helpful to become familiar with the circumstances under which the host country or the company can terminate the agreement before the contract term has expired. This will usually be described in a provision called “termination” located near the end of the agreement in which the parties reserve the right to bring the contract to an end if certain events occur. From the host country’s perspective, the types of incidents that justify termination include material violations of the contract, a declaration of bankruptcy or insolvency, or a cessation of activities in the contract area for a certain period of time. The contract will describe these conditions, as well as the termination procedure.

When reviewing a natural resource contract, make note of specific deadlines or obligations imposed on the natural resource company. If the economic prospects of a project take a turn for the worse, a company may decide to curtail its activities, causing it to miss important benchmarks. As mentioned above, this could be cause for termination of the contract. Although citizens rarely have the right to enforce contract terms, these faults can be brought to the attention of regulators or the media, which may prompt the host country to terminate the agreement or require the resource company to relinquish portions of the contract area.

GUINEA - IRON ORE MINING

“The Company undertakes to start mining operations at the latest by May 31, 2012. In the event the Company is unable to comply with the deadline . . . it must inform the Government and provide the necessary justifications . . . In the case of failure to start the operations of the [mine] within the aforementioned period that has possibly been extended, the Government may revoke the Mining Concession in accordance with the provisions of the Mining Code.”

BELIZE - PETROLEUM DEVELOPMENT

“The Contractor is authorized to conduct exploration operations during an exploration period which shall be comprised of (i) an initial exploration period of two (2) contract years . . . and (ii) subject to the conditions hereinafter provided, three (3) successive renewal periods . . . of two (2) years each to the initial exploration period. Such renewal periods shall be granted to the Contractor . . . subject to the Contractor having fulfilled its obligations hereunder for the then current period, including the relinquishment provisions . . . and having submitted with such application a work programme and work programme budget for the period of renewal . . .”

Check to see if contract renewal is contingent on the resource company completing work obligations or making certain expenditures. These conditions can be monitored.

AFGHANISTAN - GOLD ORE MINING

“Should [the Company] cease exploration activities related to the approved Exploration Plan for a period of longer than six (6) consecutive months without the approval and agreement of the Ministry of Mines (MoM), then the MoM may consider the Exploration License null and void and the exploration right will revert back to the government of Afghanistan.”

Inactivity may give rise to contract termination or loss of rights.

Host countries will include conditions in contracts that discourage resource companies from sitting on their rights.

Contract Area

Natural resource contracts allow companies to acquire rights over large tracts of land for extended periods of time. For that reason, it is essential to understand the location of the contract area boundaries in order to anticipate whether people living in or near the project area may suffer adverse impacts or be displaced. Note that the boundaries may be described or identified in an appendix or attachment to the contract; however, the appendix should at least be mentioned or identified in the main body of the agreement.

Agreements that define the contract area boundaries using geographic coordinates provide great certainty and specificity. A significant drawback, however, is that it can be difficult for community members to translate those coordinates into a clear understanding of boundary locations on the ground. With technical assistance and freely available software, these coordinates can be plotted on a map. Or, it may be possible to file a public information request with the appropriate ministry to access boundary maps that have been prepared using the coordinates.

An alternative method of identifying the contract area is through a narrative description of the geographic features that mark key points along the boundary. Using a narrative description is more accessible and understandable to community members, but may not provide sufficient specificity. A resource company may take advantage of vague boundary lines to exploit resources adjacent to its contract area.

The least desirable option is a contract that does not define the project area at all or only provides a general location where activities may occur. This method is typically used when the extent or quality of a resource has yet to be determined. The contract may call for the company to prepare a feasibility study to determine the best location for its project and facilities and submit a more detailed boundary description to regulators. This approach places a considerable amount of discretion in the hands of private companies to choose lands where they will operate and typically excludes the host country and local communities from participating in decisionmaking. If communities are unhappy with the

SOUTH SUDAN - ALL-INCLUSIVE LAND LEASE

“The Cooperative hereby agrees to lease to the Company one more parcels of forested land within the Cooperative Territory with an aggregate area of no less than 600,000 hectares (with further extension up to 1,000,000 hectares) . . . Upon completion of [a] land survey and comparison, the Cooperative and the Company shall, in good faith, determine the actual parcel or parcels within the Cooperative Territory to be leased by the Cooperative to the Company[.]”

This contract creates considerable uncertainty about the location of proposed large scale agriculture and biofuel production because the contract area will not be identified until later in time and without public involvement.

TIMOR-LESTE & AUSTRALIA - PETROLEUM DEVELOPMENT

“The Contractor shall relinquish: (i) at the end of the third (3rd) Contract Year, not less than twenty five (25) percent of the Sub-Blocks in the original Contract Area; and (ii) at the end of the fifth (5th) Contract Year, not less than a further twenty five (25) percent of the Sub-Blocks in the Contract Area.

At the end of any Contract Year . . . the Contractor may relinquish some or all[] of the Sub-Blocks in the Contract Area. Any Sub-Blocks so relinquished will be credited against the next relinquishment obligation of the Contractor . . .”

Some contracts require parts of the contract area to be turned back “relinquished” to the host country if resource discoveries are not made or if the company has remained idle. Relinquishment will affect the boundaries of the contract area.

location of a proposed project, the host government will have little incentive to intervene on their behalf because the contract has already been signed.

In some instances, the contract area does not remain static throughout the duration of a project. The agreement may require the resource company to periodically hand back, or “relinquish,” portions of the contract area that are unsuitable for further development or that the company will not be using. Relinquishment requirements are primarily seen in petroleum development contracts and their purpose is to encourage resource companies to fully and continuously explore a contract area, rather than sitting on their rights. Companies are usually permitted to voluntarily relinquish all or part of their contract area, as well. If relinquishment is addressed in a resource contract, the provisions will include a schedule identifying when and how much of a contract area must be turned back to the host country. After relinquishment occurs, the land may be made available to another company for exploration and possible development or for other purposes, including community use.

Case Study: Successful Contract Monitoring in Belize

Civil society organizations in Belize are keeping a close watch on offshore oil development contracts issued by the Belizean government. Belize’s petroleum law and each petroleum development contract require oil companies to relinquish part of the concession every two years unless an oil discovery is made. In August 2012, Oceana Belize learned that the Ministry of Energy secretly waived the relinquishment requirement in 2009 for one particular company that was idly sitting on its exploration rights. Oceana Belize notified the media and a well-orchestrated campaign widely exposed the Ministry’s missteps. With mounting public pressure, the Ministry was forced to follow the law and requested the company to voluntarily relinquish part of its concession block. The oil company relinquished over a third of its concession area back to the government, including areas that Oceana Belize and other organizations demanded to be excluded from offshore oil exploration. Thanks to their vigilance, the iconic Great Blue Hole in Lighthouse Reef Atoll and Belize’s newest marine reserve, Turneffe Atoll are now safe from petroleum exploration. Both areas are part of Belize’s treasured and internationally renowned Barrier Reef Reserve.

Public Access to Contract Area

In many instances, the boundaries of a natural resource contract area will overlap with land that local communities use to gather food, obtain drinking water, graze and water livestock, hunt and trap, or other essential uses. A contract area also may contain roads or trails that link communities or provide direct routes to commercial areas. Poorly planned resource extraction and large-scale agriculture projects pose barriers to people’s movement and access to resources necessary to sustain their livelihoods. (Impacts to land rights are discussed in more detail in the next section of the Guide).

Some contracts will contain provisions detailing whether members of the public may 1) enter or cross the contract area; 2) collect food or other materials in the contract area; 3) use land in the contract area for pasturing livestock or for agriculture; or 4) access water sources in the contract area. If members of the public are permitted to enter the contract area, take note of any procedures the resource company must follow if it intends to restrict or curtail this right. However, many contracts will allow the resource company to erect barriers and close off public access without prior notice or justification.

Public access is one of many issues addressed in natural resource contracts that can benefit from public participation during project planning and contract negotiations. Through consultation with local communities, the resource company and government officials will gain greater understanding of the impacts a particular project will have on community access to resources in and around the project area. There may be opportunities to make modifications to the proposed contract boundary or project footprint to maintain public access to these resources. Properly negotiated contracts will require a natural resource company to provide ample public notice and to consult with affected communities prior to implementing access restrictions or closures in the contract area.

LIBERIA - OIL PALM PLANTATION

“All roads including Farm Roads and trails across the Concession Area that have been and continue to be used immemorially by the population, shall remain open to free use by the public for commercial and public purposes as long as such use does not unreasonably interfere with Investor Activities or unless by mutual agreement between Investor and Government (e.g., to reroute these roads)[.]”

This contract does not provide very clear guidance as to when roads and trails in the contract area may be closed.

LIBERIA - OIL PALM PLANTATION

“Investor shall permit independent farming activities within areas of the Concession Area which are not suitable for Production, provided that such independent farmers (i) limit farming activities to non-commercial food cultivation, (ii) live within the Concession Area or had lived within the Concession Area before resettlement . . . , and (iii) seek the permission of Investor prior to commencing such farming activities. . . . Determinations of which areas of the Concession Area are not suitable for production shall be within the discretion of Investor but may be reviewed and disputed by Government if such determinations are not reasonable under the circumstances.”

Although portions of the contract area may be made available for community members to farm, there are a number of conditions that will make small-scale farming difficult to carry out.

Land Rights

Host countries frequently agree to give resource companies long-term rights over vast tracts of land and provide guarantees that the land will be free from third-party encumbrances. In many cases, however, what may be considered “public” land in the eyes of the host country government is in fact land that is owned or occupied by local communities. These communities risk losing their land rights without notice, consultation (including the opportunity to provide consent), and compensation.

Of the many natural resource contracts ELAW has reviewed, most do not address land rights adequately. This shortcoming is due in part to land laws that do not protect customary or informal land rights. Most natural resource contracts compound the problem by failing to recognize the full scope of land rights in the host country or by presuming that such rights can be quickly extinguished. International law plays a role, particularly with regard to land rights held by indigenous peoples, but host country governments often show limited recognition or respect for these rights.

When reviewing contract provisions concerning land rights, it is helpful to organize information by the following three broad topics: 1) what types of land rights are referenced in the agreement; 2) what are the procedures for terminating land ownership and use rights; and 3) what compensation or mitigation measures are proposed. Also look at the host country’s constitution and land laws to see what protections and procedures are afforded to land owners and occupiers.

Natural resource contracts frequently fail to protect the full range of land rights held by individuals and communities. Carefully compare the land rights discussed in the contract with those that are legally recognized and customarily practiced in the host country. It is common for contracts to confine protections to titled land rights, but customary land rights in some jurisdictions are protected by law. Furthermore, the concept of land rights encompasses far more than land ownership. Some individuals enjoy the right or use or occupy plots of land they do not own, whether it is for farming, food collection, or access to water. In areas with nomadic or pastoral communities, land may appear to be vacant but in reality is part of a network of parcels used seasonally.

If particular land rights are not addressed in a natural resource contract all is not lost. Look to national and international laws for provisions that may be used to protect these rights and support efforts to gain more control over land allocation. For example, human rights tribunals in Latin America and Africa have declared that collective and customary land rights held by indigenous communities are fully protected property rights that cannot be readily extinguished by state governments.²

ETHIOPIA - AGRICULTURE LAND LEASE

“The lessor shall be obliged to deliver and hand over the vacant possession of leased land free of impediments to the lessee within thirty (30) days from execution of this Land Lease Agreement.”

This contract puts considerable pressure on the host country government to resolve land rights claims within a very short period of time.

GHANA - GOLD MINING

“The owner of any private land within the Contract Area that is subject to a mineral right granted to [the mining companies], and any Person who lawfully occupies any land within the Contract Area, shall be entitled to receive compensation or other remedies as provided in the Law.”

Private landowners and lawful occupiers are recognized in this contract, but there are no specific protections for people who have customarily used land in the contract area.

In terms of procedures to terminate land ownership rights, a contract may call for compulsory acquisition by the host country or, alternatively, require acquisition to be negotiated with landowners on a case-by-case basis. With compulsory acquisition, the host country's constitution and land laws will usually provide a clear procedure and compensation scheme. In addition, the host country is usually required to demonstrate that the land is being acquired for a public purpose.³ There are several drawbacks to compulsory acquisition, however. Landowners do not have any right to veto or withhold consent to the acquisition. Furthermore, the host country's expropriation laws may not recognize customary ownership as compensable or may not provide sufficient financial relief to enable land rights holders to fully restore their livelihoods. Use and occupancy rights, unless formally recognized as a property right, are at greater risk of being extinguished without any procedural protections or compensation. For these reasons, it is generally recognized that negotiated acquisition and settlement of land rights is a more preferable approach.

When negotiated acquisition is anticipated in a natural resource contract, host countries should establish mechanisms to help landowners with the process. There is a role for public-interest advocates to assist local communities and ensure that the negotiation is fair. Landowners benefit from knowing the value of their land and whether it could provide other economic or environmental gains to their community. It is also advantageous for landowners to understand how much they should be compensated and what the true costs of resettlement entail.

Particular attention is warranted when national laws or contract language permits the host country government to authorize a resource company to occupy and use lands. In such cases, ownership rights are not formally extinguished through compulsory acquisition and little to no compensation is paid to landowners because the resource company is considered to be temporarily occupying land. As explained earlier in this Guide, however, natural resource contract terms can last many decades and long-term occupancy by resource companies has the same impact on landowners as permanent dispossession.

A natural resource contract may propose measures to mitigate impacts to land rights holders or provide compensation if these rights are diminished, but not fully extinguished. Take note of provisions that place obligations on the resource company to protect land rights or resources that local communities rely on. It may be beneficial for communities to document their land use and resource needs in case a dispute arises with the company.

GHANA - GOLD MINING

"If [the mining companies] reasonably require[] private land outside the Contract Area for Operations, they will endeavor to enter upon and utilize such land by direct agreement with the owner, and such land shall be deemed to be part of the Contract Area during any period of its occupancy and use by [the mining companies.]"

Improving Contracts: Land Rights

Natural resource contracts must recognize and incorporate measures to effectively implement the principle of free, prior and informed consent in relation to actions that will affect community lands, territories, and natural resources.

Contracts should include firm commitments to minimize involuntary displacement and resettlement caused by resource exploitation or long-term use of lands. If individuals or communities are resettled, and the process involves negotiated settlement, resource companies must agree to improve or at least restore the livelihoods of affected people to pre-project levels, through compensation at full replacement cost and additional assistance as may be required.

If national laws do not provide clear and effective procedures for individuals and communities to seek relief in instances where land is improperly acquired or a company's activities infringe on land ownership and occupancy rights, it may be appropriate to include a grievance mechanism in the contract.

If domestic laws are lacking or provide incomplete protection for land rights, a contract may reference IFC Performance Standards (Land Acquisition and Involuntary Resettlement; Indigenous Peoples) or other similar international standards.⁴

Resource Company Activities

A natural resource contract will include a section that describes the activities a company is allowed to undertake on land within (and possibly outside) the contract area boundaries. Even though the contract will primarily focus on implementation of a particular project, such as constructing an open-pit mine or establishing an oil palm plantation, it may nevertheless allow the resource company to exploit other resources or conduct activities unrelated to the main project. This information will either be set out in a section titled “grant of rights” or “rights of holder,” or described in the definitions section of the contract in a term such as “investment activities.”

Carefully review all of the activities the contract will permit the resource company to do. It is sometimes surprising to learn that a company has permission to engage in side projects. These activities might create direct competition with local businesses or small-scale producers in surrounding communities. For example, a contract that allows a mining company to grow food to feed employees reduces economic opportunities for local farmers who would otherwise have a steady market for their crops. Similarly, if a contract permits a biofuel company to clear forest land for large-scale agricultural production and also process and sell the timber, it gains an unfair advantage over local timber processors that would benefit from accessing this resource.

If carefully negotiated, natural resource contracts create opportunities for local businesses and small-scale farms to create economic links with a large-scale project. Additional discussion of this topic occurs in “Local Content.” Every effort should be made to safeguard and encourage local economic activities.

LIBERIA - OIL PALM PLANTATION

The Concession Agreement for development of an oil palm plantation and export of oil palm products defines “investor activities” to include food and other agricultural production, and sales of timber, stones, gravel, sand, and other construction-grade materials from the contract area.

Note the range of resource company activities.

SOUTH SUDAN - ALL-INCLUSIVE LAND LEASE

“The Cooperative hereby agrees that the Company shall have the right to engage in the following activities on the Leased Land . . . development, production and/or exploitation of timber/forestry resources[;]. . . the planting and harvesting of megafolia-paulownia, palm oil trees and other hardwood trees and the development of wood-based industries; and . . . [a]griculture, including the cultivation of the jetropha plant and palm oil trees (and the exploitation of any resulting carbon credits).

* * *

The Cooperative acknowledges and agrees that the Company may undertake any other activity permitted by the laws of Southern Sudan on the Leased Land . . . [including] petroleum, natural gas and other hydrocarbon resources . . . and other minerals, and may seek to engage in power generation activities on the Leased Land.”

This contract is unusual in the breadth of activities allowed, from oil palm and biofuel production, to forestry and logging, to petroleum development. The resource company has complete discretion to decide how it will use leased land.

Use of Natural Resources in Contract Area

Activities like oil and gas extraction, mining, and large-scale agriculture require extraordinary quantities of raw materials during construction and operation. It can be expected that a resource company will draw heavily on resources within and even outside of a contract area. Unfortunately, host countries are often so focused on the potential revenue to be gained from exploiting a particular natural resource that they are all too willing to give companies free and unfettered use of other valuable and essential resources, such as water, land, and construction-grade minerals (e.g., sand, rock). In many cases, these are the same resources that sustain local communities.

Natural resource contracts may contain language that sounds as though it will protect supplies of natural resources, particularly those that local communities depend on. Yet these protections are often vaguely worded - using phrases such as “shall not materially interfere” or “shall maintain an adequate supply” - which are difficult to interpret and enforce. Some contracts protect community access to natural resources but only to meet the level of need that existed at the time the contract took effect, without accounting for future population growth. Nevertheless, take note of any language that requires a company to limit its use of resources. It can be advantageous for communities in and around the project area to document their own resource use and needs in the event that a dispute arises.

Most contracts in the public domain do not address this issue well. If a resource company will be using raw materials for construction and operation, it is recommended that the contract include clear commitments that the resource company will obtain all necessary permits to extract and use these materials (including environmental impact assessment) and pay the same costs or royalties as would be expected of any other user. Sometimes these requirements are waived. If permitting requirements are not waived in the contract, it is worth confirming whether a resource company has obtained them. Contracts should contain clear and specific limits on resource use. For example, a contract may call for a company to maintain a specific minimum flow of water in waterways, designate a maximum volume of rock that can be freely quarried, or set aside certain parcels of land that cannot be logged or cleared.

SIERRA LEONE - OIL PALM PLANTATION

[The Government] agrees to enter into a water rights agreement with [the Company] and [the Company] shall be charged at a fixed rate of 3 Leone per cubic metre of water extracted from rivers and other watercourses. There will be no restriction on the volume of water extracted by [the Company] from rivers, other watercourses, wells and boreholes.

Although the resource company is paying for its use of water, it has no incentive to use it sustainably or to protect water sources used by local communities.

LIBERIA - IRON ORE MINING

The Company shall have the right to access (including by means of extraction) such water supplies as are reasonably required by it for the purposes of carrying out its Operations subject to the payment by the Company of any charges required by Applicable Law for the use of water and provided that such access by the Company does not affect the water supplies used by the surrounding population or, to the extent it does so affect water supplies, the Company provides an alternative source of water supply to the affected population.

The mining company does not have unlimited access to water; however, it may be difficult for local communities to prove that their water sources are being diminished or to push the company to provide alternative sources. A grievance mechanism can be useful for disputes like this.

Infrastructure: Electricity/Railways/Highways/Ports

Resource companies developing large-scale projects require access to infrastructure, communication, and electricity services. If such services already exist in the project area, a natural resource contract may address the resource company's right to access or use these services and at what cost. Pay attention to provisions that give the company an unfair advantage by charging lower rates (or no cost) for using publicly-funded infrastructure. The contract should not put the resource company's needs over those of citizens and local businesses, particularly if there is a risk that there might be shortages of electricity or other essential services.

ZAMBIA - COPPER ORE MINING

"[The Government] hereby exempts the Company for a period of fifteen (15) years from the date hereof from liability to pay the Excise Duty on Power applicable to the Company's purchases of electricity in relation to the operation of the Facilities during such period."

Host countries should not waive the costs of providing utility services, particularly when such services are in short supply. Mining and ore processing use a considerable amount of electricity.

In the course of negotiations, a resource company may agree to build particular infrastructure facilities, such as roads, power transmission lines, rail lines, and ports. These facilities might be necessary to carry out the project or may be offered as a benefit to local communities (or both).

A good contract will outline a clear schedule for undertaking and completing infrastructure projects, and require the resource company to follow all permitting and environmental review requirements. The resource company can more easily be held accountable if the contract specifies when particular infrastructure facilities must be completed. Surprisingly, many contracts neglect to include deadlines. In addition, the contract should clarify which party is responsible for maintaining and repairing the facility once it has been completed. If the host country will be responsible for maintenance and repair, considerations must be made as to whether there are funds and adequate capacity to do so.

ETHIOPIA - AGRICULTURE LAND LEASE

This contract lacks a plan or schedule for infrastructure development, leaving all decisions in the resource company's hands.

"The lessee has the right to . . . [b]uild infrastructure such as dams, water boreholes, power houses, irrigation system, roads, bridges, offices, residential buildings, fuel/power supply stations/out lets[,] health/Hospitals/Dispensaries, [and] educational facilities, at the discretion of the Lessee upon consultation and submission of permit request with concerned offices . . . whenever it deems so

It is also important to review and understand whether members of the public and local businesses will be able to use company-constructed infrastructure facilities (other than those specifically designated for the benefit of the public). For larger facilities, such as railways and ports, the contract may allow a company to charge a fee for third-party access and use.

Human Rights

Although natural resource contracts are recognized as important instruments through which host countries and resource companies can influence a project's impact on human rights,⁵ most contracts do a poor job of addressing this topic.

A well-drafted contract will not only include commitments to abide by national human rights laws and any international covenants that the host country is a party to, but will also include measures requiring the parties to fully evaluate and develop a plan to mitigate impacts to fundamental rights.

If the International Finance Corporation (IFC) or another international finance institution is funding the project, the resource company must follow the lender's performance standards or policies for managing and mitigating social impacts of projects. These standards and policies can generally be accessed through the website of the lending institution. There may be opportunities to seek review of a project through a bank's accountability mechanism (when available) if standards or policies have been violated.

Even if a lender is not involved with a project, social performance standards may nevertheless be referenced in a natural resource contract - particularly if national laws do not provide adequate social safeguards. Examples of such standards include the World Bank Safeguard Policies and the IFC Performance Standards on Environmental and Social Sustainability.

International Bar Association - Model Mining Development Agreement

- (a) The Parties each commit themselves to the protection and promotion of the human rights of all individuals affected by the Project, as those rights are articulated in the United Nations' 1948 Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social, and Cultural Rights, and Applicable Law.
- (b) In all dealings between Company security departments and the police, military, or other security organs of the State, the Parties pledge themselves to comply with Applicable Law and to respect the guidance set forth in the Voluntary Principles on Security and Human Rights.
- (c) The Company shall ensure that its operational policies reflect the responsibility to respect human rights and that the policies have the objectives of preventing, mitigating and remediating any potential or actual negative human rights impacts from Mining Operations.
- (d) A process to procure an independent assessment of the potential for human rights impacts from the presence and activities of the Project, and how the Company's policies, procedures, and practices affect the human rights of the population in the area of the Project, such process will be guided by the tenets of transparency, independence, and inclusivity, as defined by international standards.

An issue that deserves special attention is the matter of physical security (sometimes referred to as “asset protection”) in a project area. As the UN Special Representative on Business and Human Rights, Professor John Ruggie, observed:

Some of the most serious human rights abuses in the context of business activity have involved security personnel charged with protecting business installations or operations. These security personnel could be local police, armed forces or private security personnel. Episodes of violence, especially when they are not followed by appropriate investigation, prosecution and remedy for those who have suffered from negative human rights impacts, pose legal, reputational and financial risks for States and business investors.⁶

Most security provisions are worded very broadly, like this one.

GHANA - GOLD ORE MINING

“[The companies] shall have the right, directly or under contract with other Persons to establish and maintain their own asset protection service for the purpose of maintaining Law, order and security.”

Typically, security provisions in natural resource contracts are vaguely worded and simply authorize the resource company to assemble and maintain private security forces at its own discretion. When reviewing a contract, pay special attention to any restrictions or requirements placed on security forces. Some multinational companies have adopted policies addressing their implementation of the Voluntary Principles on Security and Human Rights. It is helpful to cross-reference national laws to determine whether private security forces may carry weapons or detain citizens. It is important for community members to understand their rights should they interact with or be detained by a member of a private security force.

If a resource company is permitted to use security forces provided by the host country, such as local police or military, a well-drafted contract will clearly identify whether the resource company or host country is responsible for human rights abuses that are committed when these forces act on behalf of the resource company. Contracts should not waive the public’s right to seek redress for violations of domestic laws committed by private or government-provided security forces.

LIBERIA - OIL PALM PLANTATION

“Each member of the Concession Protection Department shall be vetted by the Ministry of Justice as to his/her suitability and background prior to undergoing a training program to be approved by the Ministry of Justice but conducted by Investor. Those members of the Concession Protection Department submitted by Investor to Government’s police and law enforcement authorities as certified to have been specially trained and qualified and attested by the Ministry of Justice as possessing the requisite requirements, shall have enforcement powers within the Concession Area, always being subject to Law.”

In contrast, this contract imposes more scrutiny over security forces and requires training.

Environmental Protection

Environmental protection typically gets very little attention in natural resource contracts. Representatives from environmental ministries or agencies are usually not part of contract negotiating teams and may not even be aware that a large-scale natural resource extraction project or agricultural land lease is being considered.

If environmental protection is addressed, it is usually through standardized language in which the resource company agrees to abide by national environmental laws and pollution standards and/or agrees to conduct its activities in accordance with “international industry standards” or “best industry practice” for a particular sector.

When a contract includes references to “international industry standards” or “best industry practice” for protecting the environment, a resource company has discretion to choose the most lenient standards (if standards even exist). In many sectors, there are no agreed-upon sets of environmental protection requirements or the requirements are vague and aspirational. In the petroleum industry alone there are multiple sets of standards - including those published by the American Petroleum Institute (API), the International Association of Oil & Gas Producers (OGP), the International Organization for Standards (ISO), and the Australian Petroleum Production & Exploration Association (APPEA). Even if a single set of industry standards were to exist, the host country would not be able to enforce them because they usually contain flexible and non-binding language.

The contract might even state that the relevant industry standards are those applied under similar conditions and circumstances to those found in the host country. Many multi-national companies prefer this type of requirement because their conduct in the host country cannot be held in comparison to their operations in countries where environmental standards are more strict. Contracts using this language tend to lower the bar for environmental protection.

GUINEA - COPPER ORE MINING

“The Company undertakes to carry out its mining operations in accordance with accepted engineering practice, under safe conditions, and in compliance with international standards and practices that are usual in the mining industry.”

Reference to “international industry standards” allows resource companies to choose the most lenient environmental standards.

LIBERIA - RUBBER PLANTATION & PRODUCTION

“[The Company] shall take reasonable measures to ensure that Production does not cause unreasonable risks to public health or unreasonable damage to the environment. Unless [the Company] demonstrates that a particular measure is unreasonable, it shall employ measures as protective as those employed by persons in Liberia and elsewhere engaged in the production and processing of Rubber on a basis similar to Production under this Agreement.”

This type of standard lowers the bar for environmental protection.

AZERBAIJAN - PETROLEUM DEVELOPMENT

“Contractor shall comply with present and future Azerbaijani laws or regulations of general applicability with respect to public health, safety and protection and restoration of the environment, to the extent that such laws and regulations are no more stringent than the then current international Petroleum industry standards and practices being at the date of execution of this Contract those shown in [the Appendix], with which Contractor shall comply.”

This is another example of contract language that undermines environmental protection. The oil company is free to ignore any national environmental law or regulations that are more stringent than international industry standards.

When a host country has enacted comprehensive environmental laws and regulatory standards, it is preferable that contracts bind natural resource companies to these requirements. These will be the standards most familiar to host country regulators. However, there may be gaps in domestic legislation, particularly if recent resource discoveries have been made. In such cases, external standards can be used to fill the gap or supplement weak domestic laws, but

the contract should specify which set of standards takes precedence in the event of a conflict. When reviewing a contract that references domestic law and international industry standards, make sure that the contract does not allow the resource company to ignore domestic requirements that are more stringent than international industry standards.

Environmental Impact Assessment

Environmental impact assessment (EIA) is a key component of project planning. Review the natural resource contract carefully to ensure it does not waive or eliminate EIA requirements included in domestic laws. If there is no domestic EIA law, or the law is inadequate, the contract may refer to procedures established by the International Finance Corporation (IFC) or World Bank as a backstop.

A difficult problem arises with the timing of EIA procedures and execution of natural resource contracts. In most cases, the EIA is prepared after the contract is signed and the host country has made a binding commitment to the project. This means that the EIA process is rendered meaningless except to the extent that it generates environmental mitigation and management plans to buffer the anticipated impacts of the proposed project or activity. The contract may even go so far as to prescribe shorter timelines for officials to review EIAs and issue decisions than would normally be permitted under the domestic EIA law.

LIBERIA - OIL PALM PLANTATION

“Investor shall prepare and deliver to Government for approval . . . an Environmental Impact Assessment Study Report and an Environmental Management Plan complying with Law . . . [The Report and Plan must be approved by the Environmental Protection Agency of Liberia (EPA)] prior to undertaking, or causing to be undertaken, any clearing, construction, or any other physical disturbance of the land or environment. Investor shall, from time to time and at the request of EPA, prepare and deliver additional studies and/or an updated and/or amended Environmental Management Plan. The EPA shall be conclusively deemed to have approved the Environmental Impact Assessment Study Report and Environmental Management Plan (or any updates or amendments) if, within 60 days of submission. . . the EPA has not indicated a decision to withhold approval by Notice in the manner provided in this Agreement.”

This contract requires the resource company to obtain an approved environmental impact assessment and management plan before ground-disturbing activities can occur. However, the contract reduces by 30 days the time normally available under law for the environmental ministry to conduct its review and issue a decision.

Environmental Liability

Natural resource contracts should always contain language clarifying who is liable for cleanup and restoration if environmental damage occurs. In accordance with the polluter pays principle, the responsible party should be the resource company. It is important to review indemnification clauses to ensure that liability has not been reversed (e.g., turning liability back to the host country) or that the bar for holding the company accountable is not set too high, for instance, by requiring the host country to prove that environmental damage was caused willfully or through gross negligence. Under no circumstances should host governments bear financial liability for environmental damage caused by a resource company.

Some contracts call for the resource company to create a fund to pay for environmental cleanup or restoration if an accident occurs or when the project comes to an end. Review these provisions carefully. In many instances, the resource company agrees to put a small percentage of its profits into the fund. On the surface, this may seem reasonable. However, as explained more fully in “Fiscal Provisions,” companies frequently take advantage of tax loopholes to avoid declaring a profit for many years. This enables the company to shortchange an environmental fund and escape financial liability if environmental damage occurs. A better alternative is to require the company to obtain insurance or post a bond prior to breaking ground. If the company is to create an environmental fund, its contributions should be tied to gross revenue or a similar benchmark that is less susceptible to manipulation by the company.

BELIZE - HYDROELECTRIC POWER

“The Government covenants and agrees to waive, or cause to be waived, and indemnify the Producer against any private action under or with respect to, any and all environmental laws, rules or regulations now existing, or created hereafter, to which the [projects] may be subject, other than any laws, rules or regulations set forth in the [project compliance plans], as the case may be, to which the Producer has agreed to be bound.”

Host countries should not indemnify resource companies against claims of environmental damage.

GHANA - GOLD ORE MINING

“[The company] shall at all times indemnify and hold harmless the Government and its officers and agency from all claims and liabilities for . . . damage to property from any cause whatsoever arising out of its operations or as a result of its failure to comply with any law to which it is subject.”

This excerpt represents a typical indemnity clause that protects the host country.

LIBERIA - IRON ORE MINING

“The Parties agree that the Concessionaire shall . . . provide an executed parent guarantee substantially in the form [provided for in the Agreement], guaranteeing the obligations of the Concessionaire [to meet capital expenditures, environmental protections and management and provision of funds.]”

A parent company guarantee alleviates the risk that a subsidiary will not be able to cover its financial liability if environmental damage or contamination occurs.

Community Projects

Many natural resource contracts include commitments to provide benefits or services to communities that are affected by, or in close proximity to, a proposed project. A resource company might promise to build schools or medical clinics, improve or construct roads and other infrastructure, provide education and health care, or furnish housing. Certain benefits might be provided to company employees and their dependents only, or be distributed to nearby communities. Collectively, these activities can be referred to as “community projects” and are often promoted by resource companies as a way to gain local support.

There is a legitimate question whether passing responsibility to a private company to provide social services and infrastructure improperly encourages the host country to abdicate its duty to provide these services to its citizens. In addition, local communities may feel pressured to accept a project in order to gain access to health care, education and other benefits linked to the project. Alternatively, a public-private partnership may provide the only opportunity to bring services to communities in the host country. In short, whether a private company should provide or subsidize social services and infrastructure is a complex issue that has to be resolved on a project-by-project basis with close consideration of community needs and host country capacity.

When reviewing an existing contract in which a company has agreed to provide community projects, make note of any deadlines and/or funding commitments. Although natural resource contracts are rarely enforceable by third parties, communities should be made aware of the promises that have been made and timelines for implementation. If projects fail to materialize or fall behind schedule, there may be opportunities for community advocates to engage with the company directly or with government regulators to bring activities back on track.

GUINEA - COPPER ORE MINING

“From the Start Date of Commercial Production the Company shall be liable to an annual levy for local development at a rate of 1% of gross profits.”

It may take many years for a resource company to declare profits. Under this contract, the company does not have to make any financial contribution to local development efforts until then.

LIBERIA - OIL PALM PLANTATION

“Investor shall annually contribute its accrued contribution at the end of each year of the Term, or US\$5.00 per hectare of land within the Developed Areas to a community development fund established for development purposes.

* * *

[The fund management Committee] shall develop an annual budget in consultation with the Government and the Investor or as otherwise required by law.

Funds . . . may be disbursed only (i) for direct delivery of services and community infrastructure improvements, and not to fund the general work programs of administrative offices or officials, and (ii) for the benefit of Liberian communities in the affected counties. The budget for and the actual disbursements from the [fund] shall be public and shall be subject to the same audit procedures provided for expenditures by the Government and as may further be provided by Law.

* * *

The Investor shall maintain a website on which are posted the members of the Committee, all audit reports, and a short description of each project funded and the amount of funding provided.”

Audits are essential to ensure that resource companies do not improperly inflate the cost of community projects or otherwise waste money.

Some contracts may establish a community benefit fund to pay for projects. These funds are usually linked to a small percentage of the company’s annual profits. As noted elsewhere in this Guide, a company may engage in tactics to delay having to declare profits and pay income taxes, and it may take many years for a project to become profitable. Therefore, it is best if the funding commitment is linked to revenue, rather than profits, and the company provides “seed” money to fund projects during early phases when it is not generating revenue. Some communities or local governments receive a portion of royalties or other payments that resource companies make to the host country, which can be designated for community projects.

If a contract provides that the resource company will undertake community projects, look for language indicating that the host country will remain primarily responsible for providing essential services to its citizens. The company may pay subsidies or cooperate with implementation of projects, but it should not stand in the place of the host country.

The contract may also include measures to facilitate public involvement in deciding what services are needed, determining whether proposed community projects are cost effective, and ensuring that projects are satisfactorily carried out and maintained. A committee or group with members chosen from affected communities can provide oversight. If a resource exploitation project is to be implemented in phases, deadlines to complete social projects should be included within overall contract schedules and work plans so that failure to carry these projects out would be considered a breach of the contract and grounds for termination.

GHANA - GOLD ORE MINING

“It is [the Company’s] policy to contribute 1% of profit to a community works. [The Company will establish a trust] with trustees drawn from [Company] management and the communities in Ghana in which the company operates. Those trustees will draw up a charter governing the administration of these funds. One percent of the [Company] profits generated in Ghana will be paid annually into this trust and be available for distribution to projects . . . that meet the criteria as set out in the Trust Charter.”

Look for opportunities for community members to guide decisions over social projects and expenditures.

LIBERIA - IRON ORE MINING

“[T]he Concessionaire shall provide an annual social contribution of US\$ three (3) million which shall be managed and disbursed for the benefit of Liberian community in [certain specified counties] by a dedicated committee to be formed by the Concessionaire and the Government. Disbursements and allocations by the committee to the said Counties of the annual social contribution shall be subject to final Government approval . . . [and] subject to independent audit in accordance with generally accepted accounting principles.”

Employment

Proponents of foreign investment in natural resource exploitation and large-scale agriculture projects often tout labor and employment benefits. In many cases, however, these jobs never materialize or are filled by foreign workers. Furthermore, modern technology and mechanization have eliminated much of the need for workers in these sectors. Nevertheless, to the extent that employment opportunities are created it is important that a natural resource contract set forth clear benchmarks to measure the company's efforts to employ and train domestic workers.

When reviewing employment or labor provisions in a contract, look for specific and measurable goals for increasing participation of domestic workers and firm commitments to provide training and education to advance unskilled workers into skilled and managerial roles.

Contracts may also discuss labor and employment conditions. If the host country lacks adequate domestic laws on this issue, the contract may reference applicable International Labor Organization (ILO) conventions and/or International Finance Corporation (IFC) Performance Standard 2 on Labor and Working Conditions.

LIBERIA - OIL PALM PLANTATION

“Investor shall give preference for employment at all levels of financial, accounting, technical, administrative, supervisory and senior management positions and other skilled positions to qualified Liberian nationals who meet the requirements and expectations of Investor . . . it being the objective of the Parties that the operations and activities of Investor under this Agreement should be conducted and managed primarily by Liberian nationals as soon as is practicable.

* * *

Investor shall use its good faith efforts to cause Liberian nationals to hold at least fifty percent (50%) of the ten (10) most senior management positions within five (5) years of the Effective Date, and at least seventy-five (75%) of such positions within ten (10) years of the Effective Date.”

Clear employment benchmarks are essential.

AFGHANISTAN - PETROLEUM DEVELOPMENT

“An annual programme for training and phasing-in of Afghan nationals shall be established by the Contractor and shall be submitted for Approval to the Ministry. Such programme shall be included in the Work Programmes submitted by the Contractor [pursuant to this Agreement.]

* * *

The Contractor shall also be required to establish a programme, reasonably satisfactory to the Ministry, to train personnel of the Ministry to undertake skilled and technical jobs in Hydrocarbon Operations for the State.”

Training programs for citizens and ministry employees are beneficial. The language in this contract could be improved by adding annual financial commitments to support training efforts.

Improving Contracts: Local Employment

Vague employment provisions in a natural resource contract can be improved in various ways. At a minimum an agreement should:

Require employment of domestic workers for unskilled positions, with priority given to individuals from affected communities.

Limit employment of foreign workers to skilled or managerial positions.

Include a timetable identifying specific benchmarks (e.g., percentage of employees) for increasing participation of domestic workers in skilled labor and managerial positions. Although representation of domestic workers in these positions may be modest at first, employment targets should increase over the duration of the project.

Establish a presumption that domestic workers are available for skilled positions and require resource companies to prove otherwise before they may hire foreign workers.

Identify annual financial commitments for job training and education to enable more domestic workers to qualify for skilled employment.

Include a commitment from the resource company to fund training and education opportunities for government employees in relevant technical positions. This will help build capacity to properly regulate operations and implement laws.

Require resource companies to submit detailed annual reports on employment statistics and training/education programs.

Contracts may also discuss labor and employment conditions. If the host country lacks adequate domestic laws on this issue, the contract may reference applicable International Labor Organization (ILO) conventions and/or International Finance Corporation (IFC) Performance Standard 2 on Labor and Working Conditions.

Declare that failure to fulfill employment and training requirements will constitute a material violation justifying contract termination.

Fiscal Provisions

The parties to a natural resource contract stand to gain considerable revenue from resource exploitation; therefore, a contract will typically address fiscal measures in great detail, even if the host country has a comprehensive set of financial and tax laws in place. The fiscal provisions of natural resource contracts are also the most difficult to understand.

It is an unfortunate fact that host country negotiators often agree to relaxed fiscal terms under the belief that foreign resource companies have to be “attracted” to undertake investments in their country and that financial incentives will encourage other companies to make new investments. This approach discriminates against local companies and gives an unfair benefit to foreign companies. Furthermore, research has demonstrated that financial incentives have little to no influence over a resource company’s decision to undertake investment in a particular project.⁷

There is no set of “best practices” for fiscal arrangements between host countries and natural resource companies. Nor is it beneficial to compare projects across the board to determine whether a particular agreement is fair, because so many aspects are variable. The overall aim should be to maximize revenue returns to the host country, but to achieve this over a long period of time and with minimal fluctuations. In addition, the host country must be capable of administering and monitoring the fiscal provisions - otherwise there is no guarantee that revenue will be properly collected or managed.

The intent of this section of the Guide is to explain and define some of the common fiscal provisions found in natural resource contracts. To fully understand the implications of a particular set of fiscal terms, particularly if you plan to be involved in contract negotiations, it is advised that you seek expert advice.

Host countries primarily receive revenue from natural resource exploitation through taxes, royalties, bonuses, and fees. They may also receive a portion of the resource that is extracted (“payment-in-kind”). Collectively, this is known as “government take.” This Guide focuses on the two most significant sources of government revenue - taxes and royalties.⁸

Corporate Tax

Resource companies are generally subject to tax on their profits at a rate defined in the contract or in national law. This is known as the “corporate tax rate.” However, income taxes are payable only when a company reports profits, which may take many years. Some companies prolong this period of unprofitability by employing tactics to delay or avoid paying taxes. (Tax avoidance is discussed later in this chapter.)

The host country’s income tax laws will clearly specify the tax rate and may include specific rates imposed on resource extraction companies. A resource company may negotiate a tax rate lower than the rate specified in the host country’s tax laws or seek a tax “holiday” in which it is exempt from paying taxes for a certain period of time. Resource contracts should specify rates that are consistent with those in national laws, rather than give resource companies special treatment relative to other businesses.

A contract or applicable tax law may impose what is known as a “windfall tax” to capture revenue when companies experience higher-than-expected profits from their activities - usually due to rising commodity prices. This type of tax is triggered when a commodity price exceeds a certain threshold.

The amount of tax payable will be affected by the deductions that a resource company claims. Deductions, in a very general sense, reflect the costs of doing business, such as start-up costs, operating expenses, equipment, and materials. Permissible deductions will be listed in domestic tax laws, but natural resource contracts often broaden the scope of deductions a company may claim. These deductions must be scrutinized carefully and compared to those allowed under the host country’s tax laws. This comparison will help shed light on the extent to which the resource company is avoiding taxes that other similarly-situated companies must pay.

GUINEA - IRON ORE MINING

“For the production operations taking place within the Mining Perimeter . . . an exemption from the industrial and commercial profits tax and from the [minimum fixed tax] shall apply for a maximum period of eight (8) fiscal years, as of the Date of First Commercial Production.

At the expiry of this period, the Investor shall pay the industrial and commercial profits tax at the rate of thirty five per cent (35%).”

Exemptions from tax requirements are known as “tax holidays.”

LIBERIA - RUBBER PLANTATION

“Investor shall be taxed on its net taxable income in accordance with the Tax Law, provided that during the first twenty-two (22) years of the Term . . . the applicable tax rate shall not exceed 25%. For the avoidance of doubt, if at any time the rate of general application is less than twenty-five percent (25%) during the Term, Investor shall be entitled to enjoy such lower rate.”

Resource companies will seek opportunities to reduce their tax obligations, including paying a lower corporate tax rate than is required by law.

Customs Duties

It is not uncommon for import duties to be waived on specialized equipment, vehicles, and supplies that companies use for project development and production. Look for an appendix or attachment to the contract that lists categories of exempt goods and materials. Such a list helps curb tax abuse and facilitates accurate oversight and monitoring by revenue authorities. A well-designed list will not be too broad. Items such as food and fuel should not be exempted from duties, as this only encourages companies to import products that they should be purchasing from local suppliers and domestic businesses.

Export Taxes

Some countries impose export taxes on commodities and natural resources to ensure that there will be ample domestic supply. Export taxes on raw materials also encourage companies to add more value to a product through further refining or processing within the host country.

It is not uncommon to see contracts that waive export taxes. This can mean the loss of a substantial source of revenue for the host country and might encourage companies to export materials that could be used or processed domestically.

GHANA - GOLD MINING

“[The Companies] shall pay no Taxes or Duties with respect to the import, use or purchase of [mining machinery, equipment, or tools], other goods, equipment, vehicles and supplies (including medical[,] training and educational supplies and housing and office materials, furniture and supplies), and any other items required for and used in Exploration, Development and Production including, without limitation, the items listed on the Mining List attached hereto as Appendix B.”

When duty exemptions are worded this broadly, a company has freedom to import goods that it could be purchasing from local suppliers.

AFGHANISTAN - PETROLEUM DEVELOPMENT

“[F]or a period of two (2) Years from the Effective Date, the Contractor shall be entitled to export Liquid Hydrocarbons free of Customs Duties, which are currently set. . . at two and one half percent (2.5%).”

The customs duty in this contract is temporarily waived for two years.

Withholding Taxes

Another type of tax that may be discussed in natural resource contracts is withholding. Withholding taxes are assessed against certain types of payments made by resource companies, such as dividends, rental fees, management fees, and loan interest payments. This tax ensures that the host country captures its share of these funds before they are transferred to the recipient (who may be outside of the host country).

It is very common for natural resource contracts to exempt a resource company from paying some or all withholding taxes. If so, the host government may be missing an opportunity to boost its tax revenue from resource exploitation. Resource companies should stand on equal footing with other businesses and be held to the same withholding requirements set out in national tax laws. Investigate whether the host government has entered into any “dual tax” (or “double taxation”) treaties with a resource company’s home country. These treaties will typically address withholding taxes and applicable rates. (The text of most dual tax treaties can be found online).

GHANA - GOLD ORE MINING

“[The Companies] shall withhold tax on the payment of management fees paid either to an Affiliate or to a third party at the rate of ten percent (10%) and shall pay such amount to the Commissioner of the Internal Revenue Service . . . [.]”

Withholding tax is typically collected on management fees, dividends, and interest payments. Here, a mining company is required to pay withholding tax on only one of those categories and at a lower rate than is currently required by Ghanaian law (15%).

Royalty

A royalty is a payment for the use of a valuable right, including exploitation or removal of non-renewable natural resources. Royalties have long been part of natural resource contracts because they are relatively easy to administer and, as long as the resource is extracted and sold, the host country receives payment regardless of whether the company makes a profit.⁹ The royalty rate may be fixed or may fluctuate based on the quality or type of material that is produced. For example, a host country may lower the royalty rate for low-grade mineral ores in order to encourage a resource company to fully work a deposit and not just take out high-grade mineral deposits.

The most common types of royalties are: 1) unit value and 2) ad valorem. Unit value royalties are assessed as a percentage of the volume or weight of the resource produced (royalty rate \times volume or weight of resource). This type of royalty is easier to administer because it does not require consideration of the sales price or quality of the resource.¹⁰ If prices of a particular resource rise over time, however, a unit value royalty does not generate more revenue. A unit value royalty is usually applied to resources that are consistent in quality or sold in bulk, such as industrial minerals or coal. The contract will specify where in the extraction or production process that the weight or volume measurement is taken.¹¹

LIBERIA - GOLD ORE MINING

“The Operator shall pay to the Government in Dollars a royalty at the percentage rate specified below on the proceeds paid to the Operator from the sale of Minerals recovered from a Production Area and sold by the Operator:

- (a) gold and diamonds, three percent (3%)
- (b) all other minerals to be agreed but not to exceed five percent (5%).

Royalty shall be determined on a Net Smelter Return basis for gold and Gross Revenue basis for diamonds.”

An example of an ad valorem (value-based) royalty.

BELIZE - PETROLEUM DEVELOPMENT

“The Contractor shall pay to the Government a royalty equal to (i) seven and a half percent (7.5%) of the value of the annual gross production of crude oil produced and saved in each calendar year and not used or consumed in petroleum operations and (ii) five percent (5%) of the value of the annual gross production of natural gas produced, saved and sold in each calendar year and not used or consumed in the conduct of petroleum operations.”

Host countries may assess lower royalty rates for less valuable resources, or resources that are extracted simultaneously with the primary target, to encourage thorough development of non-renewable supplies.

LIBERIA - IRON ORE MINING

“The royalty rate for shipments or sales of Iron Ore in any month during the Term shall be as follows: (i) when the Index Price is US\$100 per metric ton or less the royalty will be 3.25%, (ii) when the Index price is greater than US\$100 per metric ton and less than US\$125 per metric ton, the royalty will be 3.5%, (iii) when the Index Price is greater than US\$125 per metric ton and less than US\$150 per metric ton, the royalty will be 4.0%, and (iv) when the Index Price is US\$150 per metric ton or more the royalty will be 4.5%.”

The royalty rate in this contract increases as the price of iron ore goes up. The host country collects more revenue without having to revise the contract.

AFGHANISTAN - GOLD ORE MINING

“After the start of commercial production . . . [the Company] agrees to pay, monthly, to the [Ministry], royalties at the rate of twenty six percent (26%) of the gross revenue from the sale of gold at a price set on the date of sale by the London Metals Exchange for the sale of gold.”

Inclusion of reference prices in an ad valorem royalty helps curb valuation abuses by resource companies.

Ad valorem royalties are assessed as a percentage of the value of the resource extracted or produced (royalty rate \times value of resource). The point at which the value is determined can vary. Contracts might assess value of a resource at the point of extraction, after it has been processed or refined, or when it is sold. The amount of royalty collected will automatically rise as the price of a resource increases. Note that ad valorem royalties are susceptible to transfer pricing abuse, as described later in this section. To combat this problem, some host countries do not rely on the value reported in a company’s sales invoices but instead use a neutral “reference” price published by exchanges or commodity boards.

When reviewing a natural resource contract that prescribes a royalty rate, always check the rate against those established in national laws. Also look to see where along the production chain the royalty is assessed and whether the company is allowed to offset its royalty payments with certain costs. Contracts will typically specify whether a company is permitted to deduct certain expenses, such as the cost of transporting a resource to a shipping terminal, from its royalty payments.

If there is a possibility that a valuable resource may be comingled with the primary resource being extracted or used, the contract should require the company to pay royalties on that resource, as well. An example might be a gold mining project in a deposit that also contains small amounts of copper ore. Or, an oil palm plantation established in a heavily forested area that will be cleared. A well-drafted contract will use these opportunities to obtain revenue for the host country.

Common Tax Avoidance Tactics

Even if the fiscal provisions in a natural resource contract appear to be fair, be aware of tactics that resource companies use to escape their tax liabilities. Some common tax avoidance strategies resource companies take advantage of are discussed below.

Transfer Pricing

Most companies undertaking large-scale natural resource exploitation and agricultural production have complex corporate structures with subsidiaries or related companies based in different countries. Companies often take advantage of this structure to engage in a practice called “transfer pricing.” Transfer pricing occurs when a company arranges sales with related companies for goods or services at either highly inflated or discounted prices. Transfer price abuse (also known as “mis-invoicing”) is a common tax avoidance scheme practiced by multinational companies across all sectors.

Transfer pricing abuse can occur very easily. For example, it is not unusual for a natural resource contract to waive all duties on equipment that a company brings into the host country for its operations. A company can take advantage of this tax break by paying its out-of-country affiliates (related companies) above-market prices for equipment and import that equipment duty free. The company can then deduct the inflated equipment cost from its income - thus reducing the company’s tax liability and effectively transferring funds tax-free to a related company outside of the host country. Similarly, a company might pay exorbitant fees to an affiliated off-shore company to provide technical consulting while deducting that cost from its taxable profits within the host country. Commodity export pricing is another area where mis-invoicing commonly occurs. Companies may vastly undervalue mineral ore, petroleum, or agricultural products in sales to an affiliated company. This practice reduces the amount of royalties and/or taxes that are owed to the host country.

LIBERIA - OIL PALM PLANTATION

“All transactions between Investor and any of its Affiliates shall be on such terms and conditions as would be fair and reasonable had the transaction taken place between unrelated parties dealing at arm’s length. Any transactions involving the sale of the Crude Palm Oil or Crude Palm Kernel Oil by Investor to any of its Affiliates shall be on the basis of Competitive International Prices FOB Liberia.” (“Competitive International Prices” are defined elsewhere in the contract by reference to prices quoted by the Malaysian Palm Oil Board or the Bursa Malaysia Derivatives Berhad.)

To curb transfer pricing abuse, this contract requires all sales with affiliates to be valued according to international reference prices. Whereas, with unrelated companies, the company can set any competitive price.

LIBERIA - OIL PALM PLANTATION (CONT'D)

“Investor shall have the right to sell Oil Palm Products to unrelated Persons of its choosing at prices it deems appropriate taking into account good, modern and competitive business practices, provided that within 30 days after each six (6) month period, Investor shall inform Government of the terms and conditions of all such sales that took place during the such six (6) month period.”

There are several ways to address transfer pricing abuse in natural resource contracts. The first is through provisions governing “affiliate transactions.” The contract should declare that all transactions conducted with affiliates be undertaken as if between unrelated parties dealing at arm’s length. Second, the term “affiliates” should be defined broadly enough to not only include companies directly linked to each other via shareholding (such as subsidiaries) but also companies that may have long-term contractual relations with the resource company that is a party to the contract.

Third, and depending on the resource that is being exploited, the contract should require export transactions with affiliates to be valued according to available international reference prices or indices. The contract can even mention a specific index.

Domestic tax laws, or the contract, may also directly address transfer pricing by authorizing revenue authorities to review affiliate transactions and recharacterize them if it appears that pricing abuses have occurred. Note, however, that there is usually a limited period of time for authorities to conduct this review, and it can be difficult for regulators to police transactions between affiliated companies and identify transfer pricing abuses.

Disclosure of beneficial ownership is a mechanism to limit tax avoidance, corruption, and anti-competitive practices. Beneficial owners “in respect of a company means the natural person(s) who directly or indirectly ultimately owns or controls the corporate entity.”¹³ Usually, the beneficial owner is the ultimate recipient of profits or other benefits generated by property held in another’s name. Contracts should contain provisions requiring the resource company and its contractors to disclose their beneficial ownership and regularly update this information throughout the life of the agreement, or otherwise be considered in material breach of the contract.

INTERNATIONAL BAR ASSOCIATION MODEL MINING DEVELOPMENT AGREEMENT

“Affiliate” means an entity that directly, or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with the Company. For purposes of this definition, “control” means ownership of greater than 50% of the share capital of a company and/or the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of an entity, whether through the ability to exercise voting power, by contract or otherwise.¹²

LIBERIA - RUBBER PLANTATION

“[Appendix II] is a complete and correct list . . . of (a) each Affiliate of Investor and, in each case, its relationship to Investor and the jurisdiction in which it is organized; (b) the directors and senior officers of Investor and of each Person deemed to control Investor; and (c) each Person who is the ultimate beneficial owner of five percent (5%) or more of . . . the voting rights ordinarily empowered to control the management of Investor or . . . the rights to share in the profits of Investor, and the chain through which such rights are exercised.”

Knowing a resource company’s corporate structure, affiliates, and ultimate beneficiaries helps shine a light on transfer pricing abuse and other tax avoidance tactics.

Exchange Control

Transfer pricing abuse can be influenced by foreign exchange controls. Foreign exchange controls are imposed in an effort to prevent “capital flight,” which can weaken local currency. Capital flight and tax evasion usually go hand in hand.¹⁴ To combat this problem, foreign exchange controls limit the extent to which local currency can be converted to foreign currency, restrict off-shore transfers or repatriation of currency, prevent citizens and businesses from holding off-shore bank accounts, and ration the amount of foreign currency available for exchange.

Resource companies will pay close attention to foreign exchange controls and will advocate for complete freedom to hold and transfer funds in any place and in any currency that they choose. When there are little to no controls on foreign exchange, companies can engage in transfer pricing and other tax avoidance behaviors more easily because there is less oversight of their currency flows in and out of a country.

Natural resource contracts will often contain provisions addressing foreign exchange control. Compare contract language to any requirements in the host country’s foreign exchange laws. Many developing countries have lifted exchange controls to encourage foreign investment. If there are controls contained in domestic laws, however, they should not be waived in the contract.

MONGOLIA - COPPER ORE MINING

“The Investor is hereby granted the rights to market, sell and export its Products at international market prices and to freely expend and repatriate its sale proceeds in Mongolian togrogs and foreign currencies.”

An example of a typical exchange control provision. Many countries impose no currency controls on foreign companies operating within their borders.

Ring-fencing

Ring-fencing is a “paper” separation of a taxpayer’s activities and operations that limits consolidation of income and deductions. The issue of ring-fencing comes to the fore when resource companies have more than one project ongoing in a particular country. If the host country does not have a ring-fencing rule, companies are free to combine the accounts of multiple projects even if they are geographically separate. A company can count the losses from one venture against the profits of a more successful venture, thus reducing its overall tax obligation. Ring-fencing separates each venture for accounting purposes. The “fence,” so to speak, may be established at the contract boundary or may be drawn around activities conducted under particular licenses or permits, which could encompass multiple contracts. Ring-fencing is generally encouraged to prevent companies from shifting losses to profitable activities within the host country.

If ring-fencing is not discussed in a natural resource contract, it may be addressed in domestic tax laws.

Accelerated Depreciation

Most tax laws allow businesses to deduct capital costs, which are the one-time expenditures necessary to bring a project into production. Businesses are typically permitted to write off capital costs over a period of time reflecting the gradual loss of value of assets, such as equipment. This is known as “depreciation.”

With “accelerated depreciation,” capital costs are deducted in their entirety at the outset of project development. The deduction may be allowed in the year the expenditure is made (“expensed as purchased”) or taken over a very short period of time. With activities that are highly capital-intensive, such as large-scale mining or oil and gas production, accelerated depreciation is a significant benefit to resource companies. However, this practice also allows the companies to postpone paying taxes; therefore, it is appropriate to insist that resource companies take normal (e.g., gradual) depreciation deductions.

GHANA - GOLD ORE MINING

“In computing [the Companies’] net taxable income, those deductions permitted by Law, and the following deductions to the extent not otherwise permitted as deductions under Law, including . . . those deductions arising from activities under any other Prospecting License or Mining Lease that [the Companies] may acquire after the Effective Date, and those deductions otherwise arising from any Operations carried out hereunder, shall be allowed as deductions from its gross income.”

This contract does not apply ring-fencing principles and allows mining companies to shuffle income tax deductions among current (and future) operations.

Loss Carry-Forward

Like capital costs, discussed above, most tax codes permit taxpayers to deduct business losses from a future year's profits for a designated period of time. This is known as "loss carry forward." Resource companies often incur significant business losses during the early years of projects as they are building facilities and investing in equipment, yet not generating any revenue. When negotiating a resource contract, a company will seek special treatment in order to carry losses forward for an indefinite period of time and defer payment of income tax until its losses are fully recouped.

Usually tax laws will limit the amount and/or duration of loss carry forwards. Natural resource contracts should reflect these same limits and not allow companies to carry losses forward indefinitely.

LIBERIA - OIL PALM PLANTATION

"The loss carried forward period shall be extended for a period of 5 years starting from the first year in which [the Company] has taxable income under the Law[.]"

Resource companies will seek to offset their profits with deductions and losses for as long as possible so that they do not have to pay taxes. It is not in the host country's interest to allow unlimited carry forwards.

GHANA - GOLD ORE MINING

"Any deduction arising from accelerated depreciation and any other deduction, to the extent that, for any reason, it was not claimed in a year in which it is claimable, may be carried forward without limitation and may be claimed by [any of the companies]."

Tax Holidays

Tax holidays are relatively straightforward and easy to spot in natural resource contracts. In such provisions, the host country agrees to waive application of tax laws for a particular period of time. Tax holidays appear to be used less frequently and have been replaced by provisions that allow particular tax exemptions or accelerated depreciation.

Tax holidays should not be included in natural resource contracts. Their costs far outweigh their benefits and studies demonstrate that they do not attract more investment. Furthermore, "tax holidays also increase administrative problems because tax authorities usually do not monitor company books during the period in which a firm is exempt from taxes. As a result, asset purchases, depreciation charges, and other accounts can be manipulated during the holiday period to reduce reported income, and thus taxes, after the end of the holiday."¹⁵

Case Study: Impacts of Tax Avoidance in Zambia

Tax avoidance can cause significant financial repercussions to host countries. For example, an audit conducted of the Mopani copper mining project in Zambia revealed that the mining company engaged in a number of questionable practices to avoid paying taxes, resulting in an estimated £76 million per year loss to the government of Zambia. Auditors noted that the Zambian-registered mine operator sold most of its copper at low prices to its off-shore parent company, based in Switzerland, and could not provide evidence to tax officials or auditors that sales were conducted at arm's length (as required by law). The audit questioned a number of abnormally high costs claimed by the company, as well as the veracity of production figures. Tax authorities in Zambia sought to reclaim lost revenue from the company following revelations in the audit, but were not successful.¹⁶

Capital Structure

Companies will create “shell” subsidiaries to limit financial liability for accidents or environmental contamination. A parent company may also require subsidiaries to borrow substantial amounts of money at high interest rates from it or related companies. (Loan interest is usually deductible from corporate income for tax purposes so, like transfer pricing, “affiliate” loans can be used as a tax avoidance scheme.) In countries with high corporate tax rates, there is an incentive for companies to take out loans to fund their operations so that they can deduct the financing costs and reduce their overall tax liability.¹⁷

Natural resource contracts often contain clauses that require the resource company to maintain adequate capital and not to take on too much debt. If a company is proposing to fund a project with loans, this is a strong sign that the project will be susceptible to delays or closure during economic downturns. Furthermore, the company will be using its profits to pay off these loans rather than paying income taxes to the host government.

Usually the contract will include a general statement that the resource company agrees to maintain a “reasonable and prudent” capital structure throughout the life of the agreement. This is a vague requirement that is subject to interpretation and debate. However, some contracts also include what is called a “debt-to-equity ratio.” A company will be presumed to be carrying adequate capital as long as that formula is met. A recommended debt-to-equity ratio is 2:1. Debt-to-equity ratio and other “thin capitalization” rules may also be addressed in domestic tax laws. These provisions limit the deductibility of loan interest for foreign-controlled companies once a certain debt threshold is passed.

LIBERIA - OIL PALM PLANTATION

“Investor shall not incur any new Long-Term Debt if, following such incurrence, the ratio of Long-Term Debt to Equity Capital of the Investor would be greater than 3:1.”

An example of a debt-to-equity provision capping the amount of long-term debt a resource company may acquire.

Case Study: Thin Capitalization in Ghana

A company is considered “thinly capitalized” in Ghana when its debt-to-equity ratio exceeds 2:1. At that point, according to the Internal Revenue Act, the company is not allowed to deduct foreign exchange losses or interest payments on loans. Yet, in a mining investment agreement negotiated with U.S.-based Newmont Mining Corporation in 2003, the government of Ghana agreed to provisions that allow Newmont’s subsidiaries in Ghana to hold a debt-to-equity ratio of up to 4:1 and still be considered adequately capitalized for the purposes of qualifying for tax deductions.¹⁸ This arrangement is a significant departure from Ghana’s tax law and enables Newmont’s subsidiaries in Ghana to engage in tax avoidance behavior.

Local Content

Many contracts require an investor to use domestically-produced materials or products to support local manufacturers and generate employment. These clauses are frequently called “local content provisions.” Local content standards or performance requirements may also be found in domestic laws or policies. The overall goal of these provisions is to create positive economic benefits in the host country in addition to taxes, royalties, and other payments. These benefits may include increased employment of domestic workers, new business opportunities for local/domestic companies to provide materials and services, and development of new industries.

In countries that are members of the World Trade Organization (WTO), it is important to review local content provisions carefully because they may run afoul of WTO rules if they discriminate against foreign suppliers and potentially affect international trade. Under the Agreement on Trade-Related Investment Measures of the WTO, commonly known as the “TRIMs Agreement,” WTO members agreed not to apply certain investment measures related to trade in goods that restrict or distort trade. Annex I of the Agreement contains an illustrative list of the types of TRIMs that are not permitted under WTO rules.¹⁹ The list includes contract provisions that require a company to purchase local products or restrict import of foreign products that are used by a resource company during development or production. In other words, a natural resource contract cannot require a company to purchase local goods if a better alternative in terms of price or quality exists abroad. For that reason, many contracts will contain “soft” or nonbinding language in which the resource company agrees to make best efforts to use local materials and services during the course of a project.

Regional or bilateral investment treaties may impose similar restrictions on performance requirements and trade-related measures. These agreements are discussed below in “Investment Treaties.”

GHANA - GOLD ORE MINING

“[The Companies] shall, to the maximum extent possible and consistent with safety, efficiency and economy, when purchasing goods and services required with respect to Operations, give preference to materials and goods made in Ghana, and services provided by Ghanaians or entities incorporated or formed in Ghana and owned or controlled by Ghanaians, provided that such goods and services are equal in quality, terms, delivery, service, quantity and price to, or better than, goods and services obtainable outside Ghana.”

An example of a local content provision with a non-binding commitment to purchase local goods and services.

ZAMBIA - COPPER ORE MINING

“In assessing the tenders from local contractors and suppliers, the Company will consider the extra costs it would incur if it were to grant the contract to a foreign supplier or contractor. These extra costs shall include, but are not necessarily restricted to, wharfage costs, shipping costs, stevedoring costs, customs clearance, customs duties [], and demurrage charges.”

Requiring a resource company to consider the added costs of importing supplies may tip the balance in favor of locally produced goods.

LIBERIA - IRON ORE MINING

“Upon request, the Company will provide financial assistance of up to US\$500,000 to the Government for the purposes of funding the initial costs of conducting a scoping study to assess the potential to establish downstream Iron Ore processing facilities in Liberia . . . [.]”

Feasibility studies may reveal opportunities to build economic links and generate new businesses in the host country.

Improving Contracts: Local Content Strategies

Like many aspects of natural resource contracts, local content requirements and policies are complex. However, there are a few relatively simple strategies to boost the economic benefits of resource exploitation projects.

Specific Benchmarks and Goals. Regrettably, many natural resource contracts contain vague and non-specific local content provisions that are easily ignored by the resource company. To the extent permissible by law and applicable trade agreements, contracts should include clear and realistic targets for increasing procurement of goods and materials from domestic companies. These benchmarks and targets should also apply to subcontractors and affiliates that are engaged in the project.

Define “Local.” Local content efforts should be directed towards businesses that are truly rooted in the host country. Many contracts classify local or domestic businesses simply by whether they are registered to do business in the host country or by the nationality of their owners. This approach does not take into account whether the business is legitimately employing citizens or sourcing materials and services locally. Contracts should include provisions encouraging resource companies to procure goods and services from businesses demonstrating significant participation by citizens in ownership, management, and employment.

Build Capacity and Generate Awareness of Local Resources. Local content provisions serve little purpose if domestic businesses cannot handle increased demand or provide particular supplies and services. It may be appropriate in these circumstances for the resource company to undertake a feasibility study with the cooperation of civil society organizations and trade associations to evaluate the business and employment environment at local, regional, and national levels and identify strategies to build domestic linkages and capacity at each level.

Reporting. Greater accountability can be achieved if resource companies provide periodic reports on their efforts to increase local participation and sourcing of materials, their relationships with domestic companies, and whether they have reached local content goals. Even if a natural resource contract does not contain specific local content targets or goals, reporting enables civil society organizations and local communities to discern whether a resource company is making good-faith efforts to support and benefit the local economy.

Stabilization

“Stabilization” provisions in natural resource contracts require the host country to preserve the legal and regulatory framework in place at the time a contract takes effect. Resource companies claim that stabilization provisions are necessary to protect their investments in large-scale projects and prevent sudden, unanticipated costs triggered by new regulatory requirements.

Stabilization clauses generally appear in one of two forms in natural resource contracts. The clearest examples are contract provisions that block application of new or amended regulatory requirements enacted after the date the contract is signed. The text might even be in a section titled “Stabilization.” Alternatively, stabilization language might be couched in an “economic equilibrium” clause that requires the host government to compensate the resource company for any additional costs caused by new or amended regulatory requirements.

There has been a lot of attention devoted to stabilization provisions and whether they run afoul of principles of state sovereignty over natural resources. Furthermore, such clauses could be considered unconstitutional in countries that adhere to the principle that the executive body cannot bind the legislature, or that a current legislature cannot bind the activities of a future legislature. As one expert notes: “As a matter of constitutional theory, the stabilization clause may not be able to achieve what it sets out to do. It may not serve as anything more than a comforter to the foreign investor, who may derive some security from the belief that there is a promise secured from the state not to apply its future legislation to the agreement.”²⁰ For these reasons, and because stabilization provisions interfere with the host country’s ability to implement laws that protect public welfare and the environment, they are discouraged in natural resource contracts. Nevertheless, stabilization clauses are quite common. Sector-specific laws in the host country might even require stabilization provisions to be included in natural resource contracts or permit negotiators to insert them.

GUINEA - COPPER ORE MINING

“The Government warrants the Company from the date of grant of the Concession and throughout its full duration the stabilization of Current Legislation and of all provisions, particularly fiscal and concerning customs and excise, stipulated in this Agreement.”

An example of a broadly written stabilization clause. The project is exempt from all new and amended legislation, including environmental, health, and safety laws.

LIBERIA - IRON ORE MINING

“The Government further undertakes not to adopt any provision of Law that imposes a material financial or other burden solely on the Company or any of its Affiliates, whether or not such provision specifically identifies the Company or any of its Affiliates as the target thereof, provided that this provision shall not apply to any Law reasonably intended to protect the safety, health, welfare or security of the Government or citizens of Liberia or to fulfill the Government’s international obligations.”

This stabilization clause is tailored so that the mining company must comply with future laws that protect health, safety, and public welfare.

ZAMBIA - COPPER ORE MINING

“[The Government] covenants to reimburse the Company (or, at its option, make offsetting changes in any law, statute, regulation or enactment applicable to the Company) to ensure that Company is fully, fairly and timely compensated for any costs incurred by it by reason of a failure of the [Government] to comply with the [stabilization provisions of the Agreement].”

This contract includes an economic equilibrium clause in which the host country agrees to compensate the resource company for the added costs of complying with new or amended laws.

Improving Contracts: Stabilization

The UN-endorsed Principles for Responsible Contracts contains an excellent set of negotiating principles concerning stabilization clauses.²¹ Among them:

“Contractual stabilization clauses, if used, should be carefully drafted so that any protections for investors against future changes in law do not interfere with the State’s bona fide efforts to implement laws, regulations or policies, in a nondiscriminatory manner, in order to meet its human rights obligations.”

“It is legitimate for business investors to seek protections against arbitrary or discriminatory changes in law. However, stabilization clauses that ‘freeze’ laws applicable to the project or that create exemptions for investors with respect to future laws, are unlikely to satisfy the objectives of this Principle where they include areas such as labor, health, safety, the environment, or other legal measures that serve to meet the State’s human rights obligations.”

“Stabilization clauses, if used, should not contemplate economic or other penalties for the State in the event that the State introduces laws, regulations or policies which: (a) are implemented on a non-discriminatory basis; and (b) reflect international standards, benchmarks or recognized good practices in areas such as health, safety, labor, the environment, technical specifications or other areas that concern human rights impacts of the project.”

Contract Renegotiation

Most natural resource contracts are of long duration, which makes them susceptible to changing circumstances over time. Renegotiation clauses describe the conditions under which the parties may revise a natural resource contract.

Ideally, a contract should include a renegotiation provision requiring the parties to periodically review the agreement to determine whether it is meeting its objectives and undertake renegotiation if expectations become skewed. Review might be undertaken after particular phases of the project are completed or on a periodic schedule. A less flexible option is language allowing renegotiation only after a significant change of circumstances.

Even if the contract does not contain a review period or renegotiation clause, a host country does not have to stick with an unfair deal. Once a resource company has established facilities and made significant financial investments, it will be less inclined to leave. Under these circumstances, the balance of power shifts toward the host country and it is in a better position to request renegotiation and rebalancing of benefits (a theory known as “obsolescing bargain”).²² Over the last decade, a number of countries, including Guinea, Liberia, and Zambia have successfully renegotiated natural resource contracts with positive results.

LIBERIA - OIL PALM PLANTATION

“... Government on the one hand and Investor on the other hand, shall at the request of the other consult together to discuss the provisions of this Agreement that are directly related to the Profound Change in Circumstances. The party who is of the view that Profound Changes in Circumstances exists shall provide the other party with reasonable information in respect thereof. The Parties shall meet to review the matter raised as soon after such request as is reasonably convenient for them both. In case Profound Changes in Circumstances are established to have occurred, the Parties shall effect such change in or clarification of this Agreement that they agree is necessary.”

In this excerpt, renegotiation occurs only if one party can demonstrate there has been a profound change in circumstances. This is a significant hurdle to overcome.

LIBERIA - GOLD ORE MINING

“The Parties agree that the Agreement shall be subject to periodic review once every five years after the commencement of Production for the purpose of good faith discussions to effect such modifications to the Agreement as may be necessary or desirable in the light of any substantial changes in circumstances which may have occurred during the previous five years.”

In contrast, this excerpt calls for periodic review and negotiation, if necessary, on a regular basis.

Most Favorable Treatment

Related to stabilization clauses are contract provisions promising a resource company “favorable treatment” relative to other companies that are operating (or may operate in the future) in a country. These clauses open a natural resource contract to renegotiation if the host country makes an arrangement or agreement with a different company that is considered better or more favorable to the first company. Sometimes the more favorable terms are substituted automatically without formal revision of the contract. Examples include lower royalty rates or corporate taxes, tax holidays, relaxed environmental or labor standards, or land privileges.

GUINEA - IRON ORE MINING

“[T]he company shall benefit from any more favorable clause granted in respect of the provisions of this Agreement that will be included in a mining agreement concluded at a later date with another mining company carrying out similar activities.”

AFGHANISTAN - PETROLEUM DEVELOPMENT

“The treatment accorded to the Contractor by Afghanistan shall not be less favourable than the treatment required to be accorded by Afghanistan to foreign investors under applicable law.”

Examples of most favorable treatment clauses.

LIBERIA - GOLD ORE MINING

“In the event that the Government grants to any other Person terms and conditions that are more favorable than those provided in this Agreement with respect to operations, exploration or production of the same Minerals, or in the event that the Government enacts any Law or adopts any practice or policy that permits more favorable treatment of any other Person than that accorded to the Operator by this Agreement. . . then the Government shall grant the same more favorable treatment to the Operator, with effect from the date of its application to such other Person or of its entry into force as the case may be.”

Most-favored treatment clauses are particularly dangerous because later agreements may be negotiated with no knowledge that the clause exists in older contracts. As one expert notes:

“It is also prudent to avoid . . . ‘most- favoured-company’ provisions that enable the investor to benefit from any more favourable treatment granted to other companies. The latter type of clause contrasts with the fact that each project inevitably has different cost and risk structures, so that concessions on the fiscal regimes given to a project may not be relevant to another one.”²³

For these reasons, most-favored treatment clauses should never be included in natural resource contracts.

Confidentiality

In most countries, natural resources are owned by the state and are managed on behalf of citizens. Therefore, it is the public's right to access the contracts governing use and exploitation of these resources. Yet a majority of these contracts are negotiated in secret and never publicly disclosed. Host governments claim that the agreements must be kept confidential to protect the business interests of resource companies and to secure the host government's bargaining position in future contracts. These arguments hold little weight. As an International Monetary Fund (IMF) report observed: "Little by way of strategic advantage . . . seems to be lost through publication of contracts. Indeed, it could be argued that the obligation to publish contracts should in fact strengthen the hand of government in negotiations, since the obligation to disclose the outcome to the legislature and the general public increases pressure on the government to negotiate a good deal."²⁴

The Principles for Responsible Contracts emphasize contract transparency, explaining that disclosure "promotes accountability of both parties to implement the promises agreed in the contract and notifies third parties of the rights and obligations of the parties to the contract. Therefore disclosing the contractual terms can promote trust in the investment project and the parties to the investment."²⁵ Similarly, the International Finance Corporation (IFC) Policy on Environmental and Social Sustainability currently encourages governments and companies to make extractive industry contracts public and, beginning in 2014, will require disclosure of the principle contract governing any extractive industry project it finances.²⁶ A growing number of countries are requiring contract disclosure under their constitutions or legislation, including Guinea, Liberia, Niger, Peru, and São Tomé and Príncipe.²⁷ Therefore, it is becoming accepted practice to publicly disclose natural resource contracts.

A second issue related to transparency is disclosure of information related to contract implementation. Many contracts contain broad confidentiality clauses that bar public release of the contract and prevent disclosure of any information exchanged between the resource company and the host country during the term of the contract. In many cases, these clauses clearly contradict access to information laws in the host country and unnecessarily shield the resource company's and host government's activities from scrutiny.

To reflect best practices in transparency, a natural resource contract must require public disclosure of the agreement within a short amount of time after it has been signed. In addition, the contract must include language declaring that there is a presumption in favor of public disclosure of non-proprietary information related to contract implementation and the resource company's operations. This includes putting the burden on the company to ask for information to be withheld, rather than requiring the host country to seek permission before disclosing information. A model disclosure provision for natural resource contracts, drafted by Revenue Watch, is as follows:

This Agreement will be published in [government gazette/federal register] or publicly available at [ministry website/ ministry library/ parliamentary records]. Information in relation to activities under these agreements shall be kept confidential if requested by a Party, to the extent that such Party establishes that confidentiality is necessary to protect business secrets or proprietary information. Such confidentiality is subject to [relevant disclosure laws], as well as to applicable laws and regulations, including stock exchange and securities rules, and requirements for the implementation of the Extractive Industries Transparency Initiative.²⁸

ZAMBIA - COPPER ORE MINING

The Government and Ministry of Mines and Mineral Development “hereby acknowledge that all information supplied to them pursuant to [the contract] is confidential information and hereby agree to treat as secret and confidential and not at any time for any reason to disclose or permit to be disclosed to any person or otherwise ma[k]e use of or permit to be made use of any such information . . . and upon termination of this Agreement for whatever reason [the Government and Ministry] will deliver up to the Company all working papers, computer discs and tapes or other material and copies provided to or prepared by the company pursuant to this Agreement and still retained by [them].”

This contract broadly declares that all information supplied by the resource company to the host country is confidential. At the end of the project, the host country must return all documents and other materials back to the resource company.

LIBERIA - LOGGING

“The parties understand that . . . the National Forestry Reform Law of 2006 guarantees the public free access to all documents and information related to this Contract and its administration, subject only to limited exceptions.”

Compare with the following two excerpts, which support greater transparency and access to information.

AFGHANISTAN - PETROLEUM DEVELOPMENT

“The Ministry shall have the right to keep a copy of this Contract in the Hydrocarbons Register, publish and keep publicly available and distribute to provincial offices such information and reports on the Contract, related documents and the Contractor as is required pursuant to the Hydrocarbons Law, any regulations issued thereunder and internationally accepted norms relating to transparency in the extractive industries, including production and financial data concerning all revenues from income taxes, production shares, royalties, fees and other taxes and other direct or indirect economic benefits received by the Ministry and all amounts paid by the Contractor under or in relation to this Contract.”

Maintaining Records

During the course of a project, a resource company will generate considerable information concerning its operations. Among other things, it will maintain financial records, collect operations and production data, and monitor its performance. Natural resource contracts typically include provisions indicating where company records must be maintained and whether the host country will have access to them. Under no circumstances should a contract allow a resource company to “repatriate” or maintain its books and records (other than copies) outside of the host country.

A contract may also include reporting requirements (as discussed throughout this Guide) and this information can be a valuable tool for monitoring contract implementation. It may be possible to obtain this information through an informal request to the government agency responsible for regulating the resource company’s activities or through access to information laws.

AFGHANISTAN - PETROLEUM

“The Contractor shall, in accordance with prevailing legislation and regulations and International Financial Reporting Standards, be obliged to keep and maintain complete accounts, books and records at its registered office in Afghanistan reflecting all Hydrocarbons Operations, Hydrocarbons Operations Expenditures and Gross Contractor Revenues consistent with generally accepted procedures and standards in the international petroleum industry . . .[.]”

This excerpt clearly states the host country’s expectations regarding where records will be maintained.

ZAMBIA - COPPER ORE MINING

“The Company shall maintain all original records and reports relating to its activities and operations under this Agreement including all documents relating to financial and commercial transactions with independent parties and Affiliates in its principal office in Zambia for a period of three (3) years.”

Contracts should not allow resource companies to take key documents out of the host country because regulators will not be able to monitor the company’s operations effectively.

Resolving Conflicts

Disputes are bound to arise during implementation of natural resource contracts. The ideal forum for resolving these conflicts is in the courts of the host country, particularly if they involve interpretation of the host country's law. However, contracts increasingly include provisions in which host countries waive their rights to use domestic courts to resolve disputes and instead agree to submit to binding arbitration.

Arbitration may occur under the auspices of an arbitration tribunal, known as "institutional arbitration," or may be "ad hoc," which means that the parties arrange the proceeding independently. Examples of frequently referenced arbitration tribunals in natural resource contracts include the International Centre for the Settlement of Investment Disputes (ICSID) and the International Court of Arbitration of the International Chamber of Commerce (ICC). In the case of ad hoc arbitration, the contract may state that proceedings must be conducted in accordance with the rules of the United Nations Commission on International Trade Law (UNCITRAL). The location and choice of language for arbitral proceedings will usually be specified in the contract. If the proceedings are held outside of the host country (which is likely), arbitration can be costly and disadvantageous for the host country.

International arbitration is generally considered to be "investor-friendly," meaning that the process favors resource companies. Arbitration panels are not well equipped to consider questions that affect the economic and social well-being of citizens in host countries. These obstacles create a disincentive for a host country to raise contract implementation concerns with a resource company out of fear that it will trigger arbitration proceedings. It is in a host country's interest to insist on dispute settlement through its domestic courts. This approach promotes equal treatment of foreign and domestic companies operating in the host country and provides courts with an opportunity to develop a body of precedent on natural resource contract interpretation and enforcement, which is not the case when disputes are resolved by arbitration panels.

ETHIOPIA - AGRICULTURE LAND LEASE

"In the event of a dispute arising between the lessor and lessee arising out of or in connection with this Land Lease Agreement, both parties will do their utmost to resolve the dispute amicably and to their mutual satisfaction and if they are unable to achieve such a settlement the dispute shall be referred to Ethiopian Federal Court."

These excerpts demonstrate two primary options for dispute resolution - domestic courts and international arbitration. Both contracts require the parties to try and reach an amicable settlement before initiating formal procedures.

AZERBAIJAN - PETROLEUM DEVELOPMENT

"Except as otherwise provided in this Contract, all disputes arising between [the host country's State Oil Company] and any or all of the Contractor Parties, including without limitation, any dispute as to the validity, construction, enforceability or breach of this Contract, which are not amicably resolved by the Parties in accordance with [this Agreement] shall be finally settled before a panel of three (3) arbitrators under the Arbitration Rules of The United Nations Commission on International Trade Law known as UNCITRAL"

GHANA - GOLD ORE MINING

"[The Companies] are incorporated in Ghana and notwithstanding the incorporation in Ghana of any of their successors or assignees, or of any of their other Affiliates, all such entities shall be treated . . . as nationals of the United States of America for purposes of any arbitration . . . except that [the Companies] and any other such entity may, alternatively, elect to be treated instead as a national of any other state of which, under the convention, international law or the law of such state, it is a national."

Under this contract, companies incorporated in the host country may nevertheless elect to be treated as nationals of another country for the purpose of arbitration.

There are additional downsides to arbitration. Arbitral proceedings are generally closed to the public and case documents are kept confidential. Under ICSID rules, for example, members of the public and civil society organizations may not access case documents and must obtain the consent of the host government and the resource company to attend hearings.²⁹ Although recent revisions to the UNCITRAL rules will allow more flexibility for third parties to participate in certain proceedings and grant wider access information, transparency in arbitration remains the exception rather than the rule.³⁰

The contract may allow the resource company to be treated as a national of another country for the purposes of arbitration, even if it is incorporated in the host country. This creates a double standard in which a company can take advantage of domestic incorporation for some purposes, such as obtaining a mining lease, but then assume a different nationality if a dispute arises.

If a natural resource contract is silent as to dispute resolution, it is not safe to assume that a conflict will be resolved in domestic courts. Arbitration provisions also appear in bilateral investment treaties (BITs) and it is a good idea to identify whether there are any BITs between the government of the resource company and the host country. Some investment treaties include rules that govern arbitration proceedings, including provisions allowing third-party (amicus curiae) submissions to be filed, public access to case documents and pleadings, and for proceedings to be open to the public.³¹ BITs and their implications are discussed further in “Investment Treaties.”

If disputes cannot be resolved solely within the host country’s courts, arbitration provisions can be drafted to encourage less formal routes for resolving disputes and to mitigate some of the disadvantages that host countries face. One strategy is to require the parties to attempt to settle differences through negotiation before filing an arbitration notice. Negotiation serves as an “escape valve” that allows the host government to raise performance issues with a resource company more

readily. Alternatively, some contracts include a clause requiring the parties to exhaust domestic remedies as a condition of the host country’s consent to arbitration. To protect the host country’s interests if arbitration proceeds, a contract may specify that proceedings will be conducted in the host country (or a neutral venue within the region) and in a language easily understood by the host country’s arbitral representatives.

LIBERIA - OIL PALM PLANTATION

“Neither Party shall initiate arbitration unless it has (a) issued a letter to the other Party . . . stating that it believes there is a serious dispute that they are considering taking to arbitration, and (b) the Parties have been unable to resolve such dispute within 120 days after the date of such letter. Each party shall use its best efforts to resolve such dispute in a commercial manner during such 120 day period and the arbitrators shall take into account whether the Parties have acted as such in making any award.”

Negotiation may solve contract disputes without the need for, and expense of, arbitration.

ICSID MODEL CLAUSE 13 FOR DISPUTE RESOLUTION

“Before either party hereto institutes an arbitration proceeding under the Convention with respect to a particular dispute, that party must have taken all steps necessary to exhaust . . . [administrative] [and] [judicial] remedies available under the laws of the Host State with respect to that dispute . . . unless the other party hereto waives that requirement in writing.”

This model clause requires the parties to exhaust domestic remedies before initiating arbitration.

LIBERIA - IRON ORE MINING

“Arbitration proceedings conducted pursuant to this Agreement shall be held in Brussels, Belgium or other such place as the Parties hereto may agree and shall be conducted in the English language.”

Arbitration proceedings may be held far away from the host country.

The Role of Investment Treaties

Investment treaties are agreements negotiated between two countries (known as “bilateral investment treaties” or “BITs”) or among several countries. The agreements govern private investment by entities of one country in the other country or countries that are parties to a treaty. For the purposes of this Guide, we will refer to all forms of investment treaties as “BITs.”

Typically, a BIT will require host countries to treat investors from another treaty country in a fair and equitable way, and to provide compensation in cases of expropriation. Some investment treaties prohibit host countries from relaxing or waiving applicable environmental, labor, and safety standards to attract foreign investment. As discussed in the section above on arbitration, BITs may allow investors (including resource companies) to initiate arbitration if they believe the treaty has been breached by the host country.

Many BITs include so-called “umbrella clauses.”³² An umbrella clause requires each country party to a BIT to observe all investment obligations it has entered into with investors from other treaty countries. In other words, a host country’s violation of an investment contract would also be considered a breach of the BIT, and may entitle a resource company to invoke the dispute resolution provisions of the treaty instead of being bound by the dispute resolution terms of the contract. Invoking investment treaty arbitration provisions allows the investor to circumvent the forum selection clause in the contract (if one is included).³³ As explained above, international arbitration is rarely a good option for host governments.

Another area of debate surrounds “most favored nation” clauses, which are considered a core element of BITs.³⁴ Most favored nation treatment in BITs “ensures that a host country extends to the covered foreign investor and its investments, as applicable, treatment that is no less favourable than that which it accords to foreign

Swiss Model Bilateral Investment Treaty (BIT) - Umbrella Clause

“Each Contracting Party shall observe any obligation it has assumed with regard to investments in its territory by investors of the other Contracting Party.”

Umbrella clauses are common in investment treaties.

Sample Most Favored Nation Clause (Schill 2009):

1) Neither Contracting Party shall subject investments in its territory owned or controlled by nationals or companies of the other Contract Party to treatment less favourable than it accords . . . to investments of nationals or companies of any third State.

2) Neither Contracting Party shall in its territory subject nationals or companies of the other Contracting Party, as regards their activity in connection with investments, to treatment less favourable than it accords . . . to nationals or companies of any third State.

Companies may invoke most favored nation clauses to force a host country into arbitration to resolve a contract dispute.

investors of any third country.” Companies invoke these clauses to “borrow” provisions from investment treaties that the host country has entered into with other countries.³⁵ Foreign companies have used these clauses to force host countries into international arbitration over breach of contract disputes when the contract itself has called for disputes to be resolved in domestic courts.³⁶ This practice is referred to as “treaty shopping.”

It is a good idea to determine whether there are any BITs between the home country of the resource company and the host country and, if so, whether the treaty discusses dispute resolution and other key issues that will affect the project. Searchable databases of BITs are maintained by the United Nations Conference on Trade and Development (UNCTAD) and the International Centre for Settlement of Investment Disputes.

Grievance Mechanism

Community advocates and human rights defenders are calling for natural resource contracts to include provisions allowing individuals harmed by a resource company's activities to seek relief through a non-judicial grievance mechanism. Of the many contracts ELAW has reviewed, none have included such a process. Local communities often suffer the most severe impacts during resource exploitation, yet they rarely have the right to seek review of a company's activities or to lodge a complaint.

If a contract includes a grievance mechanism, it may be helpful to compare it to the effectiveness criteria set out in Principle 31 of the UN Guiding Principles on Business and Human Rights:

- (a) Legitimate: enabling trust from the stakeholder groups for whose use they are intended, and being accountable for the fair conduct of grievance processes;
- (b) Accessible: being known to all stakeholder groups for whose use they are intended, and providing adequate assistance for those who may face particular barriers to access;
- (c) Predictable: providing a clear and known procedure with an indicative timeframe for each stage, and clarity on the types of process and outcome available and means of monitoring implementation;
- (d) Equitable: seeking to ensure that aggrieved parties have reasonable access to sources of information, advice and expertise necessary to engage in a grievance process on fair, informed and respectful terms;
- (e) Transparent: keeping parties to a grievance informed about its progress, and providing sufficient information about the mechanism's performance to build confidence in its effectiveness and meet any public interest at stake;
- (f) Rights-compatible: ensuring that outcomes and remedies accord with internationally recognized human rights;
- (g) A source of continuous learning: drawing on relevant measures to identify lessons for improving the mechanism and preventing future grievances and harms;

Operational-level mechanisms should also be:

- (h) Based on engagement and dialogue: consulting the stakeholder groups for whose use they are intended on their design and performance, and focusing on dialogue as the means to address and resolve grievances.

These criteria are a helpful roadmap, as are studies evaluating on-the-ground implementation of operational-level grievance mechanisms.³⁷

Final Thoughts

Far more could be written on natural resource contracts and ELAW intends for this Guide to provide a strong foundation for advocates who are working to improve resource governance. There are exciting opportunities to share knowledge across borders and support communities that are exercising their right to demand better management of non-renewable resources.

ELAW welcomes feedback on the Guide and suggestions for topics that should be covered in the future.

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