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Unpacking Local Content Requirements in the Extractive Sector: What Implications for the Global Trade and Investment Frameworks?

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ABSTRACT

Developing countries are placing an increasing emphasis on the need to derive more benefits from their resource wealth. To do so, a series of reforms have been undertaken to capture more gains from extractive resources. These include, among others, industrial policies to foster better sourcing of local content and job creation, fiscal reforms, and more collaborative partnerships with the extractive industry. This paper focuses on the question of local content in the oil, gas, and mining sectors, particularly the policies put in place to foster its use, and how this fits into the international trade and investment frameworks. It initially unpacks the definition and the scope of local content and the different levels of regulatory requirements used to address the question. It then presents evidence of what has worked (or not) in different contexts and under different conditions, before turning to the global frameworks governing local content requirements (LCRs). It goes on to make some recommendations on how international regulatory frameworks could be improved to fit the needs of countries and companies, and for a more equitable distribution of wealth.

Existing rules regarding some forms of LCRs, as defined in World Trade Organization (WTO) agreements, are quite clear—they are prohibited, disciplined, or allowed. When these measures were found insufficient to address the concerns of investors, countries concluded tighter agreements, in the form of bilateral investment treaties (BITs)/ international investment agreements (IIAs) or preferential trade agreements (PTAs), making LCRs almost impossible to put in place. Yet, this has not prevented the proliferation of new measures. It points to that there are significant weaknesses with the way rules are currently defined and enforced. The first weakness to be addressed regards the definition of LCRs, which is still subject to wide interpretation. Second, while changing WTO rules might take time, it is important to consolidate the role the organisation can play, in particular to reflect on ways to have a more coherent approach, given the multiple bilateral trade and investment agreements signed by its Members. Third, no cases have been brought so far at the WTO Dispute Settlement Body (DSB) on extractives-related LCRs, while BITs and IIAs disputes have extensively focused on the extractive sector. The main challenge is that there is a lack of transparency in arbitral rulings and proceedings that take place under the bilateral dispute mechanisms.

While transparency is necessary, it is not sufficient in itself. Therefore, countries should have space to engage and discuss these issues at a dedicated platform. Participation in this platform should be broadened to regional economic communities (RECs), which have their own experiences on setting guidelines on these issues, and also to other stakeholders, such as other international organizations or representatives of the private sector. LCRs are largely an investment issue and therefore require an investment policy solution. Yet, the continued relevance of the WTO amid the evolving trade and investment system will be conditional on its capacity to adapt to reflect the new realities. One way to address this is to design a variable geometry approach, while ensuring that the concerns of developing countries are addressed. This means allowing space for some countries desiring to move faster on certain issues the ability to do so, keeping the door open for others to join at a later stage, and allowing all others to observe. It is therefore proposed to adopt a carefully designed plurilateral framework on investment, with a set of protocols and rules of operation to guide such negotiations, which will then be agreed to by all Members of the WTO. Alternatively, RECs can play a key role in seeking to establish better rules, essentially for two reasons. Due to their localised mandate, they have a tendency to focus on areas of common interests to their members, such as building regional markets that reflect the specificities of their respective regions and designing rules that fit the development levels of their member countries. While these may create some challenges for the multilateral system, they may also provide a platform to engage on improving the rules using a sequenced approach.

Finally, an improved regulatory environment is conditional upon policy coherence and coordination across international initiatives, whose objectives are to improve the governance of the extractive sector. Numerous initiatives and institutions have been established to address specific issues or to achieve mutual goals. For instance, the Extractive Industries Transparency Initiative (EITI) aims at improving transparency and accountability in the extractives sector. Although not all countries are members of the EITI, this is an important element in the governance of the sector.

CONTENTS

LIST OF ABBREVIATIONS

AMDC	Africa Mineral Development Centre
AMV	Africa Mining Vision
ASCM	Agreement on Subsidies and Countervailing Measures
BITs	bilateral investment treaties
CETA	Canada-EU Trade Agreement
DSB	Dispute Settlement Body
EITI	Extractive Industries Transparency Initiative
EU	European Union
FDI	foreign direct investment
FTA	free trade agreement
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GPA	Agreement on Government Procurement
ICMM	International Council on Mining and Metals
ICSID	International Centre for Settlement of Investment Disputes
IFC	International Finance Corporation
IIAs	international investment agreements
LCA	Local Content Act
ITA	Information Technology Agreement
LCRs	local content requirements
LDCs	least developed countries
MFN	most-favoured nation
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PCA	Permanent Court of Arbitration
PTAs	preferential trade agreements
R&D	research and development
RECs	regional economic communities
RoO	rules of origin
SCC	Stockholm Chamber of Commerce
SDT	special and differential treatment
SMEs	small and medium-sized enterprises
SOEs	state-owned enterprises
TRIMs	Trade-Related Investment Measures
TRIPS	Trade-Related Aspects of Intellectual Property Rights
UNICITRAL	United Nations Commission on International Trade Law
US	United States
WTO	World Trade Organization

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INTRODUCTION

Many resource-rich developing economies have not benefited satisfactorily from the wealth created by their extractive resources. For instance, in the mining sector, it is estimated that while on an average mining foreign direct investment (FDI) accounts for 60 to 90 percent of total FDI, the sector only contributes to between 3 and 20 percent of government revenue, 3 and 10 percent of national income, and only 1 to 2 percent employment in low- and middle-income countries (ICMM 2014). For this reason, developing countries are placing an increasing emphasis on the need to derive more benefits from their resource wealth. To do so, a series of reforms have been undertaken to capture more gains from extractive resources. These include, among others, industrial policies to foster better sourcing of local content and job creation, fiscal reforms, and more collaborative partnerships with the extractive industry.

This paper focuses on the question of local content in the oil, gas, and mining sectors, particularly the policies put in place to foster its use, and how this fits into the international trade and investment frameworks. The paper is structured in four parts. Section 1 unpacks the definition and the scope of local content and the different levels of regulatory requirements used to address the question. Section 2 illustrates, using country case studies, evidence of what has worked (or not) in different contexts and under different conditions. Section 3 looks at the global frameworks governing local content requirements (LCRs). Finally, Section 4 makes some recommendations on how international regulatory frameworks could be improved to fit the needs of countries and companies, and for a more equitable distribution of wealth.

LOCAL CONTENT REQUIREMENTS IN EXTRACTIVE SECTOR: DEFINING THE SCOPE

LCRs are policy tools used by governments to generate economic benefits for the local economy, beyond fiscal benefits. It is not confined only to the extractive sector, and has been, and is still being, widely used, irrespective of countries' income levels.

In resource-based developing economies, there is an increasing tendency to use LCRs as a stimulus to combine the use of locally extracted raw materials with domestically available factors of production (such as labour, locally sourced goods and services, and so on) to create more value in the economy. The rationale behind the use of LCRs is driven by the urge to address common key challenges—(i) the over-reliance on natural resources with respect to their contributions to national income, foreign exchange, and exports; (ii) the paradox of plenty, that is, the unacceptably high prevalence of poverty and inequality amid an abundance of resource riches (Karl 1997); (iii) to mitigate and manage social and political risks due to rising expectations domestically for a better and more equitable distribution of wealth; and (iv) the need to create more job opportunities, given the capital-intensiveness of the extractive sector.

The increasing use of LCRs reflects the changing focus in the policy debate regarding the way in which the extractive sector has traditionally contributed (or not) to a country's development. It, however, calls for finding an economic and political balance in seeking to increase the benefits derived from the extractive sector, while maintaining incentives for investment and the competitiveness of the sector.

While there is little disagreement over the reasons why countries chose to encourage the use of local content, there is no agreed definition of what "local" actually covers, nor is there a full consensus on what "content" should be. It is therefore necessary to unpack the concept. As countries' experiences suggest, policy implications are likely to be different, depending on how the scope and depth of the concept is defined.

This paper makes an important distinction between, on the one hand, local content needed to stimulate forward linkages, through the use of locally available raw materials for enhanced value addition, resource-based industrialisation, and economic diversification, and on the other hand, local content used in the expansion of backward linkages, notably through the use of certain factors of production available domestically as inputs for the extractive industry, essentially to encourage the development of local supply chain providers. The rest of the paper focuses primarily on the latter.

DEFINITION AND COVERAGE

As mentioned, there is no universal definition of what constitutes "local content."[1] It is a multi-dimensional concept whose scope and depth vary substantially. In the extractives context, local content has an intrinsic spatial dimension that needs to be underscored.[2] Narrowly defined, it is viewed as value created around the region that immediately surrounds the extractive sector. In Ghana, Newmont gives more priority to "local local" companies, that is, those businesses situated in the vicinity of mining operations. More broadly defined, it involves the recognition of the "nationality" of capital or location of companies' headquarters. Companies may therefore be considered as local if (a) they are locally based and locally owned; (b) locally based but foreign owned; or (c) locally owned but foreign based. The following criteria are frequently used in various definitions of LCR.

(i) **Ownership**, notably requiring foreign firms to enter into joint ventures with local firms or to open equity to local partners to obtain licences. The aim is to ensure that sectors of national interests are not entirely foreign owned or to help the development of "national champions" through transfer of skills, know-how, or technology. In Norway, ownership of a company is not a determining factor. Brazil now accepts foreign ownership, but prefers partnerships, while Nigeria, Angola, Ghana, and Uganda consider local ownership as determinant.

(ii) **Maximisation of local procurement and preferences given** to sourcing from local companies, as an opportunity to localise supply chains where varying technologies and inputs are needed and used. If competitive, this may have considerable impact on reducing companies' operating costs while at the same time increasing the value that can be captured by local businesses. The International Finance Corporation (IFC; 2011) suggests different criteria for the definition of "local", including the size of local companies involved in the supply chain.[3]

(iii) A percentage of raw materials to be **further transformed** or beneficiated locally, notably through forward linkages. Countries such as Australia, Mongolia, Brazil, Nigeria, Zambia, and more recently South Africa have strong policies in this regard (beyond the scope of this paper).

(iv) **Local employment** at different stages of the value chain and of different levels of competencies. This is often accompanied by requirements to enhance local capabilities of employees and suppliers, through training, skills and expertise development, and transfer of know-how and technology.

(v) Requirements to bring some **level of technology** or perform research and development (R&D) in the country so that companies can perform competitively by using latest state-of-the-art technology, or for local companies to benefit from technology transfer.

TAXONOMY OF LOCAL CONTENT REQUIREMENTS

LCRs are generally articulated in policy frameworks or codified in their related regulatory instruments.[4] As Table 1 shows, these can be classified in two categories. First, policies that impose quantitative requirements on companies in the form of legally binding targets, generally in terms of volume (for example, number of local staff to be employed or number of contracts to be awarded to local suppliers) or value (that is, a percentage of spending on local procurement). They are found in legislations, contracts, licensing agreements, conditions for tender qualifications,[5] and so on and may be binding on companies, pending penalties. Second, policies that are based on qualitative requirements such as transfer of technology or training of staff. These are generally found in policy tools, legislations, and contractual agreements and are less constraining. They may contain loosely defined targets, which are non-binding. It is estimated that more than 90 percent of resource-rich countries have one form of LCR or another, 50 percent of which are of a quantitative nature (McKinsey 2013). Table A in Annex 1 summarises the types and strength of LCR regulations in place in selected resource-rich countries.

To stimulate the implementation of LCRs, governments may also offer other types of incentives to companies.

1 The World Bank (2012) definition for "domestic preference qualification" is based on the percentage of local ownership of the firm. The African Development Bank (AfDB) defines "local firms" based on place of registration, a majority of board members being nationals, and level of shares held by nationals.

2 Essentially for two reasons: (i) the nature of the industry causes the concentration of mineral extraction in a particular location; (ii) the distribution of socio-economic benefits (such as the concentration of clusters) tends to be closely linked to the geographical location of mines.

3 For a good overview of different criteria for defining "local," see IFC (2011).

4 Policy frameworks include guiding principles, national development plans, policy statements, country vision documents, and the like and set the broad orientation that governments want to take in governing the extractive sector.

5 For a thorough review of different types of local content policies, see Tordo et al. (2013).

Horizontal complementary incentives are frequently provided such as tariff exemptions on imports of equipment, fiscal exemptions in support of the development of local industries, or other measures to provide an enabling environment for local businesses to prosper and address constraints such as infrastructure deficits, stiff business climate, access to finance, or skills and capabilities shortages. Additionally, sector-specific industrial policies may be put in place to tackle key market failures that inhibit the overall development of the local economy.[6] In low-income countries, for instance, where there are few buyers (large mining companies) and not enough suppliers (due to weak local enterprises), policies may target identified parts of the supply chain.

Resource-rich countries all have a mix of quantitative and qualitative requirements, the balance being determined by the policy orientation of the government, the levels of development of the countries, and their capacity to implement and monitor these measures. Oil and gas companies tend to be subject to a higher level of quantitative regulations than mining industries, mainly as a result of the way in which contracts are defined. Countries generally tend to relax stringent numerical obligations as they move to higher levels of income, as their mineral sectors get more integrated in the global economy, or as their national suppliers become more competitive.

6 These may take the form of market failures associated with exports and FDI (use of subsidies and tax breaks); coordination failures at the level of specific sectors (use of competitiveness strategies); asymmetry of information; insufficient local capacity in R&D and innovation (support to innovation incubators), and so on.

TABLE 1:

Taxonomy of Local Content Requirements and Application in Selected Countries

Source: Adapted from Jojarth (2015).

Types of policies	Type of measures	Examples of measures	Examples of countries applying such measures
Quantitative requirements	Quotas based on numbers	Number of local population employed	Angola: At least 70 percent work force to be Angolan nationals. Nigeria: Companies are required to employ only Nigerians in junior and intermediate positions.[7] Kazakhstan: 95 percent minimum requirement for employment of nationals.
		Certain categories of procurement reserved for locals	Angola: For logistics and catering. South Africa: Procurement targets around black economic empowerment, for example, 40 percent on local procurement expenditure, 50 percent on local consumable goods, and 70 percent on local services. Nigeria: Exclusive consideration (that is, 100 percent) to Nigerian indigenous service companies,[8] provided local company has capacity to execute.
		Specific content target for certain products	Nigeria: The Local Content Act (LCA) provides for categories of activities (for example, floating products; storage and offloading vessels; steel plates) to be locally procured. LCR targets for some goods and services set between 80 percent and 100 percent.[9] Companies may be subject to penalties for non-compliance, such as cancellation of projects and fine equivalent to 5 percent of project value.[10]
	Quotas based on values	Technological transfer	Norway: Requirement to conduct at least 50 percent of research for technology in partnership with local institutions.
		Percentage of local procurement spending going to local companies	Indonesia: Companies to procure locally at least 35 percent of services for contracts > US$100,000
		Local suppliers to benefit from percentage preferential price	Kazakhstan: Procuring entities to reduce price of bids by 20 percent for local suppliers.
		State participation to obtain licenses	Brazil: Target set at 50 percent for onshore projects; 51 percent for offshore in shallow water; 37 percent for deep water projects.

Types of policies	Type of measures	Examples of measures	Examples of countries applying such measures
Qualitative requirements	Reporting and justification	Companies must report and justify hiring foreign labour or sourcing inputs from abroad	Angola: Oil companies must submit an "Angolanisation" plan to the ministry of petroleum annually, detailing how they plan to achieve their targets. Zambia: Companies to submit plan, with indications of estimated staff requirements (local and expatriates), training, and creation of a local business development programme. South Africa: Companies to report annually through a scorecard local content, employment, and company ownership to historically disadvantaged groups. Nigeria: LCA require investor to submit annual knowledge transfer plans; companies to submit an "employment succession plan" on how to "Nigerianise" such positions within a four-year period.
	Information sharing	Companies must advertise vacancies or publish tenders and procurement opportunities	Brazil: Database set up to facilitate business linkages. Chile: Information sharing, suppliers' registration and certification.
	Capability and knowledge development	Companies to train local staff or train and certify local suppliers	Norway: Upgrading capabilities of local services suppliers and industrial clusters. Brazil and Chile: Creation of suppliers development programme for small and medium-sized enterprises (SMEs); partnership with foreign firms to promote local suppliers. Mozambique: Development of local know-how required, through employment and technical training, with preference for populations living around mines.
	R&D contribution and transfer of technology	Companies commit to transfer technology to local firms Companies required to carry out some levels of R&D	Brazil: Licensing determined by R&D contribution and technological transfer; partnership with foreign firms to foster technological transfer. Norway: Partnership with multinationals to transfer technology, acquire skills, and conduct R&D.
	Preferential treatment	Companies must hire local staff or source inputs locally if available on a competitive basis	Mozambique (petroleum), Brazil, Norway: Require operator to give preference to local suppliers only if competitive on the basis of quality, price, and availability. Zambia: Maximum preferences sought for local entrepreneurs, no targets fixed. Nigeria: Preference for local suppliers in tendering process, if they have capacity and provided value of bids < 10 percent of lowest bidder. Some specific manufacturing processes such as welding and fabrication should take place in Nigeria (equivalent to prohibiting imports of fabricated products).

7 These may take the form of market failures associated with exports and FDI (use of subsidies and tax breaks); coordination failures at the level of specific sectors (use of competitiveness strategies); asymmetry of information; insufficient local capacity in R&D and innovation (support to innovation incubators), and so on.

8 Meaning Nigerian based, which can demonstrate ownership of equipment, and employing Nigerian personnel.

9 Schedule A of the Nigerian Content Development Act specifies the level of Nigerian Content to be achieved per activity or input used by operators in the oil and gas sector. For goods and services such as steel pipes and plates, cables, valves, cement, audit services and geographical survey services, the local content requirement is 100 percent (G/TRIMS/W/142).

10 See G/TRIMS/W/89.

LOCAL CONTENT REQUIREMENTS IN PRACTICE

It is difficult to make an overall assessment of the impact of LCRs in resource-rich countries, in part due to lack of empirical evidence but also because experiences vary significantly across countries. For instance, despite extensive use of LCRs, many resource-rich countries continue to attract significant levels of FDI (Nikièma 2014), although there are many cases where measures have failed to achieve their stated objectives due to a lack of capacity to implement, manage, and monitor LCRs.

COUNTRIES' EXPERIENCES IN USING LCRS

Countries that have been successful in using LCRs have all used a combination of quantitative and qualitative measures, based on their capacity to deliver, while ensuring a fair balance between their economic objectives and the viability of investments. Table 1 provides an illustration of measures taken by a number of countries. Norway, for instance, enacted regulations that had clear targets and sunset clauses for quantitative regulations. Initially, foreign companies were required to give preferences to local firms, provided the latter were competitive on the basis of price, quality, and delivery. This measure was temporary, based on performance and was later relaxed. It led to the creation a national champion, Statoil, and world-class global suppliers. Today, the domestic supply chain provides between 50 to 60 percent of capital inputs, 80 percent of operational and maintenance inputs, and exports 46 percent of its sales (Word Bank 2012).

Quantitative LCRs have been mainly used to foster local procurement, employment of local staff, technology transfer, or set up joint ventures. In Brazil, use of local content was a key criterion for the award of petroleum rights (Cosbey 2015). Due to supportive measures by the government to drive the development of local capacity and the key role of the national champion, Petrobras, commitments to local content increased from 25 percent to 80 percent in a decade (Sigam and Garcia: 2012). The corruption scandal that shook Petrobras in 2015, including on the implementation of its LCRs,[11] is expected to see a major overhaul towards liberalization of policies governing the procurement of equipment and services domestically. In Nigeria, in contrast, despite strict quantitative targets for employment and local sourcing, satisfactory results in practice have taken time to materialise due to the insufficient capacity of local suppliers to meet targets or the unavailability of sufficient skills to be absorbed by the industry. A number of Nigerian companies have, however, started to internationalise themselves and are now operating in other African countries. But given the potential of Nigeria, this remains largely insufficient.

While quantitative LCRs may work, they are in themselves not sufficient to stimulate the development of local suppliers, employment of local staff, transfer of technology, or creation of national champions. They need to be accompanied by other policies. For instance, Norway also privileged capability and knowledge development, supported by public investment in R&D and developed strategic collaborative partnerships with foreign companies to develop technology and acquire skills. Similarly, Malaysia and Chile simultaneously established strong partnerships with foreign firms, while at the same time supporting local suppliers (and small and medium-sized enterprises [SMEs] in the case of Brazil) by identifying gaps and facilitating their interaction with foreign firms. In Brazil, oil and gas field operators are required to pay 1 percent of their gross revenue to the government, which is then invested in R&D schemes in the country.

Others have opted to finance skills development and training by seeking financial contributions from foreign companies or by putting aside a share of royalties. In Nigeria, 1 percent of the total value of contracts awarded in the upstream sector goes to a Content Development Fund (KPMG 2010) to support training and business support services. South Africa and Malaysia have established skills development funds where extractive industries have an obligation to contribute. In Brazil, a share of royalties goes to the Oil and Gas Sectoral Fund to support specialised training and capacity building (Cosbey 2015).

Initiatives led by foreign companies, development agencies (such as the IFC), and chambers of commerce are an essential element in the success of LCRs. For instance, a world-class supplier programme was set up in Chile by BHP Billiton to stimulate the emergence of reliable and competitive local suppliers and build a knowledge-based mining sector. This programme was distinctive on several fronts. The company identified and presented an operational challenge to suppliers instead of simply requesting existing, standardised solutions. This created a demand for innovation, which built a better alignment with market needs and improved the use of resources, and therefore created a secured and tailor-made market for suppliers. In Ghana, inspired by its experience in Peru, Newmont, in partnership with the IFC and the Chamber of Mines, developed a programme to support the development of local businesses to supply goods and

11 The so-called Carwash scandal—in which some of Brazil's largest contractors and oil suppliers are currently facing allegations that they formed a cartel and paid kickbacks to Petrobras executives and politicians—has brought to light the downside of an excessive dependence on local industries, as this encouraged collusive behaviour.

services, and upscale the capacity of business associations to provide sustainable business support, training, and other services to the local business community. This multi-stakeholder programme led to the creation of an ecosystem of business opportunities around the mining area, including in non-mining activities, such as agriculture. In South Africa, Anglo American launched a Small Business Initiative to provide business opportunities for SMEs, in particular for historically disadvantaged populations. Mozambique also has a good track record of collaborative partnerships with the private sector to scale up business linkage programmes. For instance, the Mozal aluminium smelter was designed and implemented in partnership with a range of stakeholders to stimulate and strengthen local business capacities and enable small enterprises to compete for contracts at different stages, from construction to ongoing operation.

KEY LESSONS FROM LCR EXPERIENCES

A few lessons can be drawn from the experiences of countries that have implemented LCRs. First, policymakers need to ensure that the objectives of LCRs are clear and that they are implemented and monitored in a way that they create fully capable and competitive local suppliers and not become obstacles to the development and competiveness of industries. When local content policies were well defined and monitored in a pragmatic manner, as was the case in Norway, Chile or Brazil (including quantitative measures), they were found to be more successful.

Second, while mandatory quantitative requirements can work, quotas should not be fixed at a level that local suppliers are not able to deliver. In addition, they should be temporary, performance-based, and should be phased out as industries become competitive. Functioning and effective LCRs require a holistic approach to industrial policy. This implies that LCRs need to be accompanied by support to build the capacity of suppliers, and address skills gaps or financial constraints, as in the case of SMEs. Partnerships with the private sector are equally key to develop capacity.

Third, LCR ambitions need to be realistic and implementable by the extractive sector. They must be flexible enough to be able to adapt to changing situations. Norway phased out certain performance-based requirements as its industries became globally competitive. They need to be able to assume some potentially politically difficult trade-offs. For example, Petrobas in Brazil skimmed 20,000 jobs (one-third of its headcount) during the restructuring process in 1997 but gained in efficiency and sophistication (WTI 2013).

Fourth, successful experiences suggest that it is important to ensure a balance between quantitative and qualitative measures based on how far those measures can be monitored or implemented. For example, a legally binding quota for technology transfer may be difficult to monitor because it may not be possible for governments to identify, in the first place, which technology companies should use (Cosbey 2015). In the case of joint venture requirements, unless there is a business case to do so, there is a risk of creating a "forced marriage" that will fail if there is no trust, no shared objective, and no complementarity (Cosbey and Mann 2014). Countries were most successful when local content development was conducted through strategic collaborative partnerships with companies.

Finally, the importance of innovation, R&D, upgrading capabilities, and technology transfer should not be underestimated. These are essential complementary policies to build competitive local suppliers and efficient providers.

REGULATORY FRAMEWORKS GOVERNING LCRS

By their nature, LCRs emphasise preferential treatments for local suppliers vis-à-vis foreign goods and services providers and are therefore viewed by many as protectionist measures (Hufbauer et al. 2013). From a development perspective, they can be a tool to achieve certain economic and non-economic goals such as developing local supply chains, expertise, ensuring technological transfer, or achieving better social outcomes. From an international trade perspective, countries, however, need to be prudent to ensure that their measures do not contravene commitments at the bilateral or multilateral level. The fact that there is no agreed definition of LCRs and that their scope is very broad suggests that measures are likely to be subject to a wide range of disciplines.

RELEVANT PROVISIONS ON LCRS IN TRADE AND INVESTMENT AGREEMENTS

In the multilateral trading system under the World Trade Organization (WTO), the most relevant agreements on compliance of LCRs are the General Agreement on Tariffs and Trade (GATT), the Agreement on Trade-Related Investment Measures (TRIMs),[12] the General Agreement

12 The TRIMs Agreement clarifies existing rules contained in Articles III (National Treatment) and XI (Prohibition on Quantitative Restrictions) of the GATT, 1994.

on Trade in Services (GATS), the Agreement on Subsidies and Countervailing Measures (ASCM), and the Agreement on Government Procurement (GPA). While the GATT, the TRIMs, and the GATS apply to all WTO Members, the GPA is a plurilateral agreement, which binds only its 43 signatory members.[13] However, in many cases, LCRs are not only trade related, but essentially investment related. Therefore, international and bilateral investment agreements also largely regulate the extent to which signatory countries can use (or not) certain measures to oblige foreigners to use more local content. This section summarises the various legal provisions contained in trade and investment agreements that could potentially impact the legality of the use of LCRs.

RELEVANT DISCIPLINES IN WTO AGREEMENTS

The national treatment requirement, as provided for in Article III of the GATT, establishes a strong legal basis regarding the treatment accorded to local goods providers compared to foreign producers. The consistency of LCRs will, therefore, be defined according to the provisions of Article III:4. In addition, Article III:5 of the GATT prohibits quantitative regulations pertaining to the "processing or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources." Article III:8, however, excludes government procurement from the application of the provision of national treatment, which is subject to the obligations under the GPA for those countries that are parties to it. Article XI.1 of the GATT prohibits the use of quantitative restrictions on imports and exports through quotas, licenses, and other measures.

Article XVII of the GATT 1994 relating to State Trading Enterprises requires state-owned enterprises (SOEs) to operate in accordance with the principles of non-discrimination and requires that their purchases and sales be conducted "in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity … to compete for participation in such purchases or sales." This is particularly relevant because in many resource-rich countries SOEs play a significant role by engaging in commercial operations. A number of LCR provisions affecting the oil sector are relevant to SOEs and are therefore expected to fall within the provisions of Article XVII of GATT 1994. This provision, however, does not regulate the obligations of foreign companies to enter into joint ventures with SOEs, as required, for example, in the 2014 law in Mozambique or in Angola.

The TRIMs complements Article III of the GATT regarding treatment accorded to investment. Host countries are required to provide no less favourable treatment to foreign investors compared to what they provide to their national investors. The TRIMs provide an illustrative list of potential measures that may contravene the Agreement. These are assessed on two considerations:

1. Investment measures must be trade-related (although goods only);

2. Measures to fall within the scope of the illustrative list, that is, must be "mandatory or enforceable under domestic law or under administrative rulings or compliance with which is necessary to obtain an advantage", and which

   a. Require the purchase of a product of domestic origin, whether of specific products or in specific amounts; or

   b. Limit the purchase (in value or volume terms) of imported products.

The TRIMs agreement prohibits the use of LCRs that requires a specific percentage or quantitative target of local goods purchases by companies, and has trade-balancing requirements that restrict the volume or value that a company can import to an amount related to the level of products it exports. Finally, the TRIMs proscribes any use of export restrictions or bans, such as those adopted by Indonesia in 2012 to implement a 2009 law on unprocessed metals and non-metallic minerals to ensure smelting and downstream beneficiation unless mining companies submit plans for smelter construction. Table 2 highlights some examples of TRIMs-related measures in place in a selected number of resource-rich countries.

The ASCM is relevant to LCRs in two cases—(i) if measures to support local content are used as export subsidies; or (ii) if they are subject to the use of local products over imports, as provided by Article 3.1 (b) of the agreement.[14] Government policies supporting R&D and innovation are, however,

13 The GPA consists of 15 parties (Armenia, Canada, European Union [EU}, Hong Kong, Iceland, Israel, Japan, Republic of Korea, Lichtenstein, Netherlands for Aruba, Norway, Singapore, Switzerland, Chinese Taipei, and the US) covering 43 WTO Members (counting the EU and its 28 member states, all of which are covered by the Agreement as one party). Another 28 WTO Members and four international organizations participate in the GPA Committee as observers. Ten of these members (China, New Zealand, Montenegro, Albania, Georgia, Jordan, Kyrgyz Republic, Moldova, Oman, and Ukraine) with observer status are in the process of acceding to the Agreement.

14 Article 3.1 (b) of the ASCM Agreement in particular prohibits the use of "subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods."

considered as non-actionable, as provided by Article 8.2,[15] and therefore active industrial policies can be designed to encourage companies to innovate in new products and new production processes. By permitting subsidies to cover up to 75 percent of industrial research costs, governments have considerable flexibility to influence the technology development of companies.

LCRs are of concern to service providers. In this regard, the GATS contains provisions regarding market access and national treatment that may affect foreign suppliers (Article XVI).[16] For example, in 2010, in an effort to foster the development of its banking sector, Angola required oil companies operating onshore to use domestic banks to process their transactions. Other countries require foreign companies to give preference to employment of local staff, to limit employment of foreign staff, or to submit plans on how they intend to increase local labour participation. Nigeria, for example, requires that junior or intermediate positions be reserved exclusively for Nigerians. Similar to the GATT, government procurement (Article XIII) is excluded from the scope of the GATS. One main limitation of the GATS, however, is that its disciplines only apply to those services sectors that a WTO Member has included in its schedule of commitments. Most developing countries have made few commitments and therefore have more flexibility to apply LCRs to service suppliers.

The GPA entered into force in 1996 and its schedules were revised in 2012.[17] It is a plurilateral agreement that applies only to the 43 signatories that have acceded to it, although all WTO Members are eligible to join.[18] The objective of the GPA was to respond to political pressures to address discriminatory treatment in favour of local suppliers for government-transacted businesses, in particular in tendering procedures for contracts above a certain financial threshold.[19] The major cornerstone is non-discrimination between local and foreign suppliers. The use of offsets is explicitly excluded from the GPA but developing countries can benefit from certain flexibilities if they join it.

15 Article 8.2 of the ASCM states, "Notwithstanding the provisions of Parts III and V, the following subsidies shall be non-actionable: (a) assistance for research activities conducted by firms or by higher education or research establishments on a contract basis with firms if: the assistance covers not more than 75 percent of the costs of industrial research or 50 percent of the costs of pre-competitive development activity; and provided that such assistance is limited exclusively; to (i) costs of personnel (researchers, technicians and other supporting staff employed exclusively in the research activity); (ii) costs of instruments, equipment, land and buildings used exclusively and permanently (except when disposed of on a commercial basis) for the research activity; (iii) costs of consultancy and equivalent services used exclusively for the research activity, including bought in research, technical knowledge, patents, etc.; (iv) additional overhead costs incurred directly as a result of the research activity; (v) other running costs (such as those of materials, supplies and the like), incurred directly as a result of the research activity."

16 Article XVI covers investment measures related to services relevant to local content, such as (i) requirements to use domestic service suppliers; (ii) limitations on the number of service suppliers; (iii) limitations on the total value of service transactions or assets; (iv) limitations on the total number of service operations or quantity of service output; (v) limitations on the total number of natural persons permitted; (vi) restrictions on or requirements for certain types of legal entities (for example, joint venture requirements); and (vii) imposition of domestic equity.

17 The coverage Schedule of the Revised GPA can be found at http://www.wto.org/english/tratop_e/gproc_e/gp_app_agree_e.htm#revisedGPA.

18 At present, ten WTO Members are in the process of acceding. These are China, New Zealand, Montenegro, Albania, Georgia, Jordan, Kyrgyz Republic, Moldova, Oman, and Ukraine. Five other WTO Members have undertaken commitments in their accession protocols to initiate accession to the GPA. They are the former Yugoslav Republic of Macedonia, Mongolia, the Russian Federation, Saudi Arabia, and Tajikistan.

19 While the GATT and the TRIMs are based on a positive list approach (countries agree to liberalize only those sectors that are put forward in their respective list of commitments), the GPA is based on a negative list approach, which means that rules apply to all sectors except those that the countries chose not to include in the agreement, as reflected in their respective schedules of commitments.

TABLE 2:

Examples of TRIMs-related Measures related to the Extractive Sector

Measures	Specific details	Countries
Local procurement	Imposed use of certain amount of local inputs in production	Nigeria
Trade-balancing requirements	Limit purchase of imported goods per volume or value of local product	Nigeria
Manufacturing requirements	Certain products are required to be manufactured locally	Ghana, Indonesia, Nigeria, South Africa
Technological requirements	Require specified technology to be transferred on non-commercial terms and types of R&D to be conducted locally	Chile, Brazil, Malaysia, Mozambique, Norway, South Africa
Licensing requirements	Require investors to give preference to local suppliers	Brazil, Zambia, Ghana, Mozambique, Nigeria
Local equity requirements	Specify percentage of a firm's equity to be held by local investors	Mozambique, Nigeria

In their recent reforms, several resource-rich countries have inscribed mandatory LCRs in their contracts or legal frameworks, sometimes in the form of explicit thresholds, or in the form of conditions of operation, or as part of bidding evaluation guidelines with preferential considerations for local suppliers. Countries such as Nigeria, Indonesia, South Africa, or Brazil have enacted such measures, despite varying scope and compliance enforcements. Table 3 gives a comprehensive overview of cases where LCRs and WTO rules overlap. Some of those measures (in particularly those that are both mandatory and quota related) are clearly in breach of WTO rules. Some measures, despite their non-mandatory nature, may fall within the scope of the rules if they are deemed "necessary to obtain an advantage." Others simply fall outside the scope of the TRIMs and therefore are not in breach of the rules. Table C in Annex 1 summarises the relevant WTO provisions that apply to LCRs.

It is interesting to note that despite the relatively clear WTO rules regarding the (in)compatibility of mandatory and quantitative LCRs and despite the proliferation of such measures in particular in resource-rich countries, so far only two cases related to TRIMs have been brought under the dispute settlement mechanism (the Indonesia – Automobiles and Canada – Feed-In Tariff cases). None of them relate to the extractive sector. This is probably because governments may be reluctant to challenge tools that they themselves have used or continue to use. Or it may be because investors do not find that the WTO dispute mechanism responds sufficiently to their concerns, in particular as it does not confer monetary compensation and therefore may not repair losses due to contract cancellation or penalties incurred. In contrast, most disputes regarding LCRs in extractives have been brought by investors against host countries under dispute mechanisms of bilateral investment treaties (BITs),[20] as discussed in the next section.

LCRs, bilateral investment, and other preferential trade agreements

LCRs are strongly present in various BITs and in investment chapters of preferential trade agreements (PTAs) (Cosbey 2015). The objectives are to (i) bridge some of the gaps regarding investment and investors' protection in the WTO rule books; (ii) cover areas that fall outside the scope of the WTO; and (iii) define new sets of rules best adapted to the changing nature of the global trading system, as economies and production structures are increasingly integrated.

The 1994 North American Free Trade Agreement (NAFTA) was quite a pioneer in introducing strong disciplines regarding LCRs imposed on investors. Since then, a number of Organisation for Economic Co-operation and Development (OECD) countries have included similar provisions, though with varying scope and disciplines. However, most agreements between developing countries do not address performance/LCRs.

The coverage of disciplines under BITs varies widely and can be grouped in four main categories (for a detailed analysis, see Nikièma 2014).

1. Non-binding clauses that only encourage countries not to use LCRs. This is mostly found in "old-generation" BITs signed by developed countries.

2. Those that make a cross-reference to the TRIMS, making the latter compulsory under the BIT. These are the most common clauses that refer to LCRs. It may seem trivial but this is a critical element because with such a reference the TRIMS becomes subject to the investors-state dispute mechanism of the BIT.

3. TRIMS "plus" clauses that discipline LCRs after the investment has been made. The disciplines can go beyond what the TRIMS requires and can prohibit, condition, or discourage LCRs in the form of technology transfer, employment conditions, joint ventures, local procurement, domestic equity participation, and so on.

4. TRIMS "plus" clauses that cover pre-establishment as well as post-establishment phases. This is a significant addition to WTO provisions, as it also disciplines the conditions of entry of an investor (such as establishment, acquisition, or expansion), including granting most-favoured nation (MFN) or national treatment during the pre-establishment phase. This can constrain host countries in seeking joint ventures or equity participation. This clause is common in post-NAFTA agreements by the United States (US) and Canada, and now since the Canada-EU free trade agreement (FTA), increasingly in the EU's investment chapters in recent FTAs.

It is estimated that there are some 3,000 BITs in force globally (Cosbey and Mann 2014). One of their strengths lies in their relatively more effective complaint mechanism, compared to the WTO, viewed from an investor's perspective. While the WTO dispute settlement system provides a predictable state-to-state level mechanism, in BITs, investors can challenge states directly. This tends to increase the frequency of arbitration and cases (Nikièma 2014). Today, investor-state disputes are the most widely used mechanisms in international trade law to address LCR disputes. Of the 600 known cases of investor-state arbitration, 25 percent cover cases related to the mining, oil, and gas sectors (Cosbey and Mann 2014), although not all of them relate to LCRs. Contrary to the dispute mechanism at the WTO, arbitral award cannot be reversed and financial compensation can be significant for damage claimed.

20 These are the International Centre for Settlement of Investment Disputes (ICSID), the United Nations Commission on International Trade Law (UNICITRAL), the Permanent Court of Arbitration (PCA), and the Arbitration Institute of the Stockholm Chamber of Commerce (SCC).

TABLE 3:

Selected Countries' Measures on LCRs and Potential Relationship with WTO Provisions

Sources: Author's compilation, Trade Monitoring Database, WTO (Feb. 2015).
Note: The table highlights where LCRs and WTO agreements intersect. However, it does not say whether these measures are compatible or not with the rules. This would require a more in-depth analysis of each legislation in detail.

	Local procurement requirements (including goods, services and employment)						Ownership requirements
	GATT III	GATT XI	TRIMS	ASCM	GATS	TRIPS	Art XVII (SOE)
Australia: Buy Australia at Home and Abroad scheme: Funding in budget to reinforce local firms competitive position in procurement bids (to maximize returns on the resource boom by linking Australian suppliers to large resource projects)				+			
Brazil: Buy Brazil Act (2010): clause in government procurement (up to 25 percent preference for goods and services produced in Brazil)		+	+		+		
50 percent state participation in production licences							+
Minimum LCRs from indigenous suppliers: 70 percent for onshore, 51 percent for offshore in shallow water of up to 100 metres, and 37 percent for deep water between 100 and 400 metres		+	+				
Licensing is determined by R&D contributions and technology transfer from foreign-owned oil companies	+		+				
Ghana : Entities in the petroleum industry must submit local content plans regarding the use of local goods and services and the transfer of advanced technologies and skills to the Ghana National Petroleum Company (GNPC)			+		+	+	
Indonesia: 2008 mining law, promoting local processing of raw materials (mineral, including bauxite and nickel, and coal). Regulation does not prohibit exports of these products	+		+				
Decree prioritizing the supply of mineral coal to domestic needs (to manage and prevent shortages)	+		+		+		
Regulation requiring local and foreign bidders for energy service contracts to use a minimum of 35 percent domestic content in their operations			+		+		
Threshold of mining and coal production prioritizing supply to domestic needs at a benchmark price in accordance with effective price in the international market (to manage shortage)	+	+					
Requirement to prioritize use of domestic goods and services in investment in energy sector			+				
Industry law adopted in December 2013 increasing state ownership in strategic industries and the use of domestically produced goods and services. Law includes export ban requirements on certain raw materials		+					+

TABLE 3 CONTINUED:

	Local procurement requirements (including goods, services and employment)						Ownership requirements
	GATT III	GATT XI	TRIMS	ASCM	GATS	TRIPS	Art XVII (SOE)
Export licensing introduced for some minerals and metals		+					
Limits imposed on foreign participation in energy and mineral resources sectors and production control by government			+		+		
Renegotiations of contract of work and restrictions on foreign employees					+		
Mozambique – Mining: LCRs for goods and services	+		+		+		
Requirements for operators to give preference to local goods and services (provided they meet price, quality, and delivery standards)	+		+		+		
Requirements to provide employment and technical training to local staff					+		
Mozambique – Petroleum: Requirement to allocate 25 percent of petroleum production to domestic market			+		+		
Increased ownership of SOE in concessions							+
SOE to take lead role in production, marketing, sales							+
Local procurement requirements for goods and services	+		+		+		
Requirements for joint ventures to supply goods and services					+		
Requirements for operators to give preference to local goods and services (provided they meet price, quality, and delivery standards)	+		+		+		
Requirements to provide employment and technical training to local staff					+		
Mineral processing in Mozambique	+	+	+				
Nigeria : LCR obligations for the oil and gas sector 10 percent preference for local tenders	+	+	+		+		
Schedule A of Nigeria Oil and Gas Content Development of 2010 specifies level of LC to be achieved per activity		+	+				
All companies and operators are required to employ only Nigerians in junior and intermediate positions and only 5 percent of expats in management					+		
Equity shares to be held by Nigerian companies			+		+		
Requirements to give first consideration for goods manufactured in Nigeria	+		+				
Fiscal and tax incentives for companies that establish operations in Nigeria to carry out production, manufacturing, or production of services				+			
South Africa : Preferential procurement regulations granting preferences for local products and preferences under the Broad-Based Black Economic Empowerment scheme		+	+		+		
Policy directives on exports of ferrous and non-ferrous wastes and scrap metals		+					
Zambia: Maximum preference to be given to local procurement	+		+		+		
Joint ventures and partnerships with local companies					+		

BITs disputes are generally costly and the balance of power has often tilted in favour of investors, given their extensive legal expertise. For this reason, many resource-rich countries have recently started to review their BITs, even taking steps to unilaterally denounce them and replace them with other forms of legal frameworks that seek to provide similar levels of protection to investors, but diminish the risk of state-business disputes. One of the challenges though is that some protections provided for in BITs may continue to exist even beyond the legal life of the agreements.

PTAs that have strong investment chapters are increasingly including LCR disciplines. The recent Canada-EU Trade Agreement (CETA) is a case in point. This trend is expected to continue in mega-regional trade negotiations with a view to define new sets of rules to level the playing field for investors to remain competitive in an increasingly interconnected environment.

DEVELOPING COUNTRIES: SPECIAL AND DIFFERENTIAL TREATMENT AND POLICY SPACE

The GATT, the TRIMs, and the GATS all contain various flexibilities for developing countries under special and differential treatment (SDT) provisions.[21] These include longer time periods to implement agreements and commitments and special provisions to allow countries to temporarily derogate from some commitments for development needs. In total, there are 139 SDT provisions in WTO Agreements for developing countries.[22]

Developing countries are permitted to retain TRIMs under Article 4 on a temporary basis to the extent that the measures are consistent with the specific derogations permitted under Article XVIII of the GATT 1994 by virtue of economic development needs and subject to notification to the General Council.[23] The provision allowing developing countries longer transitional time periods has expired.

However, there exist flexible provisions in other WTO Agreements, which may be relevant to developing countries and in particular to low-income countries, granting them more policy space to develop their local industries. For instance, there exists flexibility to encourage foreign suppliers to assist in technology transfers and training through offset transactions. Least developed countries (LDCs), in particular, benefit from added flexibilities and may be exempted from applying certain provisions due to their specific economic conditions, notably under numerous exceptions provisions in different agreements (such as the ASCM), which take into account their special circumstances. They are under SDT provisions allowed to derogate from the application of some provisions of the agreements, and under special exemptions or waivers, provided longer transitional periods to implement certain agreements, such as the Trade-Related Aspects of Intellectual Property Rights (TRIPS) (Ramdoo 2015).

The GATS has a different approach to SDT. It addresses the concerns and needs of developing countries by providing flexibility on an individual basis, which is reflected in numerous provisions of the Agreement. In addition, developing countries are allowed to undertake liberalization commitments in a manner consistent with their development needs, which are negotiated on a case-by-case basis.

BITs also contain exceptions and reservations on LCR disciplines. Their scope is significantly narrower than WTO provisions in that they are not related to development objectives but rather to environmental requirements and health safety concerns.

LOOKING FORWARD: REGULATE MORE OR REGULATE BETTER?

Multiplying national initiatives to foster the development of linkages and greater participation of local actors through LCRs confirm a general trend. Resource-rich—but otherwise poor—economies are setting their priorities to get more benefits from their natural endowments and they see local content policies are a necessary trade-off between short-term efficiency and long-term economic development (Tordo 2011).

Yet, from an international trade and investment perspective, there are a number of legal constraints on how far countries can effectively go in putting in place and implementing such measures. These underline the importance of exploring effective flexibilities and alternatives but also coherent policy options with a range of stakeholders to have a balanced and pragmatic approach, which makes economic sense, both for governments that need to stimulate job creation and

21 For a comprehensive analysis of industrial disciplines and the WTO, see "Report of the First Expert Group Meeting on Reinvigorating Manufacturing: New Industrial Policy and the Trading System"; www.e15initiative.org.

22 See Note by the WTO Secretariat for the Committee on Trade and Development on Special and Differential Treatment in WTO Agreements and Decisions, 14 June 2013, WT/COMTD/W/196.

23 Article 4 of the TRIMs allows developing countries to derogate temporarily from TRIMs obligations, as provided for by Article XVIII of the GATT 1994 and related to WTO provisions of safeguard measures for balance of payments difficulties.

industrial development and for businesses that need to be able to operate efficiently and competitively in a stable and conducive environment. The approach will be viable if it makes political sense as governments are pressured domestically to show results. This is a tough task and there is no blueprint. Rather, initiatives will have to be country- and context-specific, as various successes and failures have demonstrated.

This section makes some concrete suggestions on what could potentially and realistically be done, at different levels and by different stakeholders. The objective of this section is not only to argue for more regulations but also for better regulations to ensure fair practices that are compatible with the rules, while meeting both the development objectives of resource-rich countries and the interests of extractive industries.

MAKING THE SYSTEM CLEARER: ENHANCING TRANSPARENCY, PREDICTABILITY, AND FLEXIBILITY

Existing rules regarding some forms of LCRs, as defined in WTO agreements, are quite clear—they are prohibited, disciplined, or allowed. When these measures were found insufficient to address the concerns of investors, countries concluded tighter agreements, in the form of BITs/ international investment agreements (IIAs) or preferential trade agreements (PTAs), making LCRs almost impossible to put in place. Yet, this has not prevented the proliferation of new measures. It points to that there are significant weaknesses with the way rules are currently defined and enforced.

Transparency

The first weakness to be addressed regards the definition of LCRs, which is still subject to wide interpretation. It is therefore proposed to develop an understanding within the legal text on LCRs that sets out clearly the contours of a common definition. This could be an Annex to the TRIMs agreement.

Second, while changing WTO rules might take time, it is important to consolidate the role the organisation can play, in particular to reflect on ways to have a more coherent approach, given the multiple bilateral trade and investment agreements signed by its Members. WTO transparency mechanisms (such as notification obligations, reviews in specific committees, and the trade policy review mechanism) are powerful information tools to monitor the evolution of the trade and investment frameworks in countries. Some information is available in the Trade Monitoring Database (TMD).[24] But this needs to go one step further. The TMD should be complemented with an online forum where members as well as industries can access information regarding policy instruments and measures that require LCRs.

Third, no cases have been brought so far at the WTO Dispute Settlement Body (DSB) on extractives-related LCRs, while BITs and IIAs disputes have extensively focused on the extractive sector. The main challenge is that there is a lack of transparency in arbitral rulings and proceedings that take place under the bilateral dispute mechanisms. While the International Centre for Settlement of Investment Disputes (ICSID) proceedings are published, UNICITRAL ones are often confidential. Arbitration under FTAs (if there are any regarding extractives and LCRs) is likely to be also confidential. It is therefore crucial to have a place to centralise information related to all those cases. The online forum could be one way to do this.

Predictability

While transparency is necessary, it is not sufficient in itself. Therefore, to complement the above, countries should have space to engage and discuss these issues at a dedicated platform.[25] It will allow the information to be used to reflect, shape, and frame better rules and flexibilities for developing countries regarding "inescapable" issues that are being developed outside the multilateral system. Participation in this platform should be broadened to regional economic communities (RECs), which have their own experiences on setting guidelines on these issues, and also to other stakeholders, such as other international organizations or representatives of the private sector.

Linked to the question regarding transparency in BITs' arbitration, there is a perceived inconsistency and unpredictability when it comes to the interpretation of BIT provisions across agreements during arbitration procedures, which precludes the emergence of a consistent body of law (EFILA 2015). It is, however, recognised that there is a limitation linked to the "bilateral" nature of these disputes. Yet, in the absence of a multilateral framework, there are likely to be systemic issues that impact the predictability of the system.[26]

Adapting the rules with flexibility: a plurilateral approach

LCRs are largely an investment issue and therefore require an investment policy solution. Yet, the continued relevance of the WTO amid the evolving trade and investment system will be conditional on its capacity to adapt to reflect the new realities. One way to address this is to design a variable geometry approach, while ensuring that the concerns of developing countries are addressed. This means allowing space for some countries desiring to move faster on certain issues the ability to do so, keeping the door open for others to join at a later stage, and allowing all others to observe. It is

24 See http://tmdb.wto.org/.

25 Along the lines proposed in Suominen (2014).

26 See think-pieces related to the E15Task Force on Investment Policy

therefore proposed to adopt a carefully designed plurilateral framework on investment, with a set of protocols and rules of operation to guide such negotiations (Lawrence 2006, 2008), which will then be agreed to by all Members of the WTO. Experiences exist, with the previous Tokyo Round Codes, the current plurilaterals that fall within the scope of Annex 4, and in side agreements such as the Information Technology Agreement (ITA).[27]

For this to work, however, it is important to assess the risks of such an approach as it may dilute the ability of non-parties to negotiate deals within the framework of the single undertaking (Lawrence 2008). Some countries may fear that fast-movers might start developing new (and stricter) rules and regulations among themselves that might be difficult to (re-)negotiate, with a view to multilateralise those at a later stage (Draper and Dube 2013). Yet in a context where the WTO might be losing clout, this might be the most pragmatic approach as it will allow those negotiations to be done in a transparent manner, remain open, and, most importantly, remain within the system.

ALTERNATIVE POLICIES TO LCRS: PROMOTING REGIONAL CONTENT

Alternatively, RECs can play a key role in seeking to establish better rules, essentially for two reasons. Due to their localised mandate, they have a tendency to focus on areas of common interests to their members, such as building regional markets that reflect the specificities of their respective regions and designing rules that fit the development levels of their member countries. While these may create some challenges for the multilateral system, they may also provide a platform to engage on improving the rules using a sequenced approach.

One of the economic goals of RECs is to build regional markets for domestic industries to source inputs and sell outputs. By removing intra-regional trade barriers, they also aim at encouraging the creation of national and regional value chains. If national and regional policies are well coordinated, this can be a useful complement to national efforts to create strong local clusters in and around the extractive sector. In this context, rules of origin (RoO), as alternative policies to foster local content objectives, play a significant role. The NAFTA, for instance, requires a certain level of regional content that signatory countries have to meet to qualify for free trade rules but provides for full cumulation among member states.[28] Similarly, the creation of the single market in Europe has strengthened industrial development through free movement of factors of production.

On the rules side, RECs are generally good sounding boards for what would be economically acceptable in terms of industrial policies because their member states generally have economic interests in common. Sounding the depth of their commitments in the field of industrial policies and how they manage (or not) to deal with sensitive issues regarding market access for certain products might help anticipate how their member states will react, should these issues be discussed at the multilateral level. RECs should play a more important role at the WTO. Some (the EU, for instance) are already playing a key role because they have exclusive competence in trade, others however do not have the mandate to do so. Yet, there is potential to use them better. It might be too ambitious at this stage to argue for some principle of subsidiarity, where issues that cannot be dealt with at the WTO for lack of consensus will be first dealt with at the regional level. Multilateral negotiations would then adopt an incremental approach, whereby the basic principles where all RECs have a common understanding would be taken as agreed, and negotiations would start from there. This will allow discussions to start on a pre-established basis and secure ownership because RECs will have already secured the agreement of all their members.

POLICY COORDINATION: WHAT ROLE FOR THE PRIVATE SECTOR?

At the national level, successful cases in Chile and elsewhere have shown that there is a case to support strong collaborative partnerships among firms, governments, and research institutions to strengthen the competitiveness of local firms as well as their productive capabilities. Within that framework, governments may have more flexibility to design horizontal support, including financial support, to local businesses and in particular to SMEs, or other forms of incentives to attract investment in clusters, provided that such measures equally apply to other sectors of the economy.

27 Draper and Dube (2014) distinguish between inclusive and exclusive plurilaterals. Inclusive plurilaterals generally entail conditional, unilateral, sectoral liberalization. They are market access instruments, and would probably not apply to rules. Liberalization is conducted on an MFN basis, and is conditioned on other main trading powers also conducting such MFN liberalization. A critical mass is necessary to start the negotiations. They are challenging to achieve, but once agreed upon they do not require consent by all WTO Members. The ITA is one example of inclusive plurilateral. This approach has the advantage of achieving liberalization breakthroughs where broader negotiations are stalled, such as under the Doha Round. However, it carries the longer-term danger that major exporting interests could be removed from the equation of subsequent, broader liberalization efforts. Exclusive plurilaterals involve liberalization only for those Members participating and signing up to the subsequent agreement and benefits are only available to parties to the agreement. Exclusive plurilaterals take several forms—goods PTAs, covered by GATT Article XXIV; services PTAs, covered by GATS Article V; and those residing under the Marrakesh Treaty, Annex 4, such as the GPA. It does not apply on an MFN basis and requires consensus, which might be difficult to reach, in particular as many large developing economies are opposed to it.

28 With the exception of automotive products.

At the industry level, the International Council on Mining and Metals (ICMM) has developed a methodology to promote the engagement of a wide range of stakeholders in the mining sector to assess its social and economic contribution. This should not happen in a silo. Dialogue should be enhanced and structured on a more systematic basis to allow policy coordination, with a view to fostering the design of comprehensive strategies at all levels (domestic, regional, and multilateral) that take into account the realities of all stakeholders involved to adapt to policy changes as economic and political realities evolve and to feed back into the multilateral system.

POLICY COHERENCE AND EFFECTIVENESS ACROSS INITIATIVES

Following the endorsement of the Africa Mining Vision (AMV) by African Union heads of state in 2009, the Africa Mineral Development Centre (AMDC) was created to support resource-rich countries and RECs to implement the AMV; to monitor and evaluate progress; and to provide strategic guidance, coordination, and expertise regarding its domestication. The implementation of the AMV at the national level is a critical condition to ensure that any strategic national policies regarding the sector concur with the continental policy orientation. Similarly, regional policies that support the development of the extractive sector should ensure that these are compatible with the objectives of the AMV.

Finally, an improved regulatory environment is conditional upon policy coherence and coordination across international initiatives, whose objectives are to improve the governance of the extractive sector. Numerous initiatives and institutions have been established to address specific issues or to achieve mutual goals. For instance, the Extractive Industries Transparency Initiative (EITI) aims at improving transparency and accountability in the extractives sector. Although not all countries are members of the EITI, this is an important element in the governance of the sector.

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ANNEX 1

TABLE A:

Levels of LCR Regulations in Selected Mineral-rich Countries

Source: Author's compilation

	Legal framework	Employment requirements	Procurement requirements	Ownership requirements	Reporting requirements	Penalties for non-compliance
Brazil: Oil and gas	High	Medium	High	Low	High	Yes
Chile	Low	Low	Low	Low	Low	No
Ghana: Mining	Medium	Medium	Medium	Medium	Low	No
Ghana: Petroleum	Medium	Medium	Medium	Medium	Low	No
Mozambique: Mining	Medium	Medium	Medium	Medium	Low	No
Mozambique: Petroleum	Medium	Medium	Medium	Medium	Low	No
Nigeria	High	High	High	High	Medium	Yes
Norway	Low	Low	Low	Low	Low	No
South Africa	High	High	High	High	High	Yes
Zambia	Medium	Medium	Services: Low Goods: Medium	High for small scale and artisanal; Low for others	Low	No

TABLE B:

Relevant Regulatory Frameworks on LCRs in Selected Mineral-rich Countries

Source: Author's compilation.

	Key policies	Key legislations	Key regulations	Contracts
		Mining Sector		
Chile	General Mining regulations in the constitution; Constitution organic law of mining Code and regulation governing mining	No specific legislation	No specific regulations	Yes
Ghana	Minerals and Mining Act 2006 (Act 703).	No specific legislation	Minerals and Mining (General) Regulations 2012 (LI 2173) contains details for provisions in the Act dealing with local content	Yes
Mozambique	Mining Law 2014 (Law No. 20/2014 of 18 Aug.)	Mining Law Regulations, Decree no 28/2003 to be amended as per Law 2014 Legal instruments for mega-projects: Mega-projects Law (Law 15/2011, of 10 Aug. 2011)	Mega-projects Regulations (Decree 16/2002, of 4 June 2012)	Specific local content requirements in contracts.
South Africa	National Development Plan 2030, Aug. 2012 Industrial Policy Action Plan, 2013 Minerals Beneficiation Strategy	South Africa Mining Charter 2004 Mineral and Petroleum Resources Development Act (26), 2002 Broad-Based Black Economic Empowerment Act, 2003	Specific acts regarding: Diamonds: Diamonds Amendment Acts 2005; Precious Metals Act 2005	Yes
Zambia	Mineral Resources Development Policy 2013. The policy is yet to be adopted	Mines and Minerals Development Act no 7 of 2008 ("Law 7/08") (granting and holding mining rights) Citizens Economic Empowerment Act of 2006 – Prioritizes granting of licences to investors who promote LCRs.	Statutory Instrument no 84 of 2008 Sets specific reporting requirements for investors on LCRs.	N/a

	Key policies	Key legislations	Key regulations	Contracts
Oil and Gas Sector				
Brazil	Petroleum Law 9.478/ 1997 Constitutional Amendment No. 6/ 1995	Resolution 36/07 of Ministry of Mines and Energy; Local Content Policy, 1999	Reporting requirements in Ordinance 180/2003	Contract Clause No. 2 (concessionaries to favour Brazilian suppliers if o ffer is competitive)
Ghana	Petroleum Commission Act 2011	Petroleum (Local Content and Local Participation in Petroleum Activities) Regulations 2013	Local Content and Local Participation in Petroleum Activities Policy Framework 2011	Model Petroleum Agreement 2003
Mozambique	Gas Master Plan Petroleum Law 2014 (Law No. 21/2014 of 18 Aug. 2014)	N/A covered in Petroleum Law 2014	N/A covered in Petroleum Law 2014	N/A covered in Petroleum Law 2014
Nigeria	Vision 20: 2020 A local content policy was issued in the early 2000s, which was used as a basis for the Act Petroleum Industry Bill	Nigerian Oil and Gas Industry Content Development Act, 2010	Other regulations deal to varying degrees with local content but the Act is the most significant instrument.	Yes
Norway	Act of 29 Nov. 1996 No. 72 pertaining to petroleum activities (Petroleum Act)	Regulations to the Petroleum Act, laid down by Royal Decree, 27 June 1997 (Petroleum Reg)	Technical regulations	

TABLE C:

Matching LCRs with Relevant WTO Provisions

Source: Adapted from Greenaway (1992); Mc Culloch et al. (2001).

<table>
<tr><th colspan="2">Measures affecting sourcing of inputs</th><th>Relevant WTO provisions</th></tr>
<tr><td colspan="3">Local procurement requirement</td></tr>
<tr><td>General LCRs</td><td>A percentage of value added or intermediate inputs to be purchased locally</td><td>TRIMs illustrative list para. 1 (a).</td></tr>
<tr><td>Trade balancing requirements</td><td>Imports of one product linked to export performance to other products</td><td>TRIMs illustrative list 1 (b) for internal measures; 2 (a) for border measures</td></tr>
<tr><td>Preference for local substitutes</td><td>Investors to purchase local substitutes for imports if similar component is produced locally</td><td>GATT Article III.4 if (i) imported products are accorded less favourable treatment compared to local suppliers; (ii) imported goods and the domestic products are considered as like products; and (iii) measures are inscribed in laws, regulations and requirements.</td></tr>
<tr><td>Limitations on imports</td><td>Amount of goods and services that can be imported for the production process is limited</td><td>GATT Art. III.5; GATT Art. XI.1; TRIMs illustrative list, para. 2(a)</td></tr>
<tr><td>Foreign exchange restrictions</td><td>Restrict the inflow of foreign exchange attributable to an investor to constrain the amount of imported intermediate goods</td><td>TRIMs illustrative list, para 2 (b),
Exception for developing countries GATT Art XII and XVIII:B</td></tr>
<tr><td colspan="3">Ownership requirements</td></tr>
<tr><td>Local equity participation</td><td>Some proportion of equity must be held locally</td><td>GATS Art XVI for market access restrictions and Art. XVII for national treatment, in schedule of commitments</td></tr>
<tr><td colspan="3">Employment requirements</td></tr>
<tr><td>Local employment targets</td><td>Specified employment targets have to be met</td><td rowspan="3">GATS Art XVI for market access restrictions and Art. XVII for national treatment, provided in schedule of commitments</td></tr>
<tr><td>Quotas for foreign employment</td><td>A maximum number of expatriate staff is specified</td></tr>
<tr><td>National participation in management</td><td>Certain staff has to be nationals or a schedule for “indigenization” of management has to be set</td></tr>
<tr><td colspan="3">Technology transfer requirements</td></tr>
<tr><td>R&D requirements</td><td>Investors commit to investment in R&D</td><td rowspan="2">GATS Art. IV; TRIPs Arts 3, 7 and 8; SCM Agreement Arts 2 and 8</td></tr>
<tr><td>Technology transfers</td><td>Specified foreign technology be used locally</td></tr>
<tr><th colspan="2">Measures affecting production</th><th>Relevant WTO provisions</th></tr>
<tr><td>Minimum export requirements</td><td>Certain percentage of production have to be exported</td><td>GATT Art. III.5; GATT Art. XI.1; TRIMs Illustrative List, para. 2(a)</td></tr>
<tr><td>Trade balancing requirements</td><td>Imports have to be a certain proportion of locally produced exports, either in terms of volume or in terms of value</td><td>TRIMs illustrative list 1 (b) for internal measures; 2 (a) for border measures</td></tr>
<tr><td>Domestic sales requirements</td><td>Certain product may not be exported</td><td>GATT Art. III.5; GATT Art. XI: 1; TRIMs illustrative list 2(c)</td></tr>
<tr><td>Market reserve policy</td><td>Some markets are reserved for local production</td><td>GATT Art. III.4</td></tr>
<tr><td>Product mandating requirements</td><td>Some products to be exported by the hosting country only</td><td>GATT Art. III.5; GATT Art. XI: 1; TRIMs illustrative list 2(c)</td></tr>
<tr><td>Licensing requirements</td><td>Investors to obtain license for production in the host country</td><td>GATT Art. XI.1</td></tr>
<tr><td>Technology transfers</td><td>Investors are committed to a specified embodied technology</td><td>TRIPs Arts 3, 7 and 8; SCM Agreement Arts 2 and 8</td></tr>
<tr><td colspan="3">Exceptions for developing countries: Developing countries are permitted to retain TRIMs that constitute a violation of GATT Article III or XI, provided the measures meet the conditions of GATT Article XVIII, which allows specified derogation from the GATT provisions for the economic development needs of developing countries.</td></tr>
</table>

Implemented jointly by ICTSD and the World Economic Forum, the E15Initiative convenes world-class experts and institutions to generate strategic analysis and recommendations for government, business, and civil society geared towards strengthening the global trade and investment system for sustainable development.

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