



GUIDANCE FOR GOVERNMENTS: LOCAL CONTENT POLICIES

EXECUTIVE SUMMARY

1. WHY ARE LOCAL CONTENT POLICIES IMPORTANT?

Too many resource-rich countries remain challenged by undiversified economic structures with weak industrial bases, high unemployment and economies vulnerable to commodity cycles. Many of them are reviewing or revising mining and investment codes and contracts, looking to local content policies to help exploit mining's powerful potential for inclusive economic development.

But there is no simple template; each country has different resource endowments, different skill sets in their local suppliers and labour force, different infrastructure assets and challenges, and different investment environments. The history of practice of local content policies yields more cautionary tales than best practices.

While it is important to underscore the risks associated with failed policies, there have also been successes, and lessons can be drawn from both. The mixed record of the past suggests that countries need to invest heavily in getting it right. This guidance aims to help in that process.

2. WHAT DO WE MEAN BY LOCAL CONTENT POLICIES?

Local content policies cover a broad array of approaches, ranging from mandatory targets to soft requirements, to supportive policies in areas such as education and capacity building. This guidance covers policies with five different sorts of objectives:

- Increasing mining operation procurement of local goods and services
- Increasing mining operation hiring of locals
- Increasing the spillover benefits of mining investment into non-mining sectors
- Increasing the local processing (beneficiation) of the products of mining operations
- Increasing the capacity of local actors as mining sector operators, including state-owned enterprises.



3. WHO IS THIS GUIDANCE INTENDED FOR?

This guidance is primarily aimed at government policy-makers. However, it should also be useful to any stakeholder interested in the successful implementation of local content policies—particularly mining companies, but also intergovernmental organizations, development banks and development agencies that aim to support mining-based development and non-governmental organizations and researchers focused on mining-related issues.

4. HOW SHOULD IT BE USED?

As noted above, local content policies are highly context-specific; there are no one-size-fits-all solutions. IGF's guidance on local content policies will help policy-makers ask the right questions to guide them toward workable made-in-country solutions, and will help in the process by highlighting the many lessons of history—positive, negative and mixed—and by pointing to the many helpful resources in this area. This guidance is part of a suite of guidance products developed by IGF and, like the others, can be used as a stand-alone resource. It can also be used as a basis for IGF's Mineral Policy Framework assessment and country- or regional-level in-depth training programs.

The guidance outlines four steps governments should follow in creating and implementing local content policies.

5. STEP 1: ENSURING A FIT WITH NATIONAL DEVELOPMENT OBJECTIVES

The first step for governments developing local content policies in the mining sector is to create a picture of the role that the sector plays in national development plans. Local content policies can then serve as part of the overall approach to ensure that mining investment plays its full potential role in achieving the objectives those plans entail.

6. STEP 2: TAKING STOCK

The second step for governments, having clarified their objectives, is to take stock of their current situation. This crucial step helps to highlight what opportunities might exist, what targets are reasonable, what gaps need to be addressed, what parallel initiatives might be needed, what leverage governments might have

with investors and, ultimately, what types of local content policies might be feasible, given their objectives and their particular circumstances.

The sectoral context is important: governments need to survey the political, socioeconomic and geological contexts in which investors and mining companies operate. They also need a good understanding of the opportunities—what types of skills, goods and services and what infrastructure will mining companies need? And they need to assess the gaps: to what extent are suppliers and workers able to fill those needs, and what are the shortcomings?

Finally, governments need to assess the business environment, identifying the main obstacles to mining exploration, establishment, construction and business start-up. They also need to gauge internal capacity, including resources in the ministry responsible for mining, interministerial coordination mechanisms, and consultative mechanisms with the private sector, suppliers, workers and affected communities.

As important as policy design is, even more fundamental is asking whether local content policies are the right tool to meet policy objectives in the first place. If the stocktaking exercise reveals that current domestic capabilities and skills are very low, if internal capacity for monitoring is thin, if profitability of the resource is questionable, then it may be more appropriate to focus in the short term on other policy areas such as infrastructure and basic education. Local content policies can be planned for the medium term when the prerequisites for success are more promising.

7. STEP 3: CRAFTING THE POLICIES

This guidance covers five broad types of local content policies, each aimed at different but related objectives. The first two steps—clarifying objectives and taking stock—should help make it clear whether local content policies are the most appropriate instrument and which type of policies governments should focus on. What follows should help them to decide what sorts of tools are most suitable within the chosen policy areas.

There is a logical sequence to the choice of many policy instruments. Countries embarking on their first efforts at local content policy, or with poor existing linkages, should focus first on measures to boost direct employment in



the mining sector. The skills training efforts necessary for this goal are a foundation for other forms of local content policy as well.

If local industrial capacity is sufficiently strong, they should also focus on boosting local procurement, and if capacity and markets exist they may want to explore downstream value addition.

Horizontal linkages through skills and capabilities are challenging, and will usually be pursued where there is already some success in local content via direct and upstream linkages.

Horizontal linkages through shared infrastructure are not so dependent on skills and capabilities. While they can be complex and fraught with governance issues, they can be pursued at any time, including in parallel with other efforts.

7.1 LOCAL PROCUREMENT

Policies of this type aim to boost the amount of local goods and services purchased by mining operations. Carried out successfully, they can significantly increase mining's contribution to national GDP. Indeed, they typically hold

much more potential than taxes and royalties. Local procurement can eventually be a gateway to economic diversification, with suppliers maturing into exporters and moving horizontally into non-mining sectors.

Defining “local” is key to the implementation of local procurement policies. There are three basic approaches, each with its strengths and weaknesses:

- **Geography:** Local can mean registered, incorporated, or carrying out business activities in any of various geographic delineations—national, regional, state or provincial, or in communities close to the mine site.
- **Value addition:** Local can mean that a substantial amount of value was added in country, as for example when goods are locally manufactured, or processed or assembled using some imported components. While the geographical definition might allow counting of finished goods that are imported and then simply re-sold, this definition ensures that “local” goods are the product of some substantial local economic activity. However, measuring local value added can be challenging.
- **Ownership:** Local ownership focuses on participation, which can mean some proportion of locals in management, or as owners of equity, or as employees. The challenge is to ensure that the final results are in line with the objectives; companies have been known to meet such requirements by granting equity stakes, or non-working management or Board positions, to local elites as part of payback or political patronage schemes.

There is a wide variety of policies for encouraging local procurement. On the demand side, they focus on creating a demand for local procurement of goods and services. These can range from mandatory specified percentages to voluntary incentives for achieving targets. On the supply side, the focus is on building the capacity of local suppliers to bring them up to global standards on price, quality and reliability. Both types of policies are typically needed; supplier development helps to ensure that demand-side policies do not require more than local firms are able to supply.



7.2 LOCAL DIRECT EMPLOYMENT

Policies of this type aim to enhance the amount and quality of local employment by mining operations. Carried out successfully, they can create new local jobs, grow and develop the skills of the national workforce, and support efforts to progress gender equality and social inclusion.

There are two types of local employment policies. Regulatory approaches, which typically result in prescriptive, “stick”-based policies, are generally mandatory and rely on strong compliance mechanisms. These include:

- Mandated local employment percentages, often different for different types of jobs
- Requirements to conduct training of locals, or support training facilities
- Required succession, or localization, plans
- Visa restrictions on foreign workers
- Mandated employment of Indigenous people, women or disadvantaged groups.

Facilitative approaches, which typically result in incentive-based, “carrot” policies, offer support and incentives for the development and employment of local workers. For example:

- Preferences in the awarding of mining contracts
- Non-binding requirements to hire locals (e.g., “to the extent possible”)
- Fiscal incentives for local hiring.

Governments occupy a unique position in being able to influence both the supply and demand sides of local employment in the mining sector. A government can regulate that a company complies with local content requirements; it can also facilitate education and training measures to prepare the local labour force to fulfil these requirements. In almost all cases both types of measures are imperative; simple regulation and blanket policies without parallel efforts to ensure adequate skills are available are not a recipe for success.

7.3 HORIZONTAL LINKAGES: DEVELOPMENT BEYOND THE MINING SECTOR

Policies of this type aim to foster the development of other (or new) economic sectors using the skills, capabilities and infrastructure developed by the extractive industry value chain. Carried out successfully, they can lead to economic diversification away

from reliance on the extractive sectors. They can also set the stage for economic vitality after mine closure.

Horizontal linkages can develop via two distinct channels. Infrastructure-led linkages develop when infrastructure developed for the resource sector (e.g., roads, rail, ports, water treatment, electricity, and Internet) benefits another productive sector. This type of policy seems straightforward, but requirements to build multipurpose infrastructure impose costs on the affected operations, and negotiations and governance are often complex.



Capabilities-led linkages generally develop from upstream linkages, as technology or skills developed in supplying the resource sector are then used elsewhere. Policy options in this area include supplier development programs aimed at equipping suppliers to serve a diverse client base, and broader capacity building/education initiatives that equip entrepreneurs to evolve, such as national systems of innovation.

7.4 DOWNSTREAM LINKAGES: BENEFICIATION OF MINING PRODUCTS

This type of policy aims for economic diversification, but does so within the mining sector by encouraging processing or value added for the products of mining. For certain commodities, such as petroleum and steel, downstream linkages are driven by national security concerns.



Policies to encourage downstream linkages include incentives in the form of subsidies (e.g., tax breaks, concessional loans, land grants, infrastructure), conditioned on establishment of processing operations. They also include prescriptive measures such as export duties, quotas and bans of unprocessed minerals, designed to incentivize the local use of inputs. There are also some negotiated agreements on processing, as well as preferences given in the bidding process to vertically integrated firms.

Here as much as anywhere, it is critically important to take stock, understanding the markets and trends for the processed goods through an exercise that includes market analyses, a comparative advantage review and cost-benefit analyses of new downstream sector development. The success of downstream policies will depend on whether the country can become competitive in the downstream sector over the medium term.

A number of critical prerequisites will determine the success of efforts to create downstream linkages, including: location and good infrastructure; (often) reliable and inexpensive energy access; a competitive labour force, and proximity to high-value raw materials. There are only a handful of successful examples of state-led efforts to create downstream linkages in the mining sector.

7.5 BUILDING DOMESTIC CAPACITY: FOSTERING NATIONAL MINING FIRMS

This type of policy aims to foster more mining activity in the hands of nationals, whether private sector actors or state-owned enterprises (SOEs). There is a presumption that national firms will tend to act more consistently in the national interest, including by fostering the sorts of linkages described above. SOEs are often given explicit social development mandates to accompany their economic goals.

The policy options of this type include:

- Joint venture requirements: requirements that any foreign investor in a particular sector must operate as an equity joint venture with some local partner.
- Creation/promotion of SOEs as sole actors: involving a high level of government involvement in the sector; may entail suppression of anti-competition laws, forced mergers of

existing SOEs and forced closure of smaller competitors.

- Expropriation of private firms: involving the transfer of ownership and control of an existing private sector operation to the state, or by force of law to some third party.

Any government involvement in ownership must navigate a delicate balancing act between imposing the kind of sovereign control that seeks domestic benefits, and granting the kind of independence necessary for commercial success. Several of these strategies face potential conflicts with trade and investment law.

8. STEP 4: MONITORING, REVIEW, ENFORCEMENT

Once designed, local content policies must be administered and enforced, and progress must be measured against explicit benchmarks in the form of plans or targets. They therefore must include a built-in independent monitoring and enforcement mechanism, which ensures that various stakeholders (including public institutions) can be made accountable. Such a mechanism needs common reporting requirements for mining companies, and strong systems for collecting data on the results of the interventions.

The mechanism should include a review function, such that failure is not simply met with punishment, but also involves consultation and critical assessment of the policies themselves for potential revision and improvement. It should also be mandated to propose the phasing out of certain support measures when industries become competitive enough to sustain on their own, or if, after a given timeframe, it is clear that the support measures will not have their desired effects.

9. CROSS-CUTTING CONCERNS

9.1 THE CHALLENGE OF TECHNOLOGICAL EVOLUTION

In the coming years, automation will change the face of the mining industry. One of the biggest impacts will be a drop in employment per unit of value, as automation is brought to bear on low- and mid-level skilled jobs. The immediate



implications, and the primary reasons for uptake, are that mine sites will be more efficient, will have lower greenhouse gas emissions and will suffer fewer workplace accidents.

But because the mine of the future will have fewer employees, it will also have lower spending on domestic procurement for those items that are linked to employees, such as food and housing. New technology may also mean fewer opportunities for local maintenance and servicing of capital.

Governments need to be aware of this as they plan local content strategies. Less employment ultimately means more difficulty in capturing national-level benefits from procurement spending, from the horizontal linkages that evolve from supplier development, and from direct employment.

9.2 THE CHALLENGE OF INTERNATIONAL TRADE AND INVESTMENT LAW

By their nature, local content policies underscore preferential treatments for local suppliers against foreign goods and services providers. Such measures may contravene countries' obligations under trade and investment treaties.

Some of the most prominent of those obligations are found in prohibitions on performance requirements. The World Trade Organization's rules on trade-related investment measures prohibit any advantage conditioned on the use of local content requirements, and many modern investment agreements (e.g., bilateral investment treaties, investment chapters in free trade agreements) go further, prohibiting requirements for technology transfer and joint ventures. The WTO also prohibits using local content requirements as a condition for subsidies. A number of other common subsidies, such as targeted (specific) tax preferences, may also be WTO-illegal.

While governments must be conscious of their international commitments, there has never been a WTO case brought on local content policies in the extractive sectors sector (there have been cases over export bans that were aimed at in-country beneficiation). There are many tools available to governments that do not conflict with trade rules, and a great deal of scope to pursue local content objectives in such a way as to minimize the prospects of trade and investment disputes.

10. IN CLOSING

IGF's guidance on local content policies is a guide to the questions that policy-makers need to ask to help them decide on how best to proceed in this area. While it includes a large number of brief case studies to illustrate the lessons of history, each country's solution will be unique, and dictated by its objectives and circumstance. The aim is to help governments, companies and citizens collaborate to ensure mining provides governments significant, gender-equitable, inclusive and sustainable development.



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