

between an investor and the government. It is generally beneficial to define as many of the natural resource development rules as possible, including fiscal terms, in legislation, leaving to negotiation only limited matters. This ensures consistency and transparency, while allowing for flexibility to address some project specific considerations. However, in early stages of resource development, where the rules are evolving, countries may in practice rely on project specific contract negotiations for many items governing natural resource development, including key fiscal

fiscal regimes that generally apply in these industries, while the Fiscal Terms Note provides additional important detail on the elements of such regimes. Together, they provide additional context for the issues reviewed in this note.

Negotiation Background: Country Perspectives

Balancing investment attractiveness with obtaining resource value

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fiscal regime and other key statutory or contractual conditions should be tested against their impacts on achieving the base objectives.

One of the benefits of relying on a statutory approach for fiscal regimes is that it can embody the agreed upon objectives and ensure consistency among projects.⁸ Where more of the terms are left to negotiations, the risks increase that the ultimate contract will not be as fully consistent with the country agreed upon priorities.

Experts increasingly suggest that the model with more detailed laws and regulations creates a stronger foundation upon which a country can manage its extractive industries according to national priorities. In addition to helping investors to feel like they are being treated equally across deals, consistent terms across projects can streamline monitoring for government institutions. A robust legislative framework may also result in greater public input because the public can more easily participate in the legislative process than in individual contract negotiations.⁹

Where some of the fiscal regime provisions are included in statutes while others are negotiated, the negotiations present the very real risk that conflicts may arise between statutory rules and the contract provisions. This is addressed more fully below in the context of having tax and customs representatives involved in fiscal terms negotiations to ensure enforceability of the contract terms and their conformity with the statutory provisions in place.¹⁰

Parties involved from Country standpoint (Internal and External Stakeholders)

A key factor that distinguishes natural resource development from many other

benefit of which should belong to the people of the country. In addition, considerations of how those benefits are shared between current and future generations are also involved. Finally, while the benefits are often viewed as inuring to the entire country, the disruptions that naturally occur in development activities can disproportionately be borne

[pdf](#), page 9. Also see the Natural Resource management requires an inclusive and comprehensive national strategy. To achieve this, the government must make a series of key decisions that will affect different groups and set choices extending far into the future. To avoid making decisions in a piecemeal fashion and to build a shared sense of direction, governments should, in dialogue with stakeholders, use a national strategy process to guide <http://resourcegovernance.org/approach/natural-resource-charter/precept-1-strategy-consultation-and-institutions#>; and IISD Handbook, section 4.5.1, pp. 49-50.

⁸ Consistency among investors and projects can be important from a non-discrimination and anti-corruption perspective. A further benefit to consistency in terms and terminology that a statutory approach provides is the facilitation of administration and compliance enforcement.

Resources Governance Institute, NRG Reader, March 2015, p.6. at <http://www.resourcegovernance.org/analysis-tools/publications/primer-legal-framework>

¹⁰ Where a statutory rule is no longer realistic, or is not sufficiently flexible to accommodate projects that country negotiators wish to have developed, it is arguably better to adjust the statutory rules themselves

unenforceable, and lead to conflicts and ambiguities that only increase risk and uncertainty.

by the region or locations where most of the activities are conducted. Thus, special consideration for such localities must be taken into account.

National Government representatives¹¹

s a complex exercise, given

policy and practice to assist in determining and evaluating the composition and approach of which fiscal tools to use.

Further, involvement of tax representatives in the negotiation process creates a better understanding of how the provisions are intended to operate in practice and ensures that they can in fact be implemented as intended. Many examples exist where without involvement of the tax (and customs) administrations, a negotiation will result in provisions that are contrary to the tax laws (including tax treaties) in existence, or may use terms that have different definitions under such tax provisions may intend, creating immediate ambiguities, if not outright conflicts, in the interpretation of the agreement and its enforceability under the other statutory requirements in place.¹³ In a recent African Tax Administration Forum (ATAF) meeting, one country representative noted that its Tax Administration, which had not been involved in a negotiated contract, found itself unable to implement the terms of a negotiated contract since they were in conflict with the specific tax laws of the country. This forced a renegotiation of a contract that the investor and the government negotiators had signed (and thought was finalized). This result can be largely eliminated by ensuring participation and inclusion of tax and customs administrations in the negotiation process.¹⁴

Such participation can be achieved by having representatives of the affected agencies on the negotiating team or, at a minimum, available to and regularly consulted by the team throughout the process. It is equally important that investors work with the negotiating parties to clarify that such involvement and consultation is undertaken.

Uncertainties that may exist in implementation of any aspect of the agreement will simply increase the risks the investor will see, and will therefore affect the terms of the negotiations. Reducing these types of risks is beneficial to all.

¹³ See e.g., a recent Parliamentary Briefing issued by the Natural Resource Governance Institute noting, elements of oil, gas and mining projects are coherent. Some countries have wrestled with inconsistencies d Deal from Oil, Gas and Mining Parliamentary Briefing January 2015 FISCAL REGIMES FOR OIL, GAS AND MINERALS, in http://resourcegovernance.org/sites/default/files/documents/nrgi_fiscalregime_20150311.pdf, p. 4. While ambiguities in statutory interpretations can occur, generally providing for as many of the fiscal terms as possible in statutes, and minimizing the terms that are agreed to via separate contracts, will help to reduce ambiguities. Ghana presents an interesting dichotomy here given that it has traditionally provided the fiscal terms in the mining sector on a negotiated contract basis, while it is generally standardizing terms in the oil and gas sector by means of statutory requirements.

Further, the language differences of negotiators, and differences betf1 F414.07Lthe angua iseeuLth(h)-9(u53(o)-i-4ge)4E

displayed her consistency, integrity (the negotiation team knew they could count on her backing if needed), and involvement. She sought updates, listened to the negotiating team and its advisors, was accessible, was a consensus builder, held people accountable, had

positions are far less likely to be successful.¹⁹ Nevertheless, the final product, including explanations of the various trade-offs embodied within it, should be available for review and comment. Negotiators should also be prepared to explain their final positions taken in concluding the overall agreement.

Outside Advisor Resources

It is often stated that investors negotiating natural resource development agreements possess asymmetric information and skills, given their technical expertise and greater experience in such matters. There are several ways to address this issue, depending on time and resources available.

First and foremost is to identify the information and skills the government needs (e.g. valuation of the resource or project, overall market analysis, legal or other negotiation skills, environmental expertise, and economic modeling) and then identify which of these can be adequately covered from within the government itself. In many cases, countries do in fact have the knowledge and skills required and should take full advantage of these resources. Where it is determined that gaps exist, or where additional augmentation is desirable, identifying options and putting together a plan for dealing with these is the next step. A number of possible approaches exist.

One option is to hire outside

Many organizations are available to provide overall background to a country beginning or enhancing its education on important natural resource development issues. These include well known international and regional financial and development organizations, assistance organizations supported by one or a small number of countries or other organizations, and numerous non-governmental organizations dedicated to providing support with respect to natural resource matters. These can be quite helpful in providing basic information, more general in nature, rather than specific technical support for a particular project or contract.

In addition to more generalized information and support, specific project related negotiations support is also provided by several organizations. An excellent window into the array of advisors, technical assistance programs, and other advisory and support Governments.²¹ The Portal, operated by the Columbia Center on Sustainable Investment (CCSI), is part of assistance by:

s (CONNEX) to provide developing country partners with extended and concrete expertise for negotiating complex commercial contracts. G7 Summit Communiqué, June 5, 2014.

The Code of Conduct for the CONNEX²² initiative states:

initiative is to strengthen advisory support to low-income country

A number of sample contracts are available from various sources, including the Extractive Industries Source Book,³⁰ Open Oil,³¹ and Resource Contracts.³² As of 2013, Open Oil suggested that either model or actual signed contracts were publically available for: Afghanistan, Angola, Azerbaijan, Bangladesh, Brazil, Burkina Faso, Cambodia, Colombia, Congo, Cyprus, DRC, Ecuador, Equatorial Guinea, Ethiopia, Ghana, India, Iraq, Jordan, Kenya, Liberia, Libya, Mauritania, Mexico, Mongolia, Mozambique, Nicaragua, Peru, Senegal, Sierra Leone, Tanzania, East Timor, Trinidad and Tobago, Turkmenistan, and Uganda.³³

Sample mining agreements and models/examples of mining contract provisions are available under the Model Mining Development Agreement Project.³⁴

In its directory of Petroleum and Mineral Contracts, Resource Contracts has at least one contract (model or actual) for 89 countries.³⁵

Negotiation Background: Investor Perspectives

Understand country priorities

Just as it is important for a country to critically evaluate its priorities and key objectives in developing its resources, it is basic to a successful negotiation that the investor dialogue

discussions can be at a high level where basic principles, objectives, and obligations are articulated and debated. Seeking to understand the underlying interests that the parties have can often lead to solutions to positions that might otherwise appear to be intractable.³⁶

Look for long term relationships

Investors will explain one of their basic objectives is to develop a long term, mutually beneficial relationship with the country. Agreements that are overly favorable to one side are not likely to be lasting ones and certainly will not operate to maximize the value of the resources to be developed. If overly favorable to the investor, the country will

³⁰ http://www.eisourcebook.org/676_58ContractNegotiationsandDisputeSettlement.html

³¹

press to renegotiate or simply impose new terms. If overly favorable to the country, the investor will likely terminate the contract at the first opportunity, and development of the resource itself may be jeopardized. Agreements that provide a balance of interests, and which provide some degree of flexibility in case of material and substantial changes in circumstances, can create an underlying contractual structure most supportive of a successful long term partnership.

Articulation of investor needs and investor risks³⁷

The extractives industries are unique in many ways: The sector is shaped by high sunk costs in the form of substantial investments that often cannot be recouped if a project is unsuccessful, long lead times from initial investment to project start-up, fluctuating costs and prices that in turn influence the profitability of exploration, development and extraction, volatile demand, very long production/project lives, and substantially greater environmental impacts to address, including ultimately decommissioning or reclamation responsibilities.³⁸ An investor committing to the substantial outlays required for these investments will look for a satisfactory return taking into account all of the risks the investor bears. This is one reason why it is difficult to compare fiscal regimes and general return levels across countries, since the degree of geologic, political, and economic risks varies country by country and even project by project.

One key consideration that can benefit a country in its negotiations is that the more a country can reduce investor risks, the lower the return the investor will need, and hence the more it will be willing to pay. Investors themselves further seek to reduce risks given the large, and usually upfront, amounts they make, and hence generally see benefits in stability and predictability of laws and fiscal arrangements.

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[International Oil perception of risk they will be prepared to give you an even bigger share of the reward. OR, to put it another way: Offering a stable, consistent and predictable tax environment, with a fair, transparent, timely and reliable appeals process is very valuable to IOCs. If you can convince them that you will provide this they will accept a higher government take.³⁹

Stability clauses⁴⁰

Investors frequently seek provisions in contracts that operate to limit the changes that can be made over time, most especially to the fiscal terms. This is because the projects generally involve substantial upfront capital and the project lives are expected to last for long periods. As noted, investors seek to reduce risks as much as possible, and given that government policies and officials will almost certainly change over time, a way to provide some degree of stability against such changes is often so

mechanisms used to reduce political and legislative risks.

Stability clauses have themselves evolved over time. Most of the early clauses generally froze the important aspects of the fiscal and legal regime applicable to the particular project to what was in effect at the time the contract was agreed upon. This provided investors with a higher degree of confidence that the important fiscal and other legal provisions upon which their economics were based would last throughout the project. A

change its laws over time. In reality, such clauses did not technically freeze the government from enacting changes, but instead provided a contract right to the investors

of provisions to ones more of an economic equivalence approach hence many clauses now provide that should certain governmental changes occur (e.g., an increase in the tax rate), the parties agree to negotiate changes to the contract to place the investor back in the

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made at Fiscal Management of Oil and Natural Gas in East Africa

As noted, contractual stabilization provisions have to be evaluated in terms of their interrelationship with general statutory rules in existence (or which are later enacted). The effect of such stabilization provisions may generally be more effective, and more supportable, as they apply to fiscal terms, versus human rights or other social issues, since they do not have to override the law (i.e., payments to the government can be

where the investor sets forth what it believes will be necessary for a commercial project to be viable, and the government will seek to maximize its benefits, consistent with a project going forward.

If there is the opportunity to negotiate a lower tax or royalty rate or any other payment to government, any rational company would take it. If there is an argument that the proposed arrangements in the model agreement are uneconomic, then a company would not be irrational to negotiate terms that made the mine economic under even the worst scenarios (though a forward-looking miner might be cautious about signing a deal that is "too good to be true", anticipating government dissatisfaction and potential conflict down the road). The company will want to make sure its mine is still profitable after it has incurred the costs of getting the gold out of the ground, to market, and paid the government its shares.

But the government will want to be sure of some things as well. Its job is not to bend over backwards, but to maximize the total benefit to the country. Correction, the total NET benefit. This is a key concept. Mining comes at a cost.⁴⁸

Production/operations

Once the facilities have been constructed or developed, including production, processing, and other infrastructure requirements, production operations will begin and production levels will be ramped up until production amounts set forth in the development plan are achieved (or levels are re-adjusted based on further agreement). The contract maktionrthTgbc n

stable and acceptable state. The general outline of the requirements for

Some Practical Aspects of Successful Negotiations⁴⁹

Preparing for negotiations is a time-consuming process. Getting the negotiating process right is also time consuming. Both are essential, however, if the result is to be constructive.⁵⁰

The following is a brief summary of some major practical considerations that can help achieve success:

1. Preparation, and development of policy objectives before negotiations commence.
2. Consider the long term relationship and seek a result that is positive for the government, the community, and the investor.
3. Prepare by understanding the value of the resource and the economic development goals to be sought, including revenues, employment, infrastructure, downstream opportunities, local content, environmental stewardship, education and training.
4. Build a negotiating team with interdepartmental representation and strong communication and decision making protocols.
- 5.

Before any negotiations begin, both the investor and the government will do research on one another, with the investors seeking to understand the goals and backgrounds of the governmental negotiators and information about the country and countries equally seeking to understand the nature of the potential investor and its negotiators.

The term "due diligence" generally refers to an investigation carried out by a party to learn and verify the full background, history and current situation of the other party(ies) with which it may contract. Due diligence takes time and is expensive, but thorough due diligence will prevent

transparency is in the best interest of the government, private investors and citizens. The disclosure of contracts expresses the public ownership of the exploited natural resources. Transparency also ensures that expectations from communities affected by the contracts are managed and realistic. Public disclosure of the terms of concession agreements provides a safeguard for private investors to ensure contract stability and avoid abuse in contract implementation ⁵³

Investors may prefer confidentiality to protect proprietary and competitive information, and likely to streamline the process of finalizing an agreement, but their main objective appears to be that the rules be applied uniformly. Thus, rules that may apply only to certain types of investors (e.g., publically traded companies), and thus treat competitors differently, can inappropriately provide a competitive advantage to some at the expense of others.

Dispute Resolution under a Specific Contract⁵⁴

Given the number of issues that can arise under natural resource contracts, and the long timeframes of the projects governed by such contracts, it is almost certain that disagreements on both the meaning of the contract terms and the compliance with the contract obligations (by either party) will arise. The contract itself generally provides mechanisms for resolving such disputes, with the ultimate resolution mechanism usually being litigation. However, there are often several steps that may be followed in resolving disputes other than by going to court, such as:

1. Seeking to settle the dispute among the parties themselves;
2. Referring the issue to a technical expert⁵⁵, whose conclusion may be binding or simply advisory;
3. Referring the issue for mediation (usually non-binding); and
4. Referring the issue for arbitration (which may be binding or non-binding).

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GETTING A GOOD DEAL FROM OIL, GAS, AND MINING: FISCAL REGIMES FOR
OIL, GAS AND MINERALS ⁵⁸

When designing or assessing fiscal regimes for oil, gas, and mining, government officials should take into account the following goals:

invest. Extractive projects have large upfront exploration and development costs and long production timelines. The fiscal regime must assure companies that the rules will not be unduly changed once investments are made. Stable fiscal regimes that provide a fair return to both investors and the state⁵⁹ under a variety of circumstances will be less
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extractive projects and are more sophisticated in tax planning, which can give them the upper hand in negotiations.

Contract Renegotiation Issues

Background

Ideally, contract or licensing rules applicable to long term natural resource projects will be - ⁶⁰ For example, in times of increased prices, fiscal terms which automatically adjust the amount of government take per a prescribed formula can ensure a fair revenue sharing occurs, even as total revenues increase. Conversely, in times of very low prices or increased costs, ideally the terms will adjust to promote continued operation of the project rather than making it even less economic. Thinking through items (or assumptions) that may change significantly over time, and providing flexibility in contract term design that address such potential changes may automatically be accounted for in the contract can obviate the

Prior sections noted the use of stability clauses to address law or government policy changes. The more modern stability clauses call for the parties to enter into good faith negotiations to place the investor in a similar economic position as if the rules had not changed. This can be viewed as a means of acknowledging the right of the government

The State and the Contractor shall meet if the State or the Contractor gives at least forty-

Circumstances to have occurred. At the meeting, the State and the Contractor shall review the relevant facts and circumstances and determine whether or not a Profound Change in Circumstances has occurred. To the extent that a Profound Change in Circumstances has occurred, the State and the Contractor shall enter into good faith discussions to consider and shall make such modifications to this Contract as they may

Where the government has the upper hand, choosing either 1 or 2 can lead to an outcome where the resource becomes unproductive and the project is either mothballed or terminated prematurely. For example, where conditions change to the detriment of the investor, such as long term decrease in prices or highly escalating costs of meeting commitments, it may seek some relief from the government.⁶³ Where relief is not provided, the investor will nevertheless be obligated to fulfill its contract terms. But if the project is early on, one could expect the investor to do the minimum required under the project terms, or even exercise a contract right to terminate. This may not be in the best interests of either party, and hence it is usually better to find some way to make adjustments as long as they are reasonable and balanced. An investor requesting a delay in meeting drilling commitments (to mitigate a spike in drilling costs), could perhaps be granted that by the government in return for a small delay payment. Thus, a true negotiation, with each side giving and getting something, takes place.

On the other hand, when the government approaches an investor to renegotiate contract terms, the investor who is likewise interested in promoting and growing a long term relationship, should likewise be open to a negotiation where each side gives, and gets, something. For example, an investor might agree on the renegotiation of a particular fiscal term sought by the government in return for a modification to the duration of the contract.

Some illustrations⁶⁴

Case A:
renegotiation of a number of resource contracts following the end of the civil war in 2003. Following her government coming to power in 2006, President Ellen Johnson Sirleaf ordered a review of all concession agreements, with priority given to the two

way for a more stable partnership between the companies and the Liberian government.

plainly that better contractual terms and heightened investor interest can in fact go hand in hand.

The ArcelorMittal amended agreement had some 30 improvements over the original contract; the Firestone amendment had nearly 40 improvements. The Government has widely cited the re-negotiations of the ArcelorMittal and Firestone contracts as proof of

attention of other African governments seeking to maximize value from concession agreements covering their natural resources.⁶⁶

The report provides extensive background on how the negotiations were conducted, and the give and take that ensued, ultimately arriving at agreements accepted by the parties. It shows how a principled approach to renegotiations, coupled with a sound justification underpinning them, with strong preparation, technical assistance, and political support, led to a successful result.

Case B: In several countries, major natural resource discoveries have been made but development agreements and terms have yet to be finalized.

Prior oil related contracts in place were renegotiated when natural gas was discovered to reflect the different economic and infrastructure requirements for that resource. Disputes have arisen as to whether the country negotiated sound revised contracts. Even where independent evaluations of the revised supported the contract terms, given higher costs and risks associated with new production,

Case C: A dissatisfaction with the amount and pace of revenues coming into the government during years of large price increases led to new taxes being imposed on the industry, and the obligation of existing contract holders either to sign new contracts or face expropriation.

were still justified. In Case D, the terms of the renegotiations, coupled with additional nationalizations in other industries, resulted in a real aversion to continued investments.

One might conclude that renegotiations (even ones in the context of a partial ownership level change) if based upon real changes in circumstances and in an environment where the government makes it clear it still desires a positive, though changed, ongoing relationship, can be successful and can avoid or at least reduce collateral downside effects. But where done in a less constructive manner, they can stifle ongoing investment and ultimately be counterproductive.

Consequences on Specific Project

investors will view events with apprehension, which could reduce or delay additional investments

Irrespective of whether a country uses

-- available at
<https://s3.amazonaws.com/s3.documentcloud.org/documents/1279596/mining-contracts-how-to-read-and-understand-them.pdf>

--how to read and understand <http://openoil.net/understanding-oil-contracts/>

Handbook on Mining Contract Negotiations for Developing Countries, Volume One: Preparing for Success (April 2015), International Institute for Sustainable Development, available at <http://www.iisd.org/sites/default/files/publications/iisd-handbook-mining-contract-negotiations-for-developing-countries-volume-1.pdf>

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Impacts of Fiscal Reforms on Country Attractiveness: Learning from the Facts:, Lisa E. Sachs, Perrine Toledano, Jacky Mandelbaum, with James Otto, available at:
http://ccsi.columbia.edu/files/2013/11/Impacts_of_Fiscal_Reforms_on_country_attractiveness-Website1.pdf