

LEGAL ALERT

ZAMBIA MINING & INVESTMENT INSAKA 2024

NAVIGATING MINING LICENCES IN ZAMBIA: OPPORTUNITIES AND CHALLENGES



1. Introduction

1.1 I was so privileged and honoured to be requested to do a paper and discuss the above topic as part of the program for the just ended first ever Mining InsaKa from 7 to 11 October 2024. We were challenged to discuss the following subtopics as key take aways:

- (a) Understanding the application process for mining licenses;
- (b) Insights into legal and regulatory compliance;
- (c) The role of stakeholders in licensing; and
- (d) Common challenges and how to overcome them.

1.2 Kudos to my fellow panellists Mr Samuel Maango (Director Mines Cadastre) and Mr Godfrey Mwiinga (Director General at ZEMA) for a lively discussion and for ably addressing the above subtopics. Our moderator Mr Chimwemwe Mwanza (IDC South Africa) was also amazingly on point with directing the discussion in order to bring out the real issues.

1.3 In my presentation I focused on the last two subtopics – (i) The role of stakeholders in licensing and (ii) the Common challenges and how to overcome them – and the following were my main talking points:

- (a) some of the key risks that remain in our licensing system in relation to attracting international investment capital – the investor being the key stakeholder here;
- (b) participation of Government (GRZ) in the mining sector – the Sovereign being the key stakeholder here; and
- (c) local content and domestic wealth creation – the Zambian citizen being the key stakeholder here especially for social licence reasons.

2. Investment Capital Challenges

2.1 Although Zambia has one of the most modern regulatory frameworks allowing for technocrats to run the licensing regime as well as operating a digital portal for ease of access to information, key persistent but controllable risks remain to both exploration investment capital and mining investment capital.

Exploration

2.2 The real value or underlying asset for an exploration tenement includes (i) the capital investment (ii) information generated from activities (iii) the option to acquire an interest in the licence. The Zambian legislation, however, does not appear to recognise these key aspects of the constitution of an exploration investment and essentially leaves everything to be decided by contract between the parties. This normally leaves investment capital vulnerable especially if there is a dispute and an incompetent tribunal with no experience in mining handles the dispute.

2.3 The regulator that does not recognise the risk exposure of investment capital due to the absence of specific legislative provisions also means that there is no express protection of investment capital for the investor especially where the investee licence holder acts fraudulently.

2.4 Legislation, therefore, needs to recognise that the contractual interest in the licence (such as a farm-in or joint venture etc.) plays a pivotal role in the value creation process to the extent that legislation needs to facilitate for the creation of the proprietary interest in these which are easily recognisable – for instance an easy to implement registration process that requires the consent/intervention of the interest holder before the licence can be surrendered, cancelled or disposed of would enhance risk mitigation (Australia)– commercial interest holders should not rely on the current area blocking process to protect their rights (Zambia).

Mining

2.4 In relation to mining, three key risk

issues stand out. Firstly, the real asset in a mining licence is the extent and value of the ore body as opposed to the contractual arrangements attached to the licence (except of course the financing arrangements) or the licence itself. The rights to the ore body may be lost for failure to comply although Zambia provides for an opportunity to comply before revocation to enhance security of tenure in this respect.

2.5 What appears to be missing in Zambia are express provisions in the law which provide for instances when revocation may be undertaken for another reason (e.g. change of law or policy) to the extent that at least what the investor has invested must be refunded to further enhance security of tenure (Australia, Tanzania, Zimbabwe, etc). This would partly dispense with the adverse sovereign risk assessment in this respect and should not be too difficult to introduce as there is similar express legislation with respect to land.

2.6 Secondly, Zambia has not done too well in engendering stability in some of the key areas of concern for mining investors until the recent past – the licensing regime and tax policy have been stable for at least 5-8 years. For investors stability is key and Zambia now appears to have embraced this and is on a good trajectory. As a counter weight to the lost reputation, Zambia should consider accommodating the concept of stability agreements for the additional assurance for certain large scale investments especially in light of 3 million tonne per annum target or copper metal production.

2.7 The stability agreements should not be confused with the previous development agreements which were mostly incentivisation or concession agreements. The main and singular objective of a stabilisation agreement as the name suggests would be to offer the investor stability with respect to the existing parameters so that the investor has a real chance to recoup some returns on the investment made.

2.8 Lastly, administrative refinements which are crucial for implementing and delivering government policy (e.g. 3 million tonnes copper metal production) are required in certain critical areas otherwise risk remains to disincentivise international capital investment. The uncertainty around timeous refunds of import VAT, determination of contribution to the Environmental Protection Fund, security of power supply, security of mining tenure, etc., all trigger the exacerbation of cost of doing business which could render Zambia an

uncompetitive destination. It is important, therefore, to align the implementation side of government role with its ultimate objectives for the mining sector.

2.9 It is noted that one of the key objectives of the Minerals Regulation Commission Bill, 2024 (MRCB 2024) – which we understand has been briefly withdrawn for further consultation – was to enhance administration and we look forward to its eventual implementation.

3. Government Participation

3.1 One of the key investor concerns with the MRCB2024 was mainly the role of GRZ in the mining sector. GRZ can play many roles including (i) as ultimate owner of the mineral resource (ii) as administrator or facilitator (iii) as investor (iv) as taxing authority (v) as intermediary, etc. The rules of participation in each case need to be clear, however, otherwise this could present material risk to the sector, in and of itself. The concern is mainly around the need for GRZ to participate as an investor in line with commercial practice and law.

3.2 Following privatisation of the mining sector in the late 1990s to early 2000s, GRZ policy has generally appeared to have been the retention of minority stake through ZCCM Investment Holdings Plc (ZCCM-IH) in the privatised mining operations while permitting private sector to drive new mine developments. This has boded well for new mine projects in an environment where GRZ has largely participated as regulator.

3.3 We understand under the MRCB2024, however, that GRZ is looking to participate in new projects as an investor for at least 30% threshold (Target) throughout the mining value chain from exploration, mining, marketing, transportation etc., through a new special purpose vehicle other than ZCCM-IH. It would appear that the ZCCM-IH investment objective will be mainly limited to legacy interests of GRZ

3.4 We don't see anything wrong with GRZ venturing to participate in the mining sector beyond its sovereign right as regulator. What is key, however, is for GRZ to recognise that there are different rules that apply to each type of participation.

3.5 As an investor, it would be important for GRZ to comply with investment norms which require the contribution

of value as mainly regulated by commercial law and property law (encapsulated under international investment law). This should not be confused with its powers as a sovereign to regulate (and not participate) under administrative law as a tool for acquiring a commercial advantage – as this may ultimately result in existential distortion of the sector.

4. Domestic Wealth Creation and Liquidity

4.1 There are two major opportunities to discuss under here namely (i) GRZ facilitation for wealth building at the national level and (ii) GRZ facilitation of wealth creation at the individual level.

National Level

4.2 In order for GRZ to participate with recognisable value alongside the major investors, it is important for GRZ to establish a capital base. Whether GRZ is doing this at the early stage or subsequently in the investment journey of a mining project.

4.3 As most resource endowed countries have done, GRZ may need to consider establishing a sovereign wealth fund (SWF) for better interface between what it collects as a sovereign to fund its long-term participation in the sector so as to avoid any distortion (Norway). The SWF, which should have been established a long time ago in Zambia, could source funding from licence auction sales, mining taxes, fees, etc., would give GRZ versatility to invest in any sector in Zambia, as opposed to just mining, including the ability to shield citizens from shocks such as droughts or market instability for commodities and could also help GRZ to be more deliberate in focus (e.g. on education or skills development, etc).

Micro level

4.4 Secondly, GRZ needs to facilitate for growth at the individual or micro business level in relation to participation in the mining sector. Local content policy is a good default position and could also be a good start for Zambia if well balanced and researched framework is put in place.

4.5 Real wealth creation, however, is about ownership and not merely supplying to the owners of capital. We consider that GRZ is able to facilitate for this in a fair and commercial way as a route to the acquisition of wealth by

Zambians without disturbing the current ownership structure or intruding on the existing ownership rights. This is also an important social licence issue.

4.6 One area where speculative capital is already been attracted into Zambia in considerably significant fashion is at the exploration level (apart from the small scale level where Zambians are given preference). The participation by Zambians is sometimes fraught with short termism and outright fraud from our experience. All this can be organised as good entry point for citizens.

4.7 By their inherent nature exploration licences are prone to speculation especially if there is a high chance that they are prospective. Good and helpful speculation must be encouraged in order to create value and a market for capital to come to this sector – currently there is limited regulation on how parties can ethically engage and the Cadastre would be a good platform for setting and implementing such rules to convert this sub-sector into an economically vibrant sector.

4.8 Our proposal is for GRZ to facilitate for the creation of a mining right trading platform mainly with at least a primary market and a secondary market focused mainly on exploration licences. These get traded more often than actual mining licences and there is usually little transparency in the valuation as well as Zambian participation on the upside in terms of capital gains or ultimate conversion into a profitably producing mining licence.

4.9 The primary market, were GRZ is issuing the licences for the first time, could give priority to Zambians, joint ventures involving Zambians, foreigners with investment licences, etc just the way it already is for surface rights but this time around with a proper selection process for participation and commitment. At the heart of the primary market could be concepts like original overriding royalty interest (ORI), profit or capital share rights (PCS), Net Smelter Royalties, (NSR) etc., which could be prescribed, traded on the secondary market or lost when the exploration licence expires (e.g. the PCS may be prescribed at 3% with a percentage each going to the original owner, the community, and the SWF).

4.10 The secondary market should provide the requisite liquidity for trading the licences and should essentially have no preferences and those with capital including foreign participants will obviously have an advantage but the ORIs,

PCSs, NSRs (no matter how small in percentage) will provide a level of real wealth creation for the Zambian participants.

4.11 The setting up of such a trading platform will come with many other advantages such as reduction of fraud, transparency, price discovery, etc., and would not be too challenging for Zambia to set up as it already has a reasonably well functioning cadastre system with digital access through the mining portal. What is missing is the framework to provide for escrow services, listing services, etc., and a consultation process preceding the setting up of the platform and concept.

5. Summary

5.1 Some of the key risks that remain in our licencing system in relation to attracting international investment capital – the investor being the key stakeholder here – include the following:

(a) Absence of recognition of underlying assets and derivative rights for exploration licences which may require to be fixed through a statutory amendment;

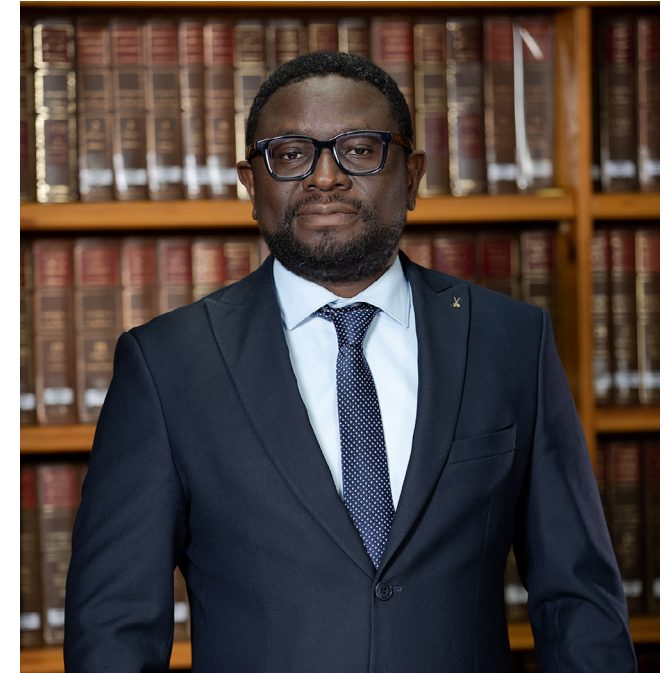
(b) Absence of policy stability especially for large scale investment in the sector which could be overcome contractually;

(c) Lack of refinement in administrative processes that facilitate mining investment, such as tax refunds, environmental funding obligations, security of power supply, security of tenure, etc., which may simply require raising administrative standards;

5.2 Participation of GRZ in the mining sector – the Sovereign being the key stakeholder here – needs to be streamlined so that it is clear that when GRZ is participating as an investor it will add commercial value to a venture or project and the establishment of a SWF could be a crucial vehicle in order to achieve this goal.

5.3 Domestic wealth creation – the Zambian citizen being the key stakeholder here especially for social licence reasons – would require a lot of creativity for better scaled up Zambian participation within the shortest possible time over and above local content policies; and we think a mining right trading platform aligned with this objective might be an opportunity.

We hope you found this alert useful. Please contact our Senior Partner, Charles Mkokweza at CMkokweza@corpus.co.zm if you have any questions relating to this legal alert.



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