An approach to defining, measuring and monitoring local procurement by the mining industry

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This brief guide is designed to assist stakeholders to develop a practical and fair system for defining, measuring and monitoring local procurement in the mining sector. It is primarily targeted at mining companies and regulators who wish to implement a common measurement system in order to optimise local procurement.

The approach has been developed as a result of a number of strategy and implementation projects conducted in Africa by **Kaiser Economic Development Partners** for the World Bank, involving extensive consultations with governments and mines across the continent. Many of these principles are also likely to apply in other locations. Further detail can be found in the World Bank report, *Increasing local procurement by the mining industry in West Africa (2012)*.

A common definition for 'local procurement' is required

Whilst the broad objectives are generally well accepted, one of the fundamental challenges in developing any local procurement programme is **the lack of a common understanding of what constitutes 'local' content, or a 'local' supplier**.

Historically, mining companies, governments and other stakeholders have adopted a wide variety of approaches for defining a 'local supplier' and these have often failed to consider important factors that will encourage sustainable economic benefit to local citizens.

The reality is that there are three distinct aspects that make up the concept of 'local':

❶ The level of **participation by local citizens** in the company	❷ The level of **value addition**	❸ The **geographical location** of the company
Across ownership, management and employment	Whether a product is manufactured locally, or a service is delivered locally	Within the vicinity of the mine, nationally or in the wider region.

Each of these critical elements relate to important (and different) areas of benefit to local economies: genuine involvement of local citizens, job creation through value addition, and emphasis on the most appropriate geographical focus. **By simply looking at locally-registered companies, for example, most of these potential benefits will not be captured.** Therefore a system is required that considers all of these elements in a simple and practical way.

It is particularly important that a **common approach is adopted across stakeholders**. This will ensure equal treatment of mines and suppliers, and will also allow a consistent approach to maximising development impacts. In addition, it provides a basis for comparing performances across mining companies, and eases the burden of information gathering and reporting.

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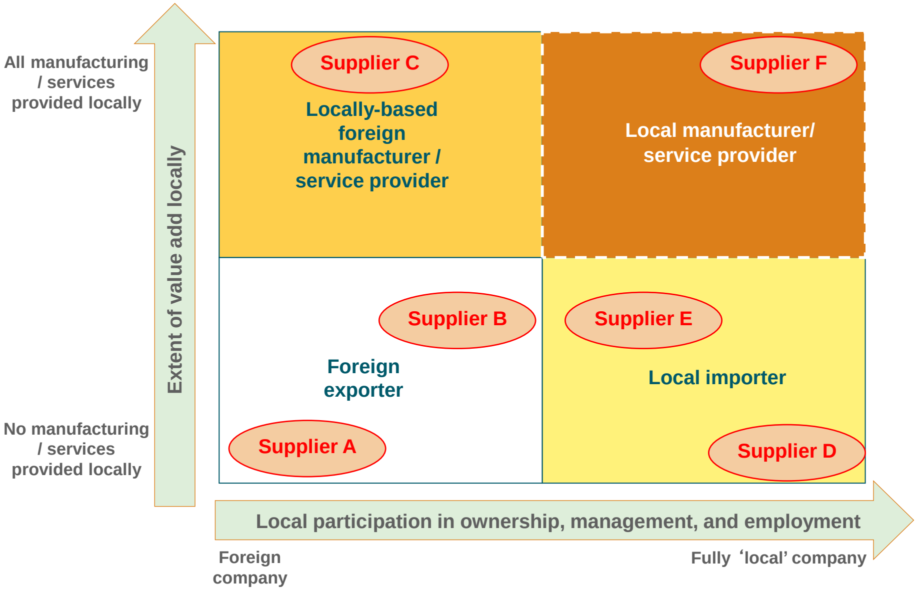
Kaiser EDP provides insight and strategic support to address some of the most crucial economic development issues facing Africa. Our local procurement work includes advising on local procurement regulation, mine local procurement strategy, and supporting supplier development. For further information contact Rupert Barnard: rbarnard@kaiseredp.com

Categorising suppliers is the most practical approach to measuring local content levels

Based on Kaiser's experience in Africa, **categorising suppliers** is a more practical approach than measuring the local content of individual contracts, given the level of administrative and reporting effort required. This approach can be integrated into vendor classification systems and reports generated from existing procurement systems. The **framework below** can be used to **evaluate mining companies' procurement spend according to different categories of suppliers** based on combinations of local participation and value-addition (introduced above). For simplicity, it assumes a geographical definition of local as 'national' (the strong preference of many stakeholders).



Some **examples of suppliers** within the framework are:

- **Supplier A** is a company which has limited or no participation by local citizens and does not manufacture its products locally (or provide services from a local base). This supplier would therefore be considered a 'foreign exporter'. Note that **Supplier A** may well be registered locally and may also have some type of local presence (e.g. a sales office), and may even have some local employees.
- **Supplier F** is on the other end of the spectrum: this is a locally-owned company, with local management and employees, which manufactures its products locally.

The other categories are also very important to track as they represent important *degrees of 'localness'*. **Supplier C**, for example, is an internationally-owned company which is manufacturing products locally (or providing services from a local base). Arguably this company is providing a greater socio-economic impact than **Supplier D**, which may have high levels of local ownership, management and employees but is simply importing products and selling them to the mines.

The dividing lines that define the quadrants above require development of **thresholds**. These thresholds should ideally be agreed upon through national consultative processes in order to take into account local regulatory and economic conditions. However, some principles to consider are set out below:

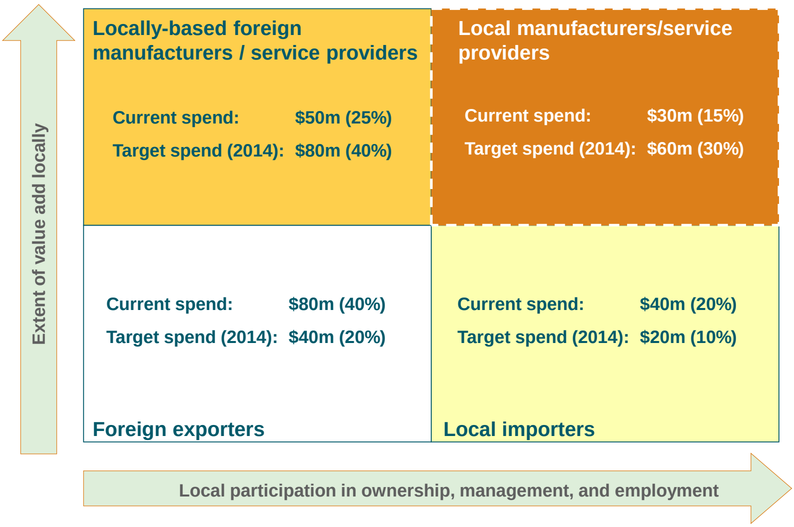
- **Participation**: significant participation from local citizens across all three areas of ownership, management and employment (e.g. 50% ownership, 85% management, 90% employment)

- **Value addition** (based on a supplier's *predominant activities*):
  - For manufactured products, value-adding companies are those who are involved in local manufacturing activities (i.e. where the majority of their products are being 'substantially transformed' locally) rather than importing/trading activities
  - For services, value-adding companies where the majority of the service is undertaken, managed and controlled locally rather than provided from elsewhere

This approach flows through to local procurement planning and monitoring

The local procurement definition and model set out above can form the basis for mines developing **local procurement plans** in terms of **target setting and approaches to preference**, and government and other stakeholders having a consistent approach to **monitoring and evaluating** progress around local procurement. The clear overall principle is that preference should be given to companies which demonstrate **higher levels of local value addition**, **stronger participation by local citizens and geographically located in the same country as the mine** (assuming quality, price and scale requirements can be met).

Once a mining company categorises all of its suppliers into the above four categories, it will be able to determine its current **spend in each category** as well as begin the process of **setting targets** and putting plans in place to increase the spend in the categories of the framework, as illustrated in the example below:



The **development of indicators** that reflect current and future (targeted) local procurement spend by the preceding categories can be used to form the foundation for **monitoring processes by Chambers of Mines, governments and other stakeholders**. There are a number of elements that need to be tracked on an ongoing basis (and captured in a mine's local procurement plan); these are summarised as follows:

- Current spend (distinguishing between capital and operational) for each category of supplier
- Number of contracts for each category
- Target spend and number of contracts
- Short term (2 years), Medium term (2 to 5 years), Long term (5 to 10 years)
- For each of the preceding types, both national (the primary measure) and regional information could be captured.

Implementation considerations

In consultation with many mining local procurement stakeholders in Africa, Kaiser has developed a number of considerations and principles when implementing this framework for consideration.

- The framework (including thresholds) is likely to be most effective when finalised and adopted through a **consultative process involving the private sector, civil society, national government and regional organisations**. This framework should also be reviewed and updated, as improved processes and information become available and can be incorporated.
- Any regulation around local procurement should ideally be aligned with the framework for measurement, targeting and monitoring local procurement.
- A **central co-ordinating body** (e.g. a national Chamber of Mines) can play a key role in supporting implementation, for example in developing a common supplier list that includes information required to measure local procurement and categorises suppliers accordingly. This process could also draw on mines' vendor questionnaires, which would need to be adapted to request the required information.
- The framework can be applied to break down **spend by main contractors** (including EPCs, mining contractors, camp management) to encourage procurement from local sub-contractors.
- Mines should develop targets annually and report on these annually to the national mining regulator. Regulators should play a role in collaborating with mines on where targets can be increased or performance improved.
- When applying the framework for measuring local procurement spend, mines and governments should act in the spirit of increasing local procurement. For example, the calculations would not need to cover 100% of spend, but should cover at least 80% of spend. Also, specifically relating to fuel (which tends to be a large spend item), it should be excluded from calculations to avoid detracting from other spend items (although associated products and services should be included, for example fuel logistics and lubricants).
- Mining procurement efforts should ideally be coordinated with other areas of preferential procurement to maximise the socio-economic benefits and sustainability (e.g. public procurement and oil and gas).
- Mines, governments and civil society need to work together to build capacity to implement and monitor the measurement framework.

<u>Note</u>: these principles are based on experiences in Africa; different approaches may be applicable in other regions based on local conditions.