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Land-Based Investment in Developing Markets: Pitfalls and Legal Considerations

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Background – Framing the Issue

Increased Land-Based Investment: Economic downturn and food price shocks have led to increased investment in developing countries, especially Africa

Undocumented Rights, Weak Frameworks: In many of these countries, the land governance framework is weak and rights are not documented. Customary and/or communal ownership structures prevail. Land markets are underdeveloped, and local government lacks capacity to deal with investors.

Increased Risk: Investing in these vulnerable areas can displace, disadvantage, or negatively impact local communities, and lead to financial, operational and reputational risks for the investor.

This Leads To…. ***Different Legal Considerations, Unique Challenges***

So What? Why Make the Extra Effort?

Human Perspective – land deals have the capacity to significantly disadvantage smallholders, for whom land is not just a place to build a house, but a source of livelihood, cultural heritage, power, and status.

Economic Equilibrium of the Contract - Investors often given long term rights to extensive areas of land, while host country benefits are limited and ill-defined, and local landholder benefits are often non-existent.

- **Resulting Contract Risk -** Where the economic equilibrium of a contract is disturbed, it creates a misalignment of incentives, and can increase the likelihood of a beneficial breach.
- **Resulting Project Risk –** An investor who loses the social license to operate will face protests, damaging of equipment, violence, etc… and this has real implications on the project.

Before Jumping In: A Few Words of Caution

This presentation is food for thought - we don't have all the answers yet. Why?

The field is new

- Investment has happened before, but not at current pace
- Investors are under more pressure now to be socially responsible

Lack of good contract models, no transparency

Every deal is different – context is incredibly important

Due Diligence and Community Consultation

Diligence room won't be enough – In this context, you can't reply on documents from a diligence room in your NYC office. Need more robust, sociological due diligence.

- **Thorough stakeholder analysis:** Need to do a thorough stakeholder analysis, because land ownership and use is often not as straightforward as in Western regimes. Customary overlaps with statutory, legal vs. legitimate, etc.
- **Identify critical and under-represented stakeholders –** Women, indigenous groups, youth, elders, seasonal land users. Etc…

Take your time – Visiting a village once is not enough.

Contract Negotiation

Who are you negotiating with? Legal vs. Legitimate Land holders

- **Legal Landholder** is the person or entity who, by law, owns the underlying rights to a piece of property. It's the person whose name will be on the lease or purchase agreement. Usually this is the Central or Regional Government.
- **Legitimate Landholder** is someone (or a group of people) who has used the land for generations, in relying on the fact that for all practical purposes, the land is theirs. It's the local community

Legal ways to bring "legitimate" landholders into the contract

- Tri-partite agreement (investor – state – community)?
- Side MOU agreement? If so, how to ensure adherence?

Compulsory Takings, Impacts on Local Communities

Land-based investment contracts often necessitate a compulsory taking of land, which can greatly harm local communities.

Broad Definition of "Takings to Satisfy a Public Purpose" –leads to greater powers of compulsory acquisition.

Informality and lack of documentation of local landholdings – Can lead to harsher consequences for local populations, who bear the negative externalities of the project but are not properly compensated for these adverse impacts.

Delivery of Compensation – For what? To whom? How? In what form?

Compensation for what?

- **Governments:** Land; Improvements on land; Natural resources
- **Communities:** Resettlement; economic loss; livelihoods

Types of Compensation Arrangements: Cash vs. profit sharing vs. land for equity vs. other joint venture-type arrangement.

- **Governments:** Cash? Infrastructure? Land for Equity?
- **Communities:** in ESG circles, one-time cash payment is considered the worst. In-kind compensation (e.g. better or equal plot of land + covering any transaction costs involved) is preferred.

Delivery of Compensation to Local Communities – Special Considerations

ESG Standards Say – Compensation should be fair, prompt, and adequate.

Delivery of compensation to local communities - to whom, by which method? Who controls distribution and allocation? Who are the beneficiaries? When is compensation delivered?

- **Community trust funds:** Who runs them? How to reduce corruption?
- **Timing of compensation:** Up-front? When project operations begin?

Host Country Instability – Stabilization Clauses and Other Safeguards Against Adverse State Action

Stabilization clauses: commit the government not to change the regulatory framework governing the investment in a way that would disadvantage the contract. Can take many forms.

Robust transfer rights - Another common method is having robust transfer rights, thus allowing the investor to exit.

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Selection of Other Important Legal Considerations

Alternatives to acquiring land: contract farming or out-grower schemes – Contractual partnership established between a company and local landholders for the production of a commodity

Tiered land acquisition vs. all at once – acquiring large tracts of land is disfavored because it disadvantages the community, but how do you ensure tiered acquisition?

Land Valuation in thin markets – alternatives to comparable sales method.

Payment for Infrastructure Upgrades – who pays?

Emerging Issues: Interaction Between Contract, National Law, and Investment Treaties

***Emerging legal argument** that investment treaties can sometimes stand in the way of positive land reforms in developing countries*

- Investment treaties are primarily aimed at **protecting foreign investment against adverse state action**, allowing investors to **seek compensation for state conduct that breaches these standards –** *Cotula, 2015*.
  - *Cotula, 2015:* Investors have used investment treaties to **challenge land reform**, if it means adverse impacts on the investment.
- **Land grabbing**: the legal protections enshrined in investment treaties could protect one-sided land deals against legitimate land claims from local or indigenous peoples.
- **Conflicts with national law:** Investment treaties can remove restrictions on foreign acquisition of land, even if national law treats foreigners differently from locals.

Concluding Remarks: Process is Critical

- How do you actually negotiate the contract, with whom, in what way?
- How do you ensure proper communication and consultation?
- Legal protections may not be enough in the face of community unrest, protest, or violence. The social license to operate is paramount

THANK YOU!