

# ENGINEERS AGAINST POVERTY

## Policy Review: Local Content Bill for the Nigerian Construction Industry *Final Report*

Bernadine Fernz, John Hawkins, Petter  
Matthews and Jill Wells

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## **Authors**

This report has been produced by Bernadine Fernz, John Hawkins, Petter Matthews and Jill Wells of Engineers Against Poverty for GEMS2.

Authors.....	i
Executive summary .....	iii
Background .....	5
Findings .....	7
1. Purpose of the Bill: Objectives and Definitions .....	7
1.1 Objectives .....	7
1.2 Definitions: .....	9
2. Requirements of the Bill .....	12
2.1 Lack of clarity: .....	13
2.2 Scope of application .....	13
2.3 Phasing of development of local content plans.....	14
2.4 Setting targets .....	14
2.5 Monitoring and reporting .....	15
2.6 Penalties and Incentives .....	16
2.7 Training and Capacity Building.....	16
3. Operational and administrative effectiveness.....	17
3.1 Nigerian Content Plans .....	17
3.2 Balancing competing objectives .....	19
4. Anticipated impacts .....	21
Recommendations.....	23

## Executive summary

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A Bill seeking to establish a Local Content Act for the Nigerian construction industry is currently at the committee stage of the lower chamber of the Nigerian legislature – the House of Representatives. The purpose of this review is to provide GEMS2, working through partners such as the Nigerian Engineering Leadership Forum, with a number of recommendations based on best practice that could be used to advocate improvements to the proposed Bill.

The review has established a number of key findings:

1. The provisions of the Bill are based on an enterprise approach. This does not reflect the value added definition of Nigerian Content whereby the whole supply chain (enterprises, material suppliers and workers) benefit.
2. As it stands, the Nigerian Content Bill does not have clear objectives or express requirements that comprehensively prescribe the increased participation of Nigerian people in the construction industry.
3. The Bill lacks clear and practical definitions (such as what constitutes a Nigerian firm and ‘first consideration’ to be given to Nigerian Firms in the “award of general contract”) that are needed to help achieve its objectives.
4. The Bill is based on the Oil and Gas Industry Nigerian Content Act (Act) and as a consequence does not reflect the characteristics of the construction industry.
5. Unlike the Act, the Bill does not include quantifiable targets for Nigerian content. Instead, the Nigerian Content Construction Industry Monitoring Board (NCCIMB) is expected to set these targets.
6. The requirement for the proposed NCCIMB to approve a local content plan for every single construction project is impractical, particularly as it covers both the public and private sector.
7. There are concerns that the appointment of the Minister for Public Works and Housing as Chair of the NCCIMB Council could lead to a conflict of interest. The Ministry will be including Nigerian content in their contracts.
8. The proposed requirement for training and capacity building based on a test of reasonable effort is weak.
9. Public procurement officials are likely to be concerned with the potential conflicts between the Bill and the requirements of the Public Procurement Act 2007.
10. There is an absence of data to be able to quantify potential impacts on employment generation and income improvement.

This review outlines a number of different examples that could be used to improve the Bill based on examples of legislation principally from South Africa and Queensland, Australia. These are summarised below as recommendations for discussion with GEMS2 and the Nigeria Engineering Leadership Forum:

1. Amend the Bill to include clear objectives that support the value-added definition of Nigerian Content including enterprises, workers, and material suppliers.
2. Improve the Bill's definitions to:
  - Reflect the various categories of business, levels of ownership and employment, to safeguard against perverse outcomes.
  - A more practical definition and measure of 'Nigerian content' to improve likely application.
3. Apply the provisions of the Bill only to public sector contracts above a set threshold
4. NCCIMB should establish Nigerian Content targets for labour and material suppliers as well as enterprises through detailed policy guidelines as the Bill currently anticipates. Alternatively, these targets could be included in the legislation if this is more likely to lead to better compliance.
5. Insert clearer obligations and conditions for training and skills development to ensure the capacity of the Nigerian workforce is fully developed. Ownership of this responsibility needs to be established and effective strategies put in place to grow capacity and monitor compliance.
6. Establish a clear incentive, penalties and monitoring framework within the Bill.
7. Require that NCCIMB
  - Review the local content plans of procuring entities (rather than firms) and /or
  - Undertake retrospective reviews of local content performance.
8. The NCCIMB Council Chair should be an independent person who does not have a potential conflict of interest.

It is important to point out that legislation on its own will not deliver improved local content in the construction industry. Strong policy and adequate enforcement are required to ensure effective implementation of local content requirements. In developing these instruments, the multiple options and pathways for local content require careful consideration and must be adapted to suit the unique characteristics of construction industry and to fit into the Nigerian context.

## Background

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Foreign construction firms dominate the construction market in many developing countries and they often source equipment, materials and even labour from their own home country. As a consequence locally owned contractors, consultants, material and equipment suppliers, and workers often do not benefit from the investment in the construction sector. The African Development Bank reported that less than 40% by value of new works contracts in 2006 were awarded to companies from Sub-Sahara Africa (African Development Bank, Annual procurement report, 2006).

A Bill seeking to establish a Local Content Act for the Nigerian construction industry is currently at the committee stage of the lower chamber of the Nigerian legislature – the House of Representatives. This follows the establishment of the Nigerian Oil and Gas Industry Content Development Act 2010. Since the Act came into force, there has been a marked increase in the award of contracts to Nigerian companies. But only 12-18% of contract sums has been spent on Nigerian made goods. The Nigeria Content Monitoring Board believes that without developing a manufacturing base there will be no further Nigeria content growth and no employment growth. This highlights the challenge of developing legislation for the construction industry which will not only increase the percentage of contracts awarded to Nigerian owned firms but have the added value of job creation.

The Nigerian construction industry has registered quite significant growth over the past few years and output is expected to continue to grow so long as oil prices and government investment remain high. But the contribution of construction to GDP and employment appear still to be very low by international standards. As in many other low income countries there are numerous reports of serious problems in the industry, including excessive time and cost overruns, poor quality construction, abandoned projects and widespread corruption. The supply of materials is reported to be substantially less than the demand with most steel and much of the cement having to be imported (Dantata 2008). An additional problem may lie in the fact that local manufacturing is high cost and cannot compete with cheaper imports, due in part to the erratic supply of power.

As is common in other African countries, the industry is extremely diverse. At one extreme is a formal organised part comprising publicly funded construction projects and projects funded by large private companies, mostly in the oil and gas and hotel industries. At the other extreme is a large and largely unregulated sector comprising numerous small privately owned projects many of them residential and often referred to as the 'domestic' sector of construction. Foreign companies dominate in the organised part of the industry (public and large private projects) together with a handful of large Nigerian firms, some of which originated as joint ventures with international firms. In the unregulated sector, construction is carried out by small local enterprises or more frequently by artisans and gangs of labourers hired and supervised by the building owner. The government has no significant influence on the operations of this sector for which there is virtually no reliable data (ibid).

This review has been commissioned by GEMS2 which is a project funded by the UK Department for International Development and jointly managed by the World Bank and Coffey International. GEMS2 is focused on improving incomes and creating jobs in the Nigerian construction and real estate sector. It employs advocacy strategies capable of delivering changes in the business environment of the sector to make it work better for the poor.

The purpose of this review is to provide GEMS2, working through partners such as the Nigerian Engineering Leadership Forum, with a number of recommendations based on best

practice that could be used to advocate improvements to the proposed Bill. To achieve this, the review will establish the following:

1. The purpose of the Bill: Definitions and Objectives
2. The requirements of the Bill
3. The operational and administrative effectiveness of the Bill
4. The potential impact of the Bill.

# Findings

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## 1. Purpose of the Bill: Definitions and Objectives

### 1.1 Definition of Nigerian content

Local content can be defined in terms of the ownership and/or location of the enterprises involved in production and/or the value-added in the production process. In construction, local content can be defined to include the involvement of local enterprises and labour in planning, design and construction services, as well as the locally added value in transactions occurring throughout the contractors supply chain (Wells and Hawkins, 2008). Local in this context is understood to mean national, but it could be defined to mean any geographic or administrative area.

The definition provided for “Nigerian Content” in the Bill follows the value-added approach:

“The quantum or composite value added to or created in the Nigerian economy by a systematic development of capabilities through the deliberate utilisation of Nigerian human, material resources and services in the Nigerian Construction industry”.

The Bill’s draftsmen should be congratulated for taking the added value approach as this is more likely to create employment and develop enterprises throughout the supply chain. In terms of application, an additional sentence or some minor amendments stating what constitutes Nigerian Content would be helpful. The definition below from the Queensland Industry Participation Policy Act 2011 policy guide provides a useful example.

“Local content refers to goods, services and labour provided by businesses located in proximity to the project site... and can be extended to include adjoining regions, the whole of the State, other States and Territories [in Australia]”.

This is a clear and concise definition which can be easily understood and effectively applied. In addition to a sound definition, clear guidelines of what constitutes Nigerian content are required to assist interpretation and application. This will help give legislation and policy a clear focus, and enable more effective implementation. Box 1 provides a further example of a definition of local content from South Africa.

#### **Box1: Definition from South Africa B-BBEE Act**

For an alternative approach, consider also South Africa’s definition of “Broad-Based Black Economic Empowerment” (B-BBEE) in the 2003 Act, which can be amended to apply to Nigerian peoples. The definition adopted for “Broad-Based Black Economic Empowerment” is the “economic empowerment of all black people including women, workers, youth, people with disabilities and people living in rural areas through diverse but integrated socio-economic strategies that include but are not limited to –

- a) Increasing the number of black people that manage, own and control enterprises and productive assets;
- b) Facilitating ownership and management of enterprises and productive assets by communities, workers, cooperatives and other collective enterprises;
- c) Human resources and skills development;
- d) Achieving equitable representation in all occupational categories and levels in the workforce;
- e) Preferential procurement; and
- f) Investment in enterprises that are owned or managed by black people”



In order to be effective, any Nigerian Content policy must firstly acknowledge that there are various types and ways of delivering local content and secondly provide a method for measuring or assessing the extent that local content is delivered according to each category. Lessons can be drawn from the B-BBEE Codes of Good Practice which adopts a 'scorecard' system for assessing Local Content (see Box 2). This could be a useful and relevant mechanism that can be adopted to assess and distinguish between the different types and levels of Nigerian content.

Secondly, the Bill stipulates that the NCCIMB will provide guidelines, definitions and measurement of Nigerian content and a Nigerian content indicator. This should clearly specify national priorities for improving Nigerian content participation including labour and material suppliers as well as enterprises to ensure the value-added definition is realised.

#### **Box 2: South Africa B-BBEE Scorecard System**

B-BBEE Codes of Good Practice 'scorecard' system for assessing Local Content. The scorecard consists of 7 elements, representing the different ways in which local content might be delivered. Each element is weighted (reflecting the priorities for local content development in South Africa) and assessed against a number of indicators. The 7 elements and potential indicators for assessment are:

1. Ownership; measures the effective ownership of enterprises by black people
  - a. Potential indicator: the extent of exercisable voting right in the hands of black/Nigerian people
2. Management Control; measures the effective control of enterprises by black people
  - a. Potential indicator: the level of Board Participation, Management Control and Non-Executive Board Membership by black/Nigerian people
3. Employment Equity; measures initiatives intended to achieve equity in the workplace
  - a. Potential indicator: the percentage of black/Nigerian women in employment
4. Skills Development; measures the extent to which employers carry out initiatives designed to develop competencies of black employees
  - a. Potential indicator: the expenditure on education or training programmes (e.g. scholarships and bursaries) for black employees
5. Preferential Procurement; measures the extent to which enterprises buy goods and services from suppliers with strong B-BBEE recognition levels
  - a. Potential indicator: the procurement spend from suppliers that are Nigerian owned or managed. For example, procurement from a firm that is 50% Nigerian owned will score greater points than from a firm that is only 30% Nigerian owned.
6. Enterprise Development; measures the extent to which Enterprises carry out initiatives intended to assist and accelerate the development and sustainability of other Enterprises
  - a. Potential indicator: size of contributions (monetary or otherwise) to beneficiaries with the intention to assist or accelerate the development, sustainability and financial and operational independence of those beneficiaries.
7. Socio-Economic Development and Sector Specific Contribution; measures the extent to which enterprises carry out initiatives that contribute towards Socio-Economic Development ... that promote access to the economy for black people
  - a. Potential indicator: size of contributions (monetary or otherwise) in favour of beneficiaries with the specific objective of facilitating sustainable access to the economy for those beneficiaries.

The performance of an entity is measured or 'scored' using this scorecard system, receiving points based on its performance for each element. Based on its local content score on the Generic Scorecard, the entity is then assigned a rating or 'B-BBEE status'.

## 1.2 Definition of Nigerian Firm

The Bill for Local Content in the Nigerian Construction Industry lacks clear and practical definitions that are needed to help achieve its objectives. As well as Nigerian Content, only four additional terms are defined: “Minister”, “Nigerian Firm”, “Partner”, and “Plan”. Many other terms and words not defined here could give rise to ambiguity or misapplication of the Act. For example, “Alliance Partner” is not defined in the Bill and it is unclear if this is synonymous with “Partner” which is defined in the Bill.

The definition of a “Nigerian Firm” as one where 100% of the shares are owned by Nigerians is highly restrictive. There are broader categories of ownership which should be taken into account, including firms that are:

- Part owned by locals with local majority stake
- Part owned by locals with foreign majority stake
- Owned by foreign capital but located in country (Nigeria)

Part-ownership can be especially important where such partnership with foreign firms can help facilitate knowledge and skills transfer. Nonetheless, it would seem that these ‘lower’ levels of Nigerian ownership cannot be treated the same as ‘wholly owned’ Nigerian firms. What this means is that clear policy guidelines are required to prescribe the qualification criteria for Nigerian ownership i.e. whether firms have to be ‘wholly owned’ by Nigerians (as stipulated in the Bill), or whether some other form of ownership or partnership with foreigners could also apply.

Further complexities arise when comparing firms with different ‘types’ of Nigerian content - ownership, management, employment etc. For example, a project proponent might have to consider bids from firms that are:

- wholly owned by Nigerians, but staffed by foreigners
- part-owned by Nigerians but staffed by Nigerians
- foreign owned but wholly staffed by Nigerians

According to the narrow provisions in the Bill, a 100% foreign owned firm that employs 100% Nigerian employees (in non-ownership capacities) is not considered a ‘Nigerian firm’ but a firm whose shares ‘are wholly owned by Nigerians’ yet employs 100% foreign staff qualifies as a ‘Nigerian firm’. This provision advances the objective of increasing the opportunities for Nigerian owned enterprises, but it does little to create jobs or alleviate poverty on a larger scale. It could lead to perverse outcomes where foreign firms that could genuinely contribute to large scale job creation and reduced unemployment and poverty levels are not given adequate consideration. There are also no express provisions against sub-contracting any contracts won to other ‘non-Nigerian’ firms.

Clause 10(a) could also result in similar outcomes. The provision in this clause is extremely vague and does not include any guidance as to what constitutes ‘services provided from within Nigeria’ or ‘goods manufactured in Nigeria’. However, applying the definition of ‘Nigerian firm’ as provided in the Bill, it could be construed that a firm whose shares are ‘wholly owned by Nigerians’, even if it does not employ Nigerians, could qualify under clause 10(a) for services provided from within Nigeria and goods manufactured in Nigeria. As above, this approach will not benefit the majority of Nigerians. It now becomes clear why clear definitions and guidelines are required in order for local content legislation to effectively increase ‘real’ participation of local enterprises and local people.

## Box 5 Case Study: Weaknesses of the Enterprise Approach

### Circumventing Local Content in Malaysia (Global Witness, 2013)

Generally, Local content laws in Malaysia require at least 51% of company shares to be owned by (bumiputera) Malaysians. A recent report by Global Witness found evidence that this local content requirement in Sarawak is routinely circumvented by exploiting the poorest people in the country. First, foreign investors identify a local person willing to act as a nominee (usually someone who is uneducated or living in the rural areas). Through an offshore agreement that is 'untraceable' in Malaysia, the foreign investor then advances a loan (of a nominal sum) to the Malaysian nominee, using the Malaysian 51% shares as collateral against the loan. This agreement transfers control of the shares to the foreign investor who gains de facto control over the company. This means that the company is in reality 100% foreign owned, or at least foreign controlled. The nominee in most cases never requests or regains control of his shares.



Another common practice is the creation of 'shell' companies where locals act as 'front-men' for foreign businesses. Usually, the local company lacks the expertise or capacity to perform the obligations in the contract. The company becomes a 'commission agent' sub-contracting the initial contract to other firms (McCrudden, 2007). This increases costs and waste.

In both these examples, local content requirements prioritising the Enterprise approach did not translate into increased participation of 'local' firms or increased job opportunities for local people or increased skills and knowledge transfer, training or learning. Instead it contributed to time, cost and resource inefficiencies.

## 1.2 Objectives

International best practice suggests that the principal objectives of the proposed legislation should be included in a Bill. As these objectives are absent from the current draft, the authors have to infer, based on the provisions in the draft, that its purpose is mainly to increase the opportunities for Nigerian owned enterprises to win contracts in both public and private financed construction projects. As a result, the value added approach defined in clause 39 of the Bill is unlikely to be realised.

This assumption is based primarily on clause 3 which states that Nigerian firms shall be given first consideration in the award of general contract and in all projects for which contract is to be awarded in the construction industry. "Nigerian Firm" is defined in the Bill as an

“indigenous company or contractors whose company shares are wholly owned by Nigerians”. That such firms should be given ‘first consideration’ (according to clause 3(1) suggests adoption of the ‘Enterprise Approach’ to Local Content, rather than the “Value Added Activity Based Approach”. This suggestion is reinforced by Clause 6 which refers to ‘all construction agreements, contracts and memoranda of understanding relating to any operation in Nigeria’. As pointed out in the GEMS2 concept note, the Enterprise Approach does not necessarily translate into more jobs or opportunities for Nigerians or aid poverty alleviation on a large scale. The Enterprise Approach could create a Nigerian “elite”, increasing economic inequality without providing the envisioned jobs and opportunities for the poorest people. The Enterprise Approach could also create opportunities for corruption and illegality, especially in areas where skills or education levels are low.

Clause 17 of the Bill requires firms to employ only Nigerians in their junior and intermediate cadres (unless the functions cannot be rendered by Nigerians). It is unclear what is meant by cadres and whether this applies to professionally qualified cadres or skilled and unqualified workers. Debates during the 2<sup>nd</sup> Reading of the Bill suggest that the Bill is focussed on skilled professionals including architects and engineers (Premium Times Nigeria, Dec 2012). However, the provision in Clause 17 itself is unclear and it could also apply to unskilled workers. Further clarity is needed as this clause could be really important, particularly as foreign firms often bring in their own workers. There are no specific objectives relating to opportunities for workers beyond this clause or material suppliers save for what is implied in sub-clauses 10(1)(a)-(b). Note that Clause 10(b) also refers only to ‘qualified’ Nigerians.

Based on the provisions mentioned above, the Enterprise approach which is based on firm ownership appears to have been prioritised in this Bill. It is important to emphasize here that without express provision of clear objectives or requirements relating to Nigerian workers or materials, GEMS2 aim of ‘street-level job creation and poverty alleviation for Nigerians’ is unlikely to be realised. This is because the provisions of a Bill are usually interpreted and applied to give effect to its objectives and is particularly important where provisions of a Bill are unclear or silent on a given point. In addition to providing clarity in the event of dispute or uncertainty, clear objectives can also help deter ‘bad behaviour’ as it requires all relevant entities to act in ‘good faith’ in accordance with the intent as well as requirements of the Bill. As it stands, the Nigerian Content Bill does not have clear objectives or express requirements that comprehensively prescribe the increased participation of Nigerian people in the construction industry.

Lessons can be learnt from other models of local content legislation and the Nigerian Content Bill would benefit from including explicit objectives not only pertaining to the Enterprise Approach but also incorporating the Value Added approach. Two examples of explicit inclusion of clear objectives for Local Content are shown in Boxes 3 and 4:

**Box 3 Objectives: South Africa Broad-Based Black Economic Empowerment Act 2003**

Objectives from the South African Broad-Based Black Economic Empowerment Act 2003 include:

- a) Promoting economic transformation in order to enable meaningful participation of black people in the economy;
- b) Increasing the extent to which communities, workers, cooperatives and other collective enterprises own and manage existing and new enterprises and increasing their access to economic activities, infrastructure and skills training;
- c) Promoting investment programmes that lead to broad-based and meaningful participation in the economy by black people in order to achieve sustainable development and general prosperity;
- d) Empowering rural and local communities by enabling access to economic activities, land, infrastructure, ownership and skills

#### **Box 4 Objectives: Queensland Industry Participation Policy Act 2011**

Objectives from the Queensland Industry Participation Policy Act 2011 include:

- a) Maximising employment and business growth ... by expanding market opportunities for local industry;
- b) Developing local industry's long-term international competitiveness, and flexibility in responding to changing global markets, by giving local industry a fair opportunity to compete against foreign suppliers of goods and services;
- c) Driving technology transfer, research and development, innovation and improved productivity for local industry ..., to enhance value for money]

## **2. Requirements of the Bill**

International best practice indicates that there are two approaches to establishing local content requirements:

1. The legislation contains detailed requirements and prescriptive targets for local content participation or
2. The legislation sets out broad principles with the detailed requirements and targets for local content participation established in national regulations and/or policy guidelines.

There are advantages and disadvantages with both approaches. The first approach provides legal clarity which can be more readily enforced but there is a lack of flexibility particularly for an industry where the type of construction projects varies considerably. The second approach is more flexible but there may be challenges in ensuring the policy is implemented. The right approach is dependent on the national context and the problem that the legislation is trying to solve.

The Bill has opted for the second approach and includes the following requirements:

- All regulatory authorities, operators, contractors... to consider Nigerian content as an "important element of their overall project development and management philosophy for project execution"
- 'First consideration' to be given to Nigerian Firms in the "award of general contract and in all projects for which contract is to be awarded... in the construction industry"

The Bill also requires a firm wishing to obtain a construction contract to submit a 'Nigerian Content Plan' to the Nigerian Content Construction Industry Monitoring Board (NCCIMB). The plan has to include provisions intended to ensure that:

- First consideration is given to services provided from within Nigeria and to goods manufactured in Nigeria
- Qualified Nigerians are given first consideration for training and employment for which the plan was submitted

The plan also has to set out how the firm (or alliance partner) intends to ensure the use of locally manufactured goods where such goods meet the specification of the industry and/or give first consideration to qualified Nigerians for training and employment.

The NCCIMB is then responsible for:



- monitoring and coordinating the Nigerian content performance of all operators and
- providing guidelines, definitions and measurement of Nigerian content and Nigerian content indicator to be utilised throughout the industry

The rest of section 2 will deal specifically with the requirements that have been included in or omitted from the Bill and the potential implications. It will also propose some alternatives.

### **2.1 Lack of clarity:**

The requirements in each of the above clauses are vague and difficult to measure. As will be explained below, clear guidelines comprehensively prescribing the conditions or elements of 'consideration' that must be met are required to ensure that 'first consideration' can be 'evidenced' and that all firms are judged fairly on the same criteria. Without comprehensive guidelines or policy stipulating the requirements for integrating Nigerian content as an 'important element of ... project development' or clear criteria for 'first consideration' entities can sidestep the provisions in this Bill by adopting superficial or token actions in their local content strategy.

"First Consideration" is a crucial term that should be explicitly laid out but does not appear in the Bill's Schedule of Definitions. It is not clear what is required of the 'regulatory authorities, operators, contractors, subcontractors, alliance partners and other entities involved in .. the Nigerian construction industry', apart from a vague duty to 'consider' Nigerian content, Nigerian firms, Nigerian goods and services etc. It is not clear what suffices as 'consideration' either as an 'important element of project development' or for the award of general contracts. It is also unclear how 'consideration' will be measured or what action is required to demonstrate that an entity has adequately 'considered' Nigerian content or Nigerian firms. Furthermore, clause 11 of the Bill leaves the interpretation and application of 'first consideration' to the discretion of the entity submitting the Nigerian Content Plan. If left undefined, this could serve as a ready-made loophole for entities eager to avoid local content requirements. This is because they could justify a contract award to a non-Nigerian firm on the basis that they 'considered' a Nigerian firm but ultimately chose not to make an award. Therefore, it is necessary to clearly set out in this Bill precisely what constitutes 'first consideration' and whether there exists a duty to award or merely a duty to 'consider'. Additionally, clear guidelines are needed to stipulate the conditions or elements of 'award' or 'consideration' that must be met. This means that evidence is required to prove that 'first consideration' was in fact given and which can help minimise opportunities for circumventing Nigerian Content requirements.

### **2.2 Scope of application**

The current Bill specifies that all entities, all contracts and all projects are bound by local content requirements. However, there are a vast number of projects and contracts of varying sizes and values involved in the construction industry. Imposing a blanket local content requirement on all entities, contracts or projects may be impractical for two reasons. The first is because the Board would not have the capacity (the process requirements for every firm to submit a Nigerian Content Plan to the Nigerian Content Construction Industry Monitoring Board will be discussed in section 3). The second reason is that the government has little control over contracts, especially small contracts, in the private sector. It may also be inequitable for example, in relation to small firms, projects or contracts where increased costs could price them out of the market.

It is suggested instead, that local content requirements should only be imposed on contracts and projects when certain conditions are met, for example on contracts or projects in the public sector and/or those that exceed a stipulated value. This approach has been adopted in Queensland and South Africa:

1. Queensland Local Industry Policy only applies to government funded infrastructure projects exceeding \$5m in value or in the case of projects in regional or rural Queensland, projects exceeding \$2.5million in value. Additionally, any project exceeding these values must include local content as one of the general tender evaluation criteria.
2. South Africa's Preferential Procurement Regulations 2011, also adopts a similar system; the 80/20 preferential points system is only applicable to public sector projects and to bids equal to or above R30,000 and up to a value of R1 million. The 90/10 preference point system is applicable to bids with a Rand value above R1 million.

Exemptions should also be considered. For example, where costs would be unreasonable, or where the materials or expertise do not exist within the local industries.

### **2.3 Phasing of development of local content plans**

Additionally, the Bill or Guidelines should stipulate at which point in the project cycle local content requirements must be addressed. Currently local content plans are only required of firms bidding for contracts. Although not specifically stated in the Bill, this should include contracts for planning and design of projects as well as contracts for construction. However, it is generally recommended that specific objectives such as the promotion of Local Content should be considered at the earliest possible stage of the project cycle, ideally at project identification and initial planning when alternative ways of meeting the objectives of the project that optimise the use of local labour and materials should be considered (Wells and Hawkins 2008). The objectives should then be carried through to the detailed design, procurement planning, tender evaluation, contract award and implementation.

A good example can be found in the Policy guidelines for Queensland Local Industry Policy which stipulates that the potential for local content should be considered when:

- Undertaking procurement planning (both strategic procurement planning and planning for significant purchases)
- Preparing project designs and specifications
- Developing non-price tender evaluation criteria
- Compiling select tender lists for building contractors and consultants
- Advertising opportunities for building contractors and consultants
- Selecting and engaging building contractors and consultants

This means that the owners and proposers of construction projects must assume major responsibility for addressing local content. Objectives for local content and how they are to be achieved should be included in the social aspects of 'environmental and social action plans' which all proposers of major projects should be required to produce. It would be logical for project owners, who become the clients of the construction industry, to be also responsible for the vetting of local content plans submitted by firms bidding for contracts (this is discussed further in section 3.1).

### **2.4 Setting targets**

The Bill does not clearly specify the obligations (apart from 'first consideration') imposed on "all regulatory authorities, operators, contractors, subcontractors, alliance partners and other entities involved in... the Nigerian construction industry". As 2.1 indicates, it is anticipated that the NCCIMB would set targets for Nigerian content within the guidelines, definitions and measurement of Nigerian content (see clause 22(g)(i)).

This may include targets for the percentage of contracts to be awarded to Nigerian firms or the volume of workers that should be employed or trained. Entities operating within the Nigerian construction industry must be able to understand the obligations imposed on them and the measure for compliance. Without quantifiable targets for awarding contracts to Nigerian firms or for the purposes of achieving GEMS2's goals, employing Nigerian workers or using Nigerian goods, and the value added definition of Nigerian content is likely to be ineffective.

In contrast, the Oil and Gas Industry Nigerian Content Act (the Act) is much more prescriptive with detailed targets for Nigerian content. For example, it sets a minimum level of Nigerian content in a schedule for the various, tasks, services and materials within the value chain. The schedule's units of measurement include: man hours, spend, number, tonnage, volume ranging from 45% to 100%. If there is inadequate local capacity to meet any of the targets in the schedule, the Minister may authorise continued importation of items for 3 years.

The Oil and Gas Act also contains clear requirements for management quotas and labour. For example, operators may retain 5% of management positions as expatriate positions to take care of investor interests (clause 32) but should get approval of the Board before making an application for expatriate quota (clause 33). Projects and contracts with total budget exceeding \$100 million must contain a 'labour clause' mandating a minimum percentage of Nigerian labour in specific cadres as stipulated by the Board (clause 34). In addition clause 5 says that all operators and companies in the Nigerian oil and gas sector should employ only Nigerians in their junior and intermediate cadres or any other grades designated by the operator or company.

## 2.5 Monitoring and reporting

The Bill states that NCCIMB will be responsible for monitoring and enforcing the legislation. But the scope of organisations that it monitors is limited to operators (clause 22(g) and the other types of organisations listed in clause 2 (all regulatory authorities, contractors, subcontractors, alliance partners and other entities) are absent. The only other reference to monitoring is in clause 18 which states that 'It shall be the responsibility of the firm to effectively communicate its Nigerian content policies and procedures to its contractors and subcontractors and monitor and enforce their compliance'.

The Board also is responsible for capacity building, providing guides, monitoring, coordinating and measuring Nigerian Content performance and undertaking research. Clause 19 refers to the Board conducting seminars etc. to enhance the implementation of the Act.

The Oil and Gas Local Content Act provides much more detail on the reporting requirements for local content. This includes Operators providing the Monitoring Board with advertisements, pre-qualification criteria, technical bid documents, technical evaluation criteria and the proposed bidders list for all future contract awards **above \$1,000,000**. Then on a quarterly basis the operator will be provide to the Board:

- A list of all contracts, subcontracts and purchase orders exceeding \$1,000,000 which will be executed in the coming quarter, together with details, estimated value and dates of tender
- Prior to issue of adverts a description, copy of prequalification notification, list of companies and dates
- Prior to issue of ITT list of bidders, company ownership, location and date of tender



- Prior to award of contract, name of company, list of subcontractors/suppliers, estimated Nigerian content (person-hours) etc. etc.
- At the end of each quarter, all the information above for contracts awarded in previous quarter

The Board will decide which contracts to review and notify operator accordingly (clauses 17-24)

NCCIMB will be overseen by a Council chaired by the Minister of Works and Housing. Firstly we understand that the Ministry has been split into two: The Ministry of Works and the Ministry of Housing. Secondly, this appointment could lead to a conflict of interest as the Ministry will be one of the major organisations implementing local content plans.

## **2.6 Penalties and Incentives**

Clause 20 provides penalties for non-compliance, specifically that any firm, contractor or sub-contractor who fails to comply with the provisions of this Bill will be liable to a fine of 5% of the project value. But it is not clear whether this means failure to submit a local content plan or failure to implement it. Where applicable the project may even be cancelled. It is important to include penalties for bad behaviour, but, as detailed above, any penalties or enforcement will be redundant if there lacks adequate monitoring and reporting mechanisms.

Additionally, options for incentivising compliance should also be considered. Currently the Bill is silent on incentives for optimising local content. As an example, the Malaysian Labour Utilisation Relief Incentive, introduced in 1972 to promote labour intensive industries, provided increasingly generous tax exemptions for pioneer status industries the greater the number of full-time employees (UNCTAD 2003).

## **2.7 Training and Capacity Building**

Steps must also be taken to ensure sufficient capacity is available within local industries. Clause 16 provides that where 'Nigerians are not employed because of their lack of training, the contractor shall ensure .. that every reasonable effort is made ... within a reasonable time ... to supply such training'. This clause is weak: the onus is on the contractor to take reasonable effort within a reasonable time to provide training. Without strong guidelines prescribing the precise effort and timescales for the contractor to act, it is unlikely that any real capacity building activity will occur.

In South Africa, the Skills Development element is expressly included in the B-BBEE Generic Scorecard. The scorecard includes specific measurement principles for assessing skills development activity, for example, expenditure on learning programmes for black employees and the number of employees participating in Learnerships or other learning in the workplace. Skills Development should be adopted as one of the elements constituting Local content and included as a necessary criterion for Local Content Plans to ensure that local capacity develops sufficiently to fully meet the needs of the Nigerian construction industry.

Lessons can also be learnt from the Queensland Local Industry Policy which applies various Structured Training and Employment Policies to government building and construction contracts. This includes the '10% Training Policy' requiring a minimum 10% of the total labour hours on any Queensland Government building or civil construction project (valued over \$250,000 for building or \$500,000 for civil construction) to be undertaken by indigenous workers, apprentices, trainees or cadets or used for the upskilling of existing employees (to a maximum of 25% of the deemed hours). This '10% Training Policy' plays a key role in ensuring the building and construction industry continues to employ apprentices and trainees

and upskill its existing workforce. Contractors are required to provide evidence of compliance with the policy, and this information will ultimately be considered in any review of their eligibility to tender for future government work (Queensland Government, 2011).

Finally, despite the obvious utility of the provision of skills training by firms and contractors, the responsibility for developing and upskilling the local workforce cannot be left wholly to private sector. The Nigerian government should also develop a framework for skills policy that ensures the vocational and educational training sector is responsive to the changing needs of the Nigerian labour market and that meets the skills challenges in the construction industry. The government must work with industry, employers and unions to ensure that adequate training is provided to build the capacity of the Nigerian workforce.

### **3. Operational and administrative effectiveness**

The operational and legal effectiveness of the Bill will be determined by whether the requirements recognise the characteristics and particular problems within the Nigerian construction industry, they are drafted clearly and do not conflict with other legislation. As we have seen in the previous section, the requirements that have been included in the Bill are very short and there are numerous gaps that could result in ineffective application.

#### **3.1 Nigerian Content Plans**

It is quite clear that the Bill has been based on the Oil and Gas Industry Content Act. Whilst the purposes of the Bill are similar, the industries are structured very differently and require different approaches to developing local content. As a consequence, the authors have doubts on how the requirements of the Bill will operate in practice and its purpose realised.

According to the Oil and Gas Industry Content Act, operators are responsible for the preparation of Nigerian content plans to be submitted to an independent Monitoring Board. The plan should set out how the private sector operator intends to give first consideration to Nigerian goods and services, first consideration to Nigerians for training and employment and ensure the use of locally manufactured goods. It should also include an Employment and Training plan containing a time frame for employment opportunities and to report each year on new employees. In addition they have to submit a research and development plan as well as plans for insurance, legal services, financial services.

Clause 7 of the Bill is based on these provisions in the Oil and Gas Industry Content Act. Clause 7 requires firms bidding for contracts to consider and submit a Nigerian Content Plan to the Nigerian Content Construction Industry Monitoring Board as part of their tender proposal. The Board which is established to monitor, coordinate and implement the provisions of the Bill, then has to issue a Certificate of Authorization to the firm indicating it is satisfied with the Plan for the project.

The oil and gas sector is characterised by a one or two government ministries or agencies licensing a limited number of private operators to develop oil and gas installations in a country. In Nigeria there are 8 Joint ventures, 9 production sharing contracts, 23 sole risk/marginal field operators and 1 service contractor operating in the sector (EITI 2012). The Act applies to this limited number of operators and their supply chain. In contrast the Bill for the Development of Local Content in the Nigerian Construction Industry will apply to hundreds of public sector entities at both federal and state government as well as potentially thousands of private sector entities bidding for 'any contract, permit or interest ... in the Nigerian construction industry'.

In the oil and gas sector, the Monitoring Board may have the capacity to review the Local Content plan from the 41 organisations listed in the above paragraph. In the construction sector however, the resource requirements for undertaking a similar process with thousands of procuring entities involved in the construction industry are enormous. Potentially reviewing every local content plan as part of a tender process will become an administrative bottleneck to commissioning construction projects. This will then have a negative impact on economic growth and development.

One alternative could be drawn from the Queensland Local Industry Policy. Based on the Queensland model, the Local Content Plan should be considered and developed by the project proponents instead of the entities bidding for contracts. Project proponents of any publicly funded infrastructure project (exceeding \$5million) are required to develop Local Industry Participation Plans. The project proponents should identify the availability (or otherwise) of a competitive market within close geographic proximity to the project site (or the state or country where immediate local capacity is unavailable) and ways for their project to maximise local industry participation. This places an obligation on project proponents and developers to provide local industry with tendering and employment opportunities, is more efficient and likely to be more effective as local content requirements can expressly be included in the tender process.

According to the Queensland model, project proponents consult with the Industry Capability Network (ICN) [in the case of Nigeria this is likely to be the Nigerian Content Construction Industry Monitoring Board (NCCIMB)] at the pre-tender stage prior to the preparation of the Local Content Plan. The Local Content Plan is submitted to the ICN at least 30 days prior to going to tender for project construction or acquisition of capital assets. The ICN assesses and responds with advice or amendments within 14 days of receiving the draft Local Content Plan. This alternative model places an obligation on project proponents to ensure local industries are given fair and reasonable opportunities to be included in major works. This approach also enables Local Content requirements to be considered at the earliest possible stages (initiation, development, design and implementation).

**Box 1: Queensland Ayr Hospital Redevelopment (Queensland Govt, 2008)**

The Ayr Hospital Redevelopment Project in 2005 shows that Queensland's Local Industry Policy mechanisms can be highly effective. The contractor, Abigroup Constructions made a significant effort to support the principles of the Policy and worked with the Industry Capability Network (ICN) to actively identify local capabilities. A Local Industry Participation Plan detailing how the project would meet local industry policy requirements was developed. The main tender document included a list of local interested businesses allowing contractors to contact local suppliers who had registered their interest in the project. Initially 27 local sub-contractors were awarded work on the project (Queensland Government, 2008).

Note that this approach in Queensland applies only to public sector contracts and projects exceeding a certain value, meaning that only a limited number of contracts have to be considered by the Monitoring Board. This model does have the potential to drive increased consideration for local content, enabling local content to be considered at the earliest possible stage and enabling inclusion at the tender stage. However, it does not wholly overcome the administrative bottlenecks anticipated by the existing mechanism proposed in the Bill.

Another alternative to be considered is retrospective reviews of project performance which could be more cost effective, and additionally, overcomes the potential delays that may occur as a result of having to submit Nigerian Content Plans to the Monitoring Board. However, this process of review and monitoring only takes place after projects have been

completed and it does not provide redress for past projects or guarantee the inclusion of local content from the outset. It can only drive improved performance for the future and only if the right targets are set, and incentives and penalties are applied.

### 3.2 Balancing competing objectives

Local content objectives are invariably set at a macro level and then implemented at a micro-level with planners tasked with balancing the primary project objectives and the local content requirements in the Bill. This can lead to concerns over the potential to compromise the ultimate purpose of delivering a built asset, particularly the loss of economy and inefficiency in procurement and the reduction in competition. The World Trade Organisation and the World Bank believe that the inclusion of business opportunities for local firms can distort the market, and are at odds with fundamental elements of global public procurement rules (Hawkins, 2012).

This concern will be an issue when public procurement officials have to consider both the Public Procurement Act 2007 and the Bill. Section 32(2) of the Public Procurement Act states 'The objective of bid evaluation shall be to determine and select the lowest *evaluated* responsive bid from bidders that have responded to the bid solicitation'. With the Bill overriding all previous legislation there is the potential for this requirement in the Public Procurement Act 2007 to be compromised, particularly where Local Content plans submitted by Nigerian firms means that their tender is more expensive than others submitted by international firms.

However Section 33(2) goes on to say that '...the selected bidder need not be the lowest cost bidder provided the procuring entity can show good grounds derived from the provision of this Act to that effect'. The key here may lie in the word '*evaluated*' as the Local Content Bill proposes that contractors bidding for contracts include a Local Content plan in their bids and that these plans are included in tender evaluation. Good practice requires that the criteria for evaluation be clearly spelled out in the invitation to tender and this may require some amendment of the Procurement Act. The best way forward would be to operate a two stage bidding process whereby bids are first evaluated on their local content plans and only those containing a minimum specified local content are then assessed on price. This is the procedure used in South Africa, as shown in Box 7.

#### Preferencing

Clause 34 of the Act provides a domestic preference to Nigerian firms under international competitive bidding. A procuring entity may grant a margin of preference in the evaluation of tenders when comparing tenders from domestic bidders with those from foreign bidders or when comparing tenders from domestic suppliers offering goods manufactured locally with those offering goods manufactured abroad. Where a procuring entity intends to allow domestic preferences, the bidding documents shall clearly indicate any preference to be granted to domestic suppliers and contractors and the information required to establish the eligibility of a bid for such preference.

The Public Procurement Bureau shall by regulation from time to time set the limits and the formulae for the computation of margins of preference and determine the contents of goods manufactured locally.

Clearly the allowance of a margin of preference and the role of the Public Procurement Bureau in monitoring its application has a potential conflict with the role of the Local Content Monitoring Bureau. This potential challenge may be exacerbated by PPB's objectives of:

- ensuring the application of fair, competitive, transparent. value-for money standards and practices for the procurement and disposal of public assets and services ; and

- the attainment of transparency, competitiveness, cost effectiveness and professionalism in the public sector procurement system (Nigeria National Assembly, 2007)

However preferencing is not the only- or the most effective – way of increasing the participation of local contractors. Alternatives that would evade potential conflicts with procurement rules are splitting contracts into smaller parcels that local firms can handle and developing designs and specification that are within the capacity of local contractors.

Preferencing in construction tender award is also not an effective way of promoting locally manufactured goods as construction materials are usually purchased by the contractor and not directly by a government client. Requiring contractors to submit local content plans as part of the tender process (to meet the specifications of the client) is one of the best way of promoting their use.

### **Box 2: South Africa Procurement System**

South Africa has developed a procurement system that attempts to balance its macro-policy objectives, with a fair, equitable, transparency, competitive and cost-effective procurement system. The construction industry in South Africa is being used to develop black-owned small and medium sized enterprises and to generate employment under Black Economic Empowerment Laws. The legal system does not set minimum thresholds. Instead a 'Targeted Procurement' system provides for two methods for achieving local content objectives.

- A preference is provided to the targeted group of black-owned businesses in the tender evaluation criteria;
- The local content objectives are defined as contract participation goals, and firms compete on how they would achieve the goals. Points are allocated within the tender evaluation criteria for the methodology to achieve the goals (Hawkins, 2012).

The South African National Standards Bureau has published an 8 part standard for Construction Procurement. Parts 5 to 8 establish key performance indicators (KPIs) to measure the outcomes of a contract in relation to the engagement of targeted enterprises, joint venture partners, local resources and local labour and to establish a target level or minimum performance criteria for a contractor to achieve or exceed in the performance of a contract. These standards enable a procurement system to respond to aspects of sustainable development in a meaningful and measureable way (ISO, 2011). This series was used as a basis for ISO-10845: Construction Procurement (2011) and is underpinned by the South Africa Preferential Procurement Policy Framework Act 2011. Here, bids invited on the basis of local production and content are evaluated by following a two-stage bidding process. In the first stage, evaluation is made in terms of the minimum threshold for local production and content as stipulated in the bid documents. A bid is disqualified if the bidder fails to meet the stipulated minimum threshold for local production and content. Only bids that achieve the minimum stipulated threshold for local production and content can be evaluated in the second stage, where it will be assessed according to the preference points system.

These methods meet the requirements of the South African governments' macro-policy objectives and the requirements of the WTO and World Bank for a procurement system based on competition (Hawkins, 2012).



### **Box 3: Buy America Act: Minimum Threshold for Local Content**

An alternative approach is to set a minimum legal threshold for local content. For example, The 'Buy America Act' requires only domestic construction material to be used in public construction. It defines domestic construction material as (a) an unmanufactured construction material mined or produced in the US, or (b) a construction material manufactured in the US if the cost of its US components exceeds 50% of the cost of all components (cost of components to include transport costs). The Act requires that only domestic construction material be used with the following exceptions:

- the cost would be unreasonable (exceeding alternative by >6%)
- the material is not available in sufficient quantity/quality
- application of the principle would be impractical or inconsistent with public interest (e.g. trade agreements)
- for construction contracts > \$6.5 but <\$7.3 million

(Part 25 – Foreign Acquisition, Buy America Act, 1954)

## **4. Anticipated impacts**

The anticipated impacts of the local content Bill include generation of industry opportunities and income improvement for Nigerians. Quantifying these impacts however is extremely difficult as to do so accurately would require comprehensive data sets on a range of variables including labour productivity, existing industrial capacity and infrastructure investment pipelines.

In the absence of the data needed to realistically quantify impacts, an alternative approach is to identify factors that are likely to enhance the achievement of employment and income improvement impacts. Key factors to keep in mind are:

### **Optimising rather than maximising local content**

Is it possible to have too much of a good thing? The experience of promoting local content in the oil and gas sector suggests that it is (Heum, P. *et al*, 2003). Unrealistic local content targets can lead to increased costs, a reduction in government revenues, scheduling risks and act as a disincentive to inward investment. This is usually because they have been set beyond the capacity and capabilities of local industry. Optimal local content targets take local industrial capacity into account. They are accompanied by a range of measures aimed at supporting industrial development and increase over time as industrial capacity is built.

### **Working towards international competitiveness**

Local content provisions provide protection for Nigerian firms to develop their capabilities without having to face the full rigours of the market. This is necessary as Nigerian firms are not able to compete in parts of the construction sector at present, but protection should be seen as a means by which Nigerian firms can become more skilled and competitive over time and eventually achieve international competitiveness. If local content provisions were introduced and they did not enable Nigerian firms to achieve international competitiveness this would constitute a 'double market failure' as they would have had the unintended effect of entrenching production inefficiencies and establishing an uncompetitive domestic industry (Warner, M. 2011).

### **Understanding the commercial and public policy impacts**

The introduction of local content regulations is likely to have unintended negative consequences. This could include for example a reduction in tax revenues, increases in

capital expenditure and delays in the delivery of built assets. These are trade-offs that might be necessary to obtain the positive impacts associated with optimising local content. The challenge for regulators is to understand what those impacts might be and on whose strategic interests they might impact. UK based consultancy Local Content Solutions have developed a tool to achieve this in the oil and gas sector (Warner, M., 2010). The Economic Impact Optimisation (EIO) model quantifies the impacts of different Local Content Scenarios and with minor modifications could be applied to the construction industry.

### **Promoting employment intensive construction methods**

Employment intensive construction methods use materials and technologies that rely more on labour and less on machinery in attempt to generate additional employment and direct a greater proportion of expenditure towards wages. This can be particularly beneficial where unemployment and underemployment are a problem and where poor people are marginalised in relation to economic activity. Research undertaken by Engineers Against Poverty (EAP, undated) shows that in addition to these positive socio-economic impacts, employment intensive construction can also deliver cost savings over conventional methods in the construction of rural roads.

## Recommendations

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This review has outlined a number of different examples that could be used to improve the Bill based on examples of legislation principally from South Africa and Queensland, Australia. These are summarised below as recommendations for discussion with GEMS2 and the Nigeria Engineering Leadership Forum.

1. Amend the Bill to include clear objectives that support the value-added definition of Nigerian Content including enterprises, workers, and material suppliers.
2. Improve the Bill's definitions to:
  - Reflect the various categories of business, levels of ownership and employment, to safeguard against perverse outcomes.
  - A more practical definition and measure of 'Nigerian content' to improve likely application.
3. Apply the provisions of the Bill only to public sector contracts above a set threshold
4. NCCIMB should establish Nigerian Content targets for labour and material suppliers as well as enterprises through detailed policy guidelines as the Bill currently anticipates. Alternatively, these targets could be included in the legislation if this is more likely to lead to better compliance.
5. Insert clearer obligations and conditions for training and skills development to ensure the capacity of the Nigerian workforce is fully developed. Ownership of this responsibility needs to be established and effective strategies put in place to grow capacity and monitor compliance.
6. Establish a clear incentive, penalties and monitoring framework within the Bill.
7. Require that NCCIMB
  - Review the local content plans of procuring entities (rather than firms) and /or
  - Undertake retrospective reviews of local content performance.
8. The NCCIMB Council Chair should be an independent person who does not have a potential conflict of interest.

It is important to point out that legislation on its own will not deliver improved local content in the construction industry. Strong policy and adequate enforcement are required to ensure effective implementation of local content requirements. In developing these instruments, the multiple options and pathways for local content require careful consideration and must be adapted to suit the unique characteristics of construction industry and to fit into the Nigerian context.



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