The art of the rare earth deal: Is the devil in the details?

Mineral rights deals may seem like a big win, but they are not without risk.

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Considering the wider implications of mineral rights deals

The recently mooted U.S./Ukraine critical minerals agreement has reignited interest in such transactions. Mineral rights deals have the potential to have significant implications for global trade, European strategic planning and resource sovereignty. Investors and policymakers must consider the long-term risks and legal ramifications of such agreements, including the potential for nationalisation, as seen most recently in Bolivia's lithium industry.

Resource sovereignty and the risks of nationalisation

While both Washington and Kyiv continue to ponder the implications of securing/granting preferential access to Ukraine's rare earth elements ("**REEs**") and other critical resources, policymakers will continue to evaluate the long-term risks and legal implications of such a deal. One crucial concern that needs to be considered in any strategic resource agreement and should not be overlooked by U.S. policymakers, is the ever-present spectre of nationalisation. Should an agreement be reached and signed, Ukraine could move to reclaim control over its mineral resources as a result of economic or political pressure, much like Bolivia did with its lithium reserves in the previous decade.

1 Resource sovereignty and the risks of nationalisation

Historically, states have exerted control over strategic resources to protect national interests. Nationalisation of mineral resources typically occurs when governments seek to reclaim foreign-controlled assets due to shifts in political priorities, economic crises or popular opposition to foreign ownership.

A potential U.S. deal with Ukraine raises legal questions under bilateral investment treaties ("**BITs**") and the Energy Charter Treaty (to which the U.S. is notably not a party), both of which provide mechanisms for investor protection against expropriation. If Ukraine were to reclaim mining and processing facilities granted to U.S. firms and others under the umbrella of a U.S./Ukraine deal, investors could seek to initiate international arbitration proceedings,

arguing unlawful expropriation. However, as history shows, international legal protections often provide little deterrence when political imperatives drive nationalisation efforts.

> *"...the success of the rare earth deal will depend on its legal framework, enforcement mechanisms and both sides' long-term commitment to honouring their commitments."*

2 Lessons from history

2.1 The nationalisation of the Bolivian lithium industry

Bolivia's nationalisation of its lithium industry in 2019 serves as a stark warning to both investors and politicians proclaiming to have reached "a great deal" where mineral rights are concerned. Initially, Bolivia opened its lithium reserves to foreign investment, striking agreements with German and Chinese firms. However, domestic unrest, political shifts and nationalist sentiments led to a swift reversal. Former President Evo Morales, under public pressure, cancelled foreign contracts citing the need to retain domestic control over the country's most valuable resource.

The Bolivian case underscores key legal and political risks:

- **Unilateral Contract Cancellation:** Bolivia withdrew from binding agreements without honouring contractual protections, prioritising national economic interests.
- **Investor-State Disputes:** German investors threatened arbitration under BITs, but Bolivia relied on sovereign immunity and domestic legal justifications.
- **Repercussions for future foreign investment:** The move strained Bolivia's relationships with foreign investors and partners, deterring future large-scale projects.

2.2 Three oil nationalisations – Venezuela, Argentina and Russia

In 2007, Venezuelan President Hugo Chávez nationalised the nation's oil industry. Foreign entities, such as ExxonMobile and ConocoPhillips, were forced to hand over majority stakes to a state-owned entity, Petróleos de Venezuela, S.A. The Venezuelan state was successfully sued by the foreign entities whose assets were expropriated, but the collapse of the Venezuelan economy made enforcement of the arbitral award exceptionally difficult.

The Argentinian nationalisation of Yacimientos Petrolíferos Fiscales ("YPF") in 2012 saw the government of Cristina Fernández de Kirchner expropriate a 51% stake in YPF from Repsol of Spain. Repsol sued Argentina for approximately USD 10 billion but the parties later settled at a figure closer to USD 5 billion.

The Russian government's dismantling of Yukos between 2003 and 2006, saw the largest private company in Russia fall into the hands of state-owned Rosneft. While foreign shareholders of Yukos successfully sued for compensation, the USD 50 billion arbitral award has been largely ignored by the Russian state.

The key takeaways from these three examples:

- **Economic circumstances may make enforcement difficult:** The severe downturn in the Venezuelan economy had a negative impact on enforcement.
- **Political circumstances may make enforcement difficult:** Russia has largely ignored the outcome of the Yukos arbitration, leaving shareholders out of pocket.
- **Benefits of negotiation:** Repsol was at least able to obtain some compensation by settling its dispute with Argentina.

2.3 Indonesia and Mongolia – leveraging resource sovereignty

Two mining examples provide us with a glimpse into alternative outcomes.

The Grasberg Mine is one of the world's largest gold and copper mines. It was originally developed and operated by Freeport-McMoRan, a U.S.-based mining company, under a contract with the Indonesian government that granted Freeport significant control over the site for decades. By the 2010s, Indonesian political leaders began pushing for greater national control over the country's natural resources, arguing that foreign companies were extracting wealth at the expense of the local population. A new mining law was introduced requiring foreign companies to gradually divest at least 51% ownership of major mineral projects to Indonesian entities. In 2017, Freeport-McMoRan was forced to sell a majority stake in the Grasberg Mine to an Indonesian state-owned company. Freeport and Indonesia ended up renegotiating terms that were much more favourable to Indonesia, however Freeport retained operational control.

The Oyu Tolgoi Mine, located in Mongolia's Gobi Desert, is jointly owned by Rio Tinto and the Mongolian government. In 2009, Mongolia signed a deal granting 66% ownership to Rio Tinto through its subsidiary, Turquoise Hill Resources, while the government retained a 34% stake. As Mongolia's economy became increasingly reliant on Oyu Tolgoi, public dissatisfaction grew over foreign dominance of the project. By the 2010s, Mongolian lawmakers began pushing for a renegotiation of the contract, citing concerns over revenue distribution and sovereignty. Mongolia demanded higher royalties and a bigger share of mining profits, the parties eventually settled on a deal whereby Rio Tinto agreed to write off $2.3 billion in debt owed by Mongolia and increase economic benefits for the country.

These examples highlight:

- **Resource sovereignty can be used as leverage to renegotiate terms:** In both cases, the overall goal of the governments were achieved, not through nationalisation, but by using the resources to put pressure on its commercial counterpart.
- **While not always "win-win", negotiated outcomes are better than nationalisation's "win-lose" outcome:** While both Rio Tinto in Mongolia and Freeport in Indonesia ended up in less favourable positions than they had been at the beginning, they did manage to retain control of the projects.

2.4 Asserting resource sovereignty is a high-risk approach

The 1950s provide us with two propositions of the high risks faced by states seeking to reassert control over natural resources.

The nationalisation of the Anglo-Iranian Oil Company ("AIOC") by the Iranian government in 1951 triggered a major confrontation with the UK. Iran's oil industry was controlled by AIOC, a British firm that later became BP. Iran received only a small share of the oil revenues, which fuelled nationalist resentment. In 1951, Prime Minister Mohammad Mossadegh led a movement to nationalise AIOC, arguing that Iranian resources should benefit

Iranians. The UK imposed an economic blockade, preventing Iran from selling its oil on international markets. The Iranian government's moves sparked an international legal battle - the case was taken to the International Court of Justice, which eventually ruled in Iran’s favour. Although the judicial battle was won, the U.S. and the UK orchestrated a *coup d'état* in 1953 which overthrew Mossadegh and reinstated the Shah, who reversed the nationalisation of AIOC and restored Western control over Iran's oil.

The Suez Crisis is further proof that nationalisation carries with it great risks. When President Nasser of Egypt wrested control of the Suez Canal from the Anglo-French Suez Canal Company in 1956, a major international incident was triggered. The UK, France and Israel launched a military invasion in an attempt to seize control of the canal and remove Nasser from power. The invasion faced heavy international opposition. The U.S., the Soviet Union and the United Nations pressured the invading forces to withdraw, marking a shift in global power dynamics away from traditional European colonial powers. Despite the military action, Egypt successfully nationalised the canal, expelling European influence from the region. Suez Canal revenues became a major source of income for Egypt and remain so to this day.

Both the Iranian nationalisation of AIOC and the Suez Crisis provide us with salient lessons:

- **If the resources in question have significant economic and/or strategic value, other state actors may get involved:** In both instances, the value of the resource being expropriated was such that military responses were instigated.
- **Nationalisation is not always the end of the story:** In the case of Iran, it was reversed following the coup. With Suez, although nationalisation prevailed in the end, there was a military cost.

2.5 Securing the deal is one thing, making it last is another

History has shown us time and time again that lopsided treaties (or those that are perceived to be lopsided) rarely last long. If after securing a mineral rights deal with the United States, Ukraine were to follow a path to nationalisation, legal challenges from the U.S. would most likely arise. Enforcement of arbitration awards, however, remains difficult. Countries facing national security crises or economic downturns often prioritise domestic needs over investor protections, making legal recourse an uncertain remedy.

3 Protecting European stakeholders

The EU, as Ukraine's primary economic partner, has a vested interest in ensuring stable and fair access to critical mineral resources. The EU-Ukraine Association Agreement includes commitments to fair trade practices and regulatory alignment, which could provide a basis for European legal challenges should an eventual U.S./Ukraine deal impinge on Ukraine's obligations to European investors.

Additionally, the EU’s Critical Raw Materials Act aims to secure at least 10% of its REE needs from EU sources by 2030. If a deal between Ukraine and the U.S. creates an exclusive supply chain for American industries, European goals may be compromised. This, in turn, may create tensions in any eventual EU accession talks between Ukraine and the EU.

4 Details matter

The as yet unsigned U.S./Ukraine mineral rights deal has brought the high-stakes nature of international resource agreements into the spotlight. While the potential agreement promises economic benefits and supply chain security, the legal and geopolitical risks cannot be overlooked. The threat of nationalisation, coupled with Ukraine’s economic

fragility and historical precedents like those referred to earlier, raise legitimate concerns for investors and policymakers alike.

Ultimately, the success of a rare earth deal will depend on its legal framework, enforcement mechanisms and both sides' long-term commitment to honouring their commitments. It is perhaps a transactional truism that the fine print of a deal often determines its fate. In the world of critical minerals, the devil is indeed in the details.

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