MACRO-FISCAL FRAMEWORK FOR MANAGING MINING AND PETROLEUM REVENUES IN SIERRA LEONE

Presented at the Conference on Fiscal Management of Mining and Petroleum in West Africa

Ministry of Finance and Economic Development- Sierra Leone

28TH FEBRUARY 2018
Outline

1. Selected Country Data
2. Pre- and Post Shock Macroeconomic Performance
3. Pre- and Post-Shock Domestic Revenue/Mineral Revenue Performance
4. Fiscal Regime for Mining and Petroleum
5. Legal Reforms & Institutional Framework
6. Macro-Fiscal Forecasting
7. Fiscal Management of Extractive Revenues
8. Challenges and Lessons
Selected Country Data

- **Population**: 7,092,113 (2015 Census)
- **Geograph. Area**: 71,740 Sq.km (27,699 Sq Mi)
- **GDP per Capita** (av.2012-2017)-$660
- **Major Exports**: iron ore, diamond, rutile, bauxite, Ilmenite, fisheries,
- **Main Economic Activities**: Agric., Mining, Fishery;
- **Employment**: Agric-52.9%, Serv. -31.2% Industry (incl. mining and const.) -9.6%.
- **Poverty Incidence**: -52.9% (2011 SLIHS)
Macro performance deteriorated significantly following the twin shocks (commodity price and Ebola).

<table>
<thead>
<tr>
<th></th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017 (Est)</th>
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</thead>
<tbody>
<tr>
<td><strong>REAL GDP GROWTH (%)</strong></td>
<td>15.2</td>
<td>20.7</td>
<td>4.6</td>
<td>-20.1</td>
<td>6.3</td>
<td>5.6</td>
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<tr>
<td><strong>EXCLUDING IRON ORE (%)</strong></td>
<td>5.3</td>
<td>5.6</td>
<td>0.9</td>
<td>3.2</td>
<td>4.5</td>
<td>3.5</td>
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<tr>
<td><strong>INFLATION (e.o.p) (%)</strong></td>
<td>12</td>
<td>8.5</td>
<td>9.8</td>
<td>10.1</td>
<td>17.4</td>
<td>15.3</td>
</tr>
<tr>
<td><strong>TRADE BALANCE (% OF GDP)</strong></td>
<td>-22.6</td>
<td>-0.7</td>
<td>-7.5</td>
<td>-18.0</td>
<td>-17.4</td>
<td>-16.7</td>
</tr>
<tr>
<td><strong>GROSS RESERVES ($m)</strong></td>
<td>420</td>
<td>514</td>
<td>633</td>
<td>580</td>
<td>503</td>
<td>503</td>
</tr>
<tr>
<td><strong>EXCHANGE RATE (Le/$) (av.)</strong></td>
<td>4,214</td>
<td>4,223</td>
<td>4,534</td>
<td>5,081</td>
<td>6,203</td>
<td>7,284</td>
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2. Pre- and Post-Shock Domestic Revenue/Mineral Revenue Performance

Domestic revenues declined and stagnated after the shocks. Mining revenues declined sharply.

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<tr>
<th>(Le billions)</th>
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<th>2017 (Est)</th>
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<tbody>
<tr>
<td>DOMESTIC REVENUES</td>
<td>1,874</td>
<td>2,280</td>
<td>2,226</td>
<td>2,330</td>
<td>2,889</td>
<td>3,346</td>
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<tr>
<td>MINING REVENUES</td>
<td>452</td>
<td>470</td>
<td>386</td>
<td>225</td>
<td>315</td>
<td></td>
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<tr>
<td>Licenses</td>
<td>25</td>
<td>39</td>
<td>42</td>
<td>38</td>
<td>48</td>
<td>44</td>
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<tr>
<td>Mineral Royalties</td>
<td>90</td>
<td>162</td>
<td>145</td>
<td>49</td>
<td>108</td>
<td>104</td>
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<tr>
<td>Income Taxes</td>
<td>208</td>
<td>226</td>
<td>190</td>
<td>128</td>
<td>151</td>
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<tr>
<td>Customs &amp; Excises</td>
<td>16</td>
<td>9</td>
<td>9</td>
<td>11</td>
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<tr>
<td>Mining Revenues</td>
<td>2.9</td>
<td>2.6</td>
<td>1.9</td>
<td>1.0</td>
<td>1.3</td>
<td>-</td>
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<tr>
<td>Licenses</td>
<td>0.2</td>
<td>0.2</td>
<td>0.2</td>
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<td>0.2</td>
<td>0.5</td>
<td>0.4</td>
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<tr>
<td>Income Taxes</td>
<td>1.4</td>
<td>1.2</td>
<td>0.9</td>
<td>0.6</td>
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<td>Customs &amp; Excises</td>
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<td><strong>GGDO</strong></td>
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3. Fiscal Regime for Mining and Petroleum

A. Mining (i) Royalty:
- Royalty (Artisanal Mining): 3%
- Royalty (Mining Company): (i) 6.5% - precious stones; (ii) 8% - special stones; (iii) 5% - precious metals; (iv) 3% others; or depending on the mining agreement;
- Royalty computed on the market value of minerals.

(ii) Corporate Income Tax (CIT):
- CIT – for mineral operations -30% (But tax holidays; Capital Allowances; Overpricing of Assets, Loss Carry Forward, Lack of Capacity to Audit imply low revenues from CIT)

(iii) Personal Income Tax (PIT) – Highest Marginal Rate-35% but companies (expatriates) pay - 25% initially, after 3 months, back to normal income taxes;

(iv) Mineral Resource Rent Tax: designed to secure a greater share of the return derived from EI operations;
- Withholding taxes – on management fees unless where exempted;
3. Fiscal Regime for Mining and Petroleum cont’d

- Exploration licenses;
- Impact Assessment fees;
- Monitoring fees;
- Community Development levy 0.1% of export revenues
- Custom duties: Big mining companies have waiver, small companies pay;
- GST: Import & Domestic GST Waived for mining equipment; but paid on non-mining equipment
3. Fiscal Regime for Mining and Petroleum cont’d

B. Petroleum

(i) Royalty a) 10% for Crude Oil; b) 5% for natural gas; Minister may adjust this but less than 80% of the above rate; royalty on market price;

(ii) Income Tax – 30% for petroleum operations;

(iii) Petroleum Resource Rent tax; designed to secure a greater share of the return derived from EI operations;

(iv) Petroleum: Signature bonuses; licenses.
4. Legal and Institutional Framework for Managing Extractive Revenues

Legal Framework:

- **Mines and Minerals Act (2009)** – regulates mineral sector: Investments (exploration, mines development & marketing); transparency & Accountability; employment & welfare;

- **Core Minerals Policy**: basis for sound investment; institutional capacity building; harmonized legal and regulatory practices and domesticate the Africa Mining Vision (AMV)

- **Public Financial Management Act (2016)** – Chp. 6 Management of Extractive Industries Revenues; section 78 proposes a fiscal rule;
Legal Framework cont’d

- **Public Financial Management Regulations 2017** - for implementing the PFM Act (2016)
- **Petroleum Act (2011)** – regulates upstream petroleum sector;
- **Extractive Industry Revenue Act (2017)** – Submitted to Parliament, Nov. 2017- consolidates fiscal regimes for the EI sector; and restricts negotiation of fiscal regimes;
Institutional Framework

- National Minerals Agency - Responsible for administration and Regulation for the mining sector; Implements policies;
- National Revenue Authority – Established the EIRU - carry out audit & forecasting EI Revenues.
- Mineral Revenue Task Force - Monitors, analyze and identify challenges in the EI sector;
- Sierra Leone Extractive Industry Transparency Initiative (SLEITI) - To help Sierra Leone comply with EITI guidelines; empower citizen to hold Gov’t accountable for stewardship of revenues
Institutional Framework cont’d

- Public Investment Management Unit – (MOFED)
  - to conduct feasibility studies; determine strategic priority, value for money, costing realistic and funding availability. However, no detailed studies/Investment analysis;
- Cash Management Committee – Short-term/weekly cash management;
- Mining Repository – online mining database to comply with EITI;
- Mining cadastre: Register of mineral rights, rights applications and cadastre survey map.
5. Fiscal Management of Extractive Revenues

A. Mineral Revenue Forecasting

- Economic prospects Survey including mining companies;
- Project economics including assumptions for production, exports, prices, costs, etc;
- Validation from National Minerals Agency;
- Global outlook; WEO prices not equal to company prices due to deductions;
- Macro-Fiscal Working Group: membership
- Forecasting models: FARI/SLIMM;
- Forecasts discussed and agreed with IMF.
5. Fiscal Management of Extractive Revenues cont’d

Part VI of the PFM Act (2016) establishes 3 (three) funds for the management of extractive revenues and proposed a Fiscal Rule

(i) Transformation and Development Fund (TDF) Account: All extractive industry revenues shall be deposited into this Fund, which is part of the Consolidated Revenue Fund for the purpose of funding Transformational Development Projects.

The amount transferred from the TDFA into the TDSA shall be made in accordance with the Fiscal Rule proposed in section 78 of the PFM Act.
Fiscal Management of Extractive Revenues cont’d

- **Transformational Development Stabilization Fund (TDSF):** when the amount to be deposited into TDF exceeds the amount to be withdrawn for dev projects, the difference deposited into TDSF and vice versa in order to avoid volatility in Government spending.

- **Intergenerational Savings Fund (ISF):** When the amount in the TDSF exceeds a certain amount (determined by Minister), difference transferred into the ISF.
6. Challenges & Lessons

• International price volatility - revenue volatility - expenditure volatility (pro-cyclicality);
• Managing the aftermath of declining revenues difficult;
• Difficulty verifying actual production and prices (Arms Length Price); transfer pricing
• Difficulty verifying actual costs of machinery/production impacting negatively on assessing taxable income;
• Fiscal Regimes varies from one Mining Lease Agreement to another;
• Unwillingness to provide data by Mining Companies (EIRA will address this)
6. Challenges & Lessons

- Significant initial expenditure growth- including investments on infrastructure, wages and salaries;
- Government entered into contracts in anticipation of higher revenues, which did not materialize resulting in the accumulation of Arrears to Contractors.
The End

Thank you for your Attention