



International Taxation Challenges in the Mining Sector in SSA

APRIL 14, 2019

**Taxing to Develop:
International Taxation Challenges for Africa**

5th IMF/WBG Spring Meetings Conference on Taxation

Organization of the Presentation

- Mining in Sub-Saharan Africa: translating mining into revenues
- Main Challenges and vulnerabilities
- Brief final comments and discussion

Mining in Sub-Saharan Africa: translating mining into revenues

Mining in SSA: a key resource

Importance of mining in Africa

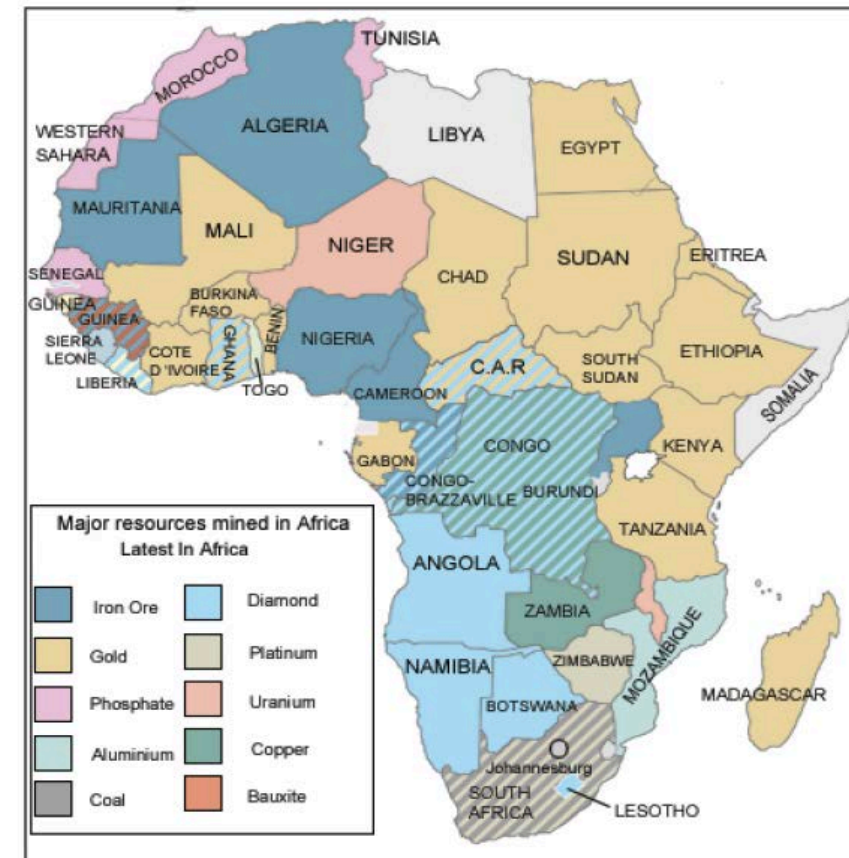
Africa represents **17 percent** of the worldwide mineral exploration investment.

30 percent of the world's mineral reserves

- 40 percent gold reserves
- 60 percent cobalt reserves
- 90 percent of precious gems

Africa Holds Vast Mineral Reserves

Mineral Resources By Country

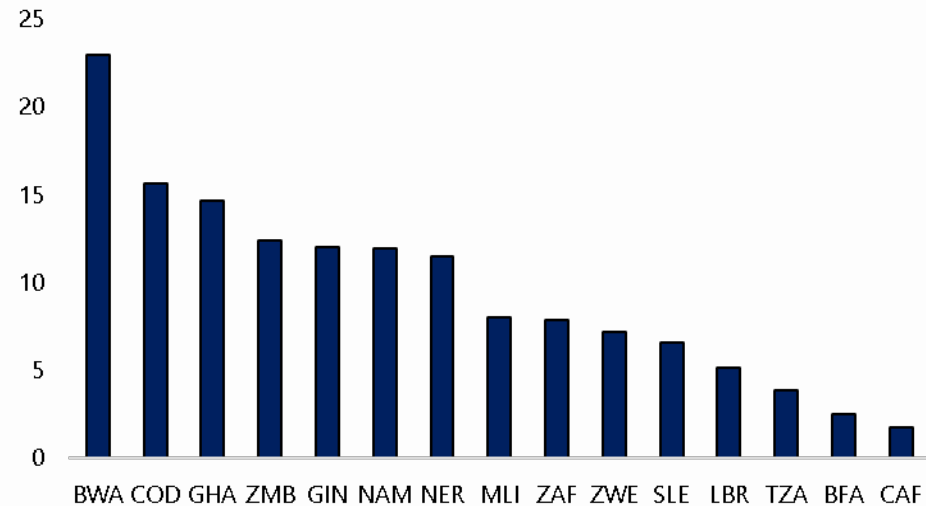


Source: Raw Material Group, US Geological Survey, BMI

Mining in Sub-Saharan Africa: a source of growth

Mining makes an important contribution to GDP...

Sub-Saharan Africa: Resource GDP, average 2000-15
(in percent of total GDP)



Sources: Country authorities and IMF Staff estimates.
Note: includes mining resource-rich countries.

... and even more to exports

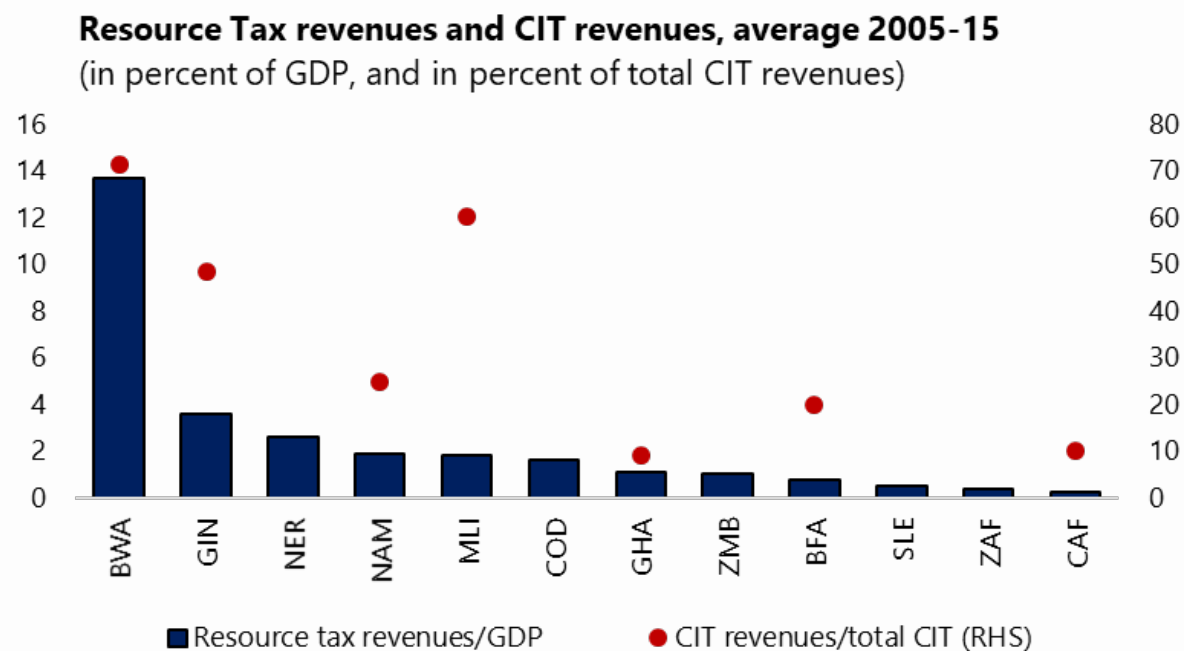
Sub-Saharan Africa: Non-renewable resource exports, average 2000-15
(in percent of total exports of goods)



Sources: Country authorities and IMF Staff estimates.
Note: includes mining resource-rich countries.

Mining in SSA: a source of tax revenues

Mining is important for tax revenues



Sources: Country authorities and IMF Staff estimates

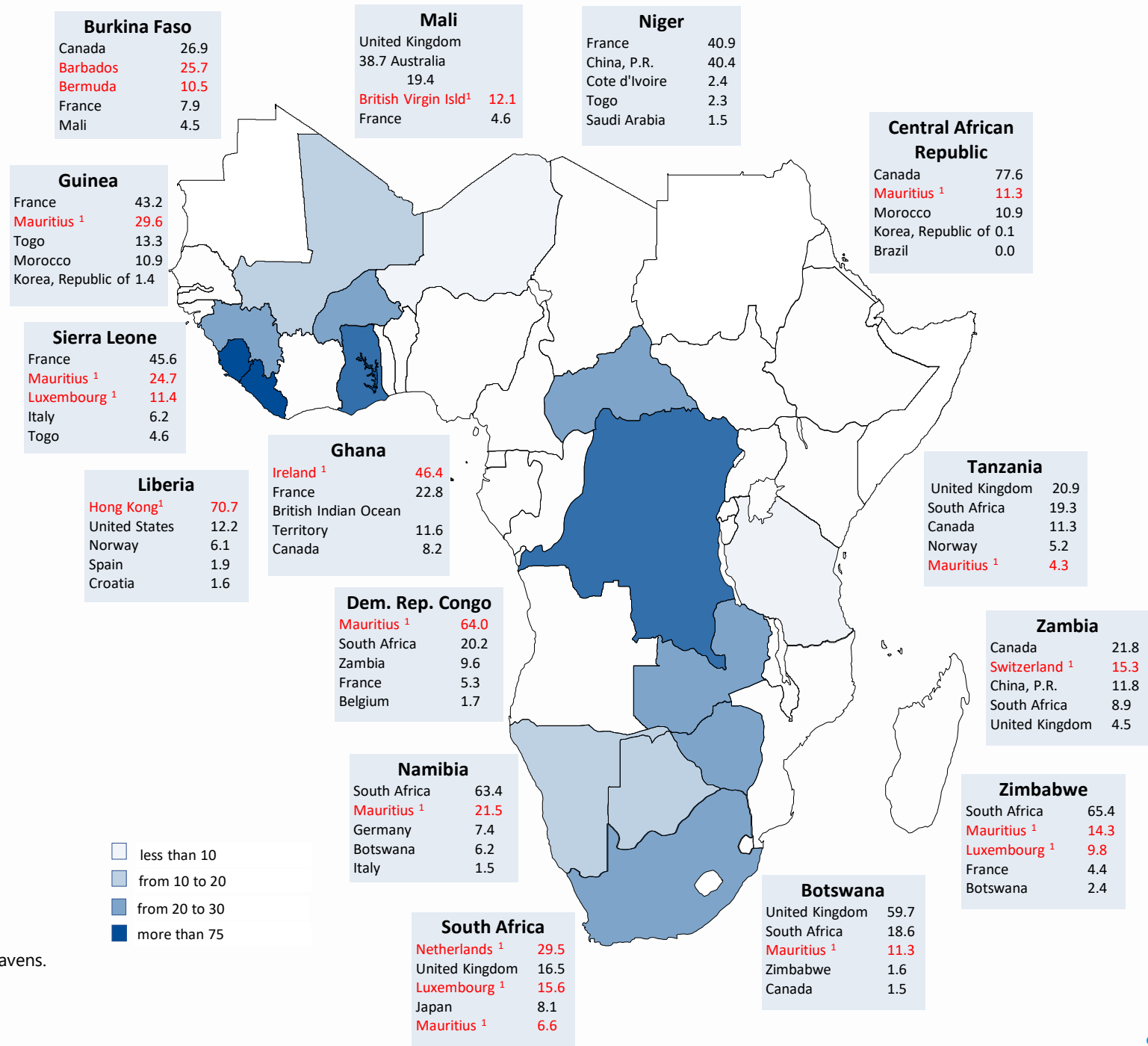
Main challenges and vulnerabilities

Challenges to tax revenue mobilization in SSA



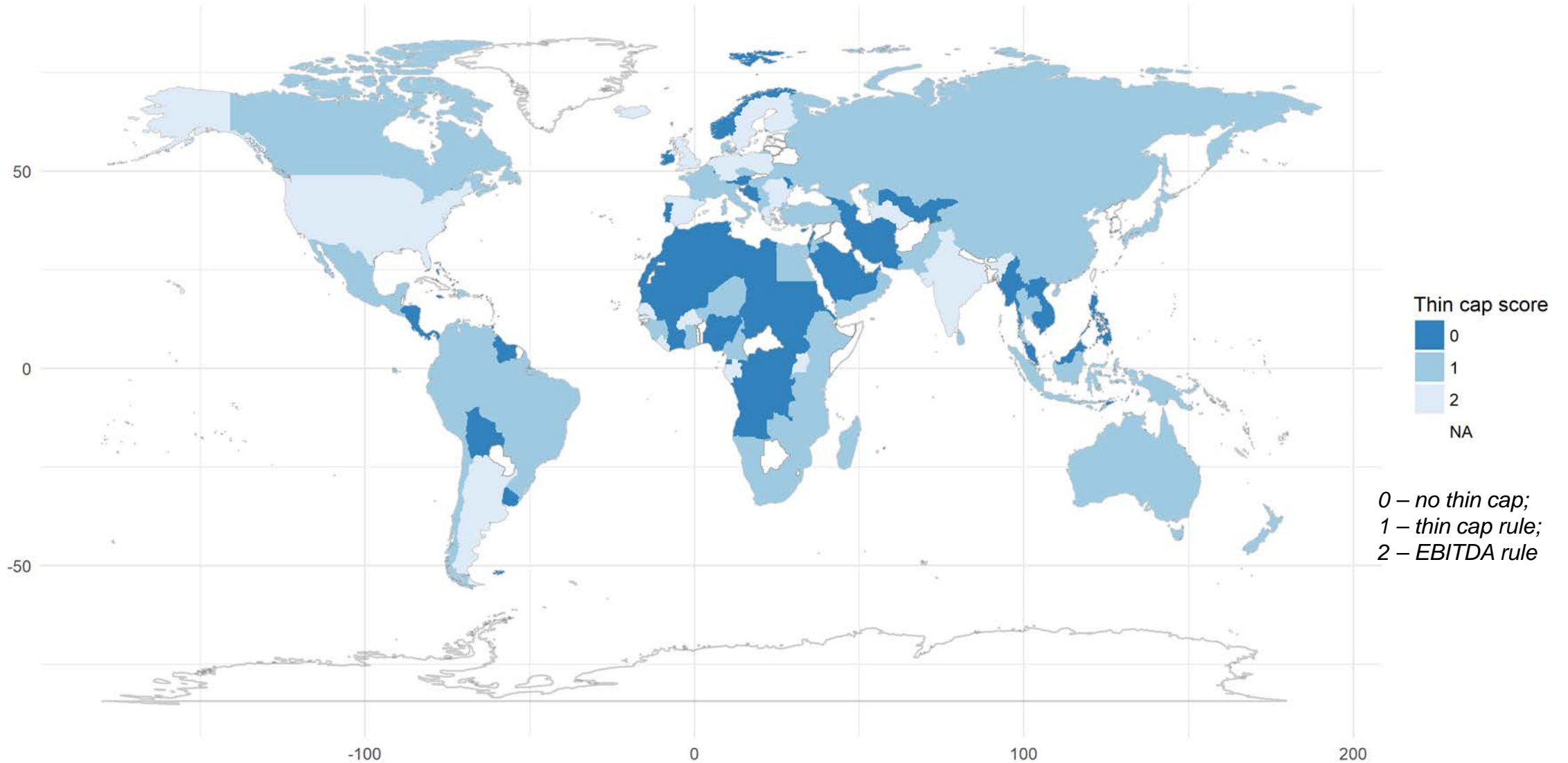
Vulnerability: FDI coming from Low-Tax Jurisdictions

Top 5 sources of FDI from Low Tax Jurisdictions, 2017 or latest available
(percent of total FDI)



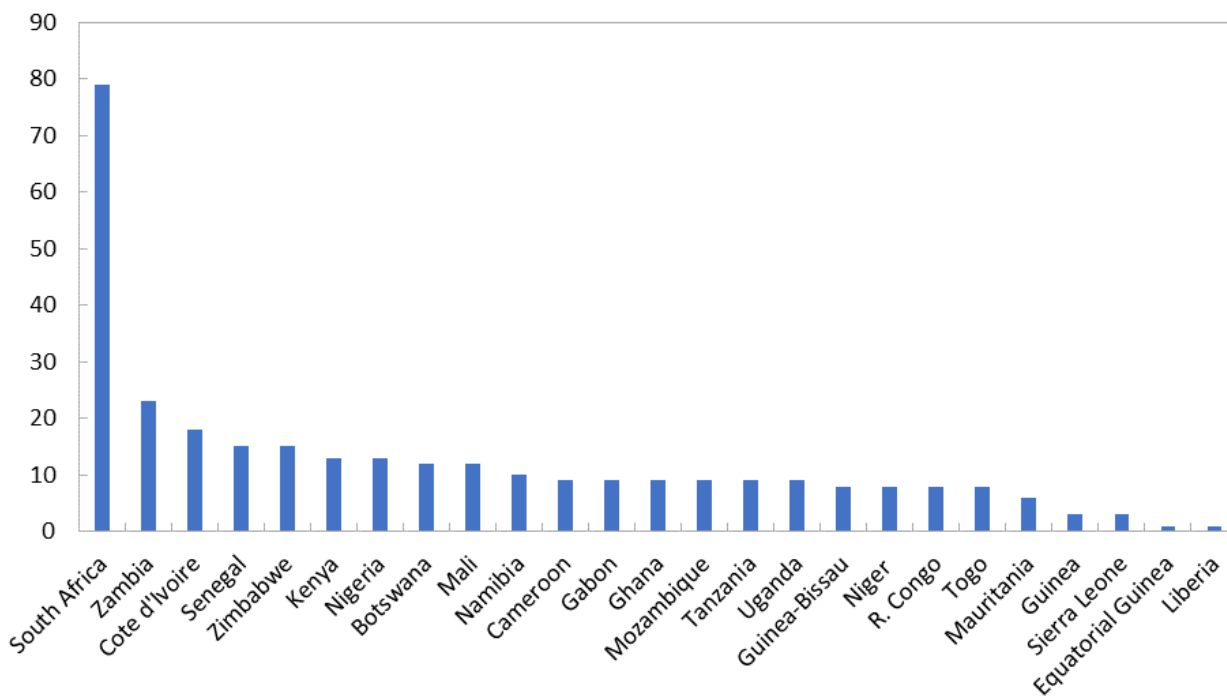
Source: OXFAM; and IMF Coordinated Direct Investment Survey.
Note: Low tax jurisdictions as defined by OXFAM, Top 15 Corporate Tax Havens.

Vulnerability: Lack of limitations on debt



Vulnerability: Reduced withholding rates

Number of Tax Treaties, 2016

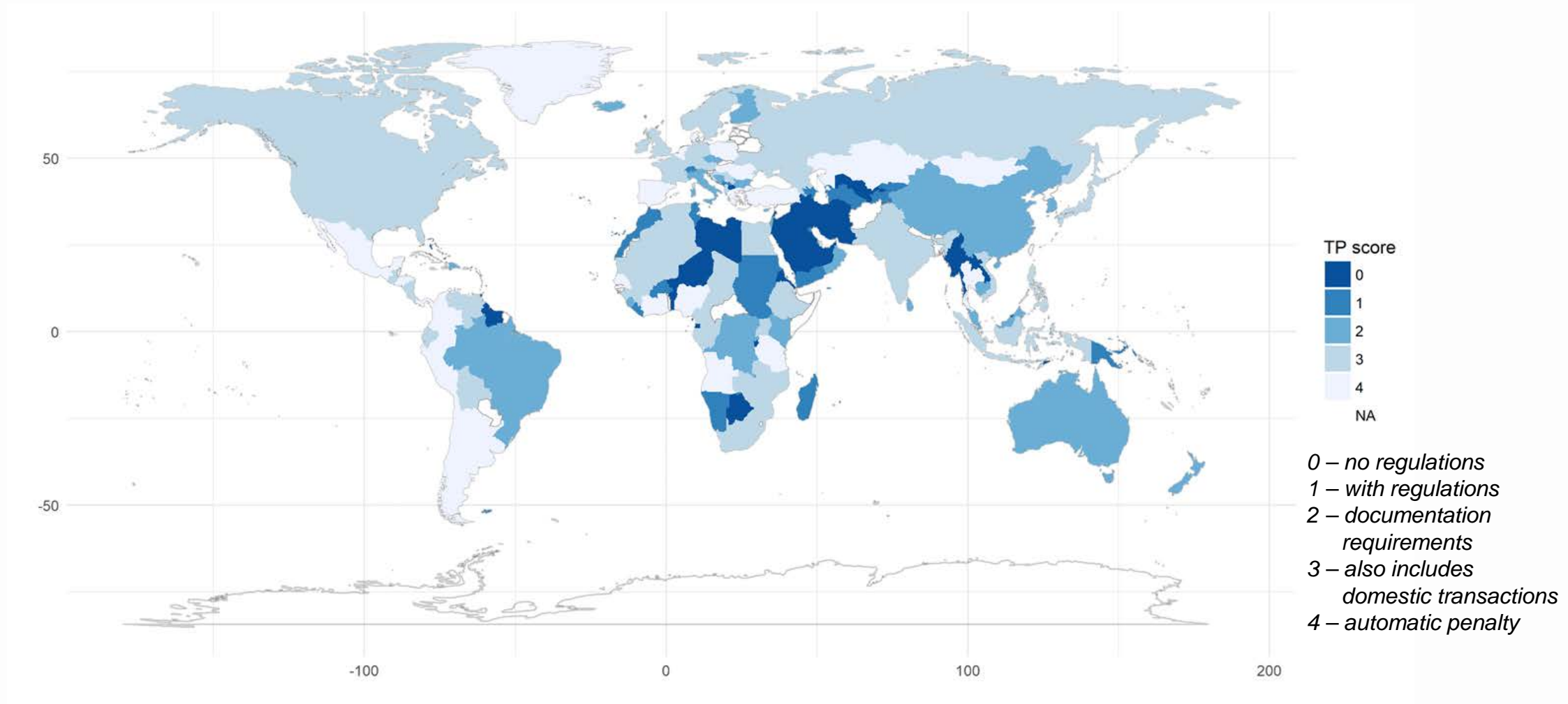


Source: IBFD

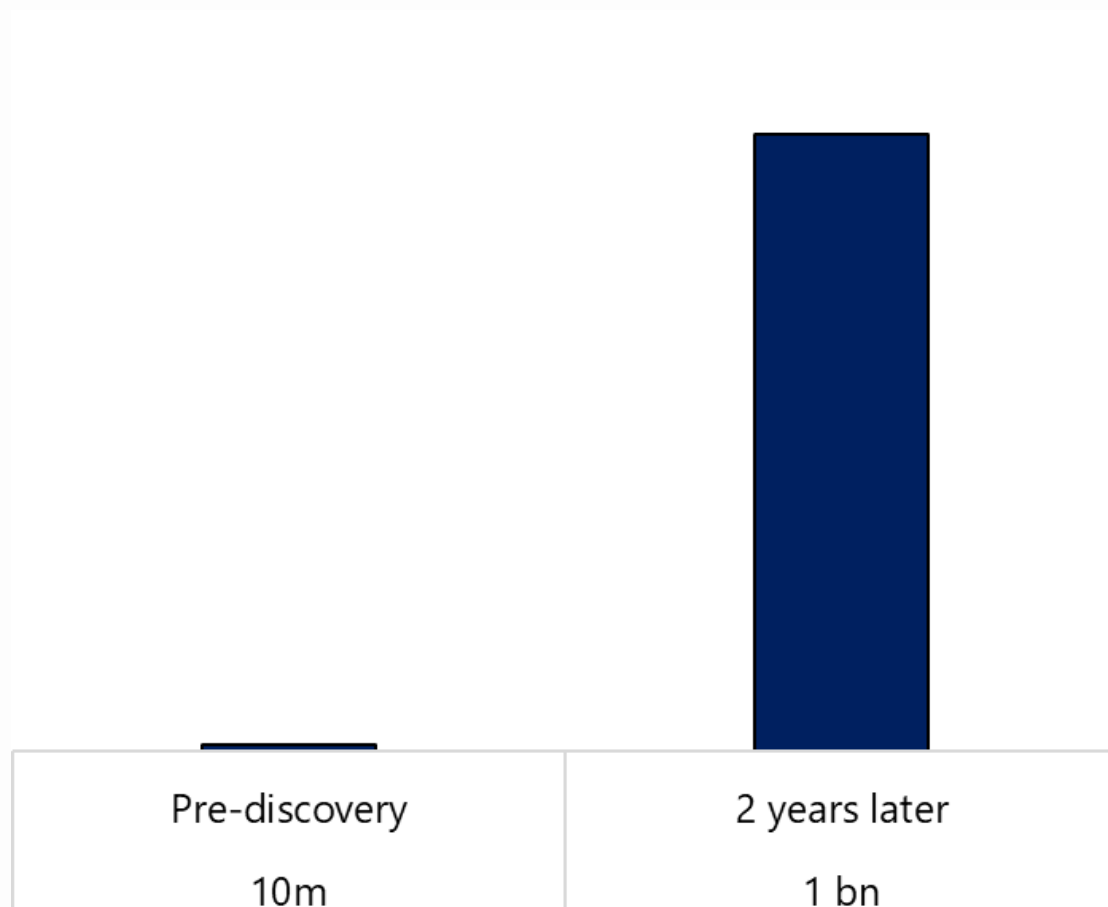
	Dividends	Interest	Royalties
	Lowest Treaty rate	Lowest Treaty rate	Lowest Treaty rate
Botswana	5	7.5	5
Cameroon	10/15	10	0
Cote d'Ivoire	10	10	5
Equatorial Guinea	n/a	n/a	n/a
Gabon	15	10	0
Ghana	10	0	8
Guinea	0	0	0
Guinea-Bissau	10	10	10
Kenya	5	10	10
Liberia	15	20	20
Mali	5	5	0
Mauritania	10	10	0
Mozambique	0	0	5
Namibia	10	10	0
Niger	10	15	0
Nigeria	7.5	7.5	7.5
R. Congo	0	0	0
Senegal	0	0	0
Sierra Leone	0	0	0
South Africa	0	0	0
Tanzania	0	0	0
Togo	10	15	0
Uganda	0	10	10
Zambia	0	5	5
Zimbabwe	7.5	5	7.5

Orange – reduced rate; red – reduced to zero

Vulnerability: Less protection against transfer pricing manipulation



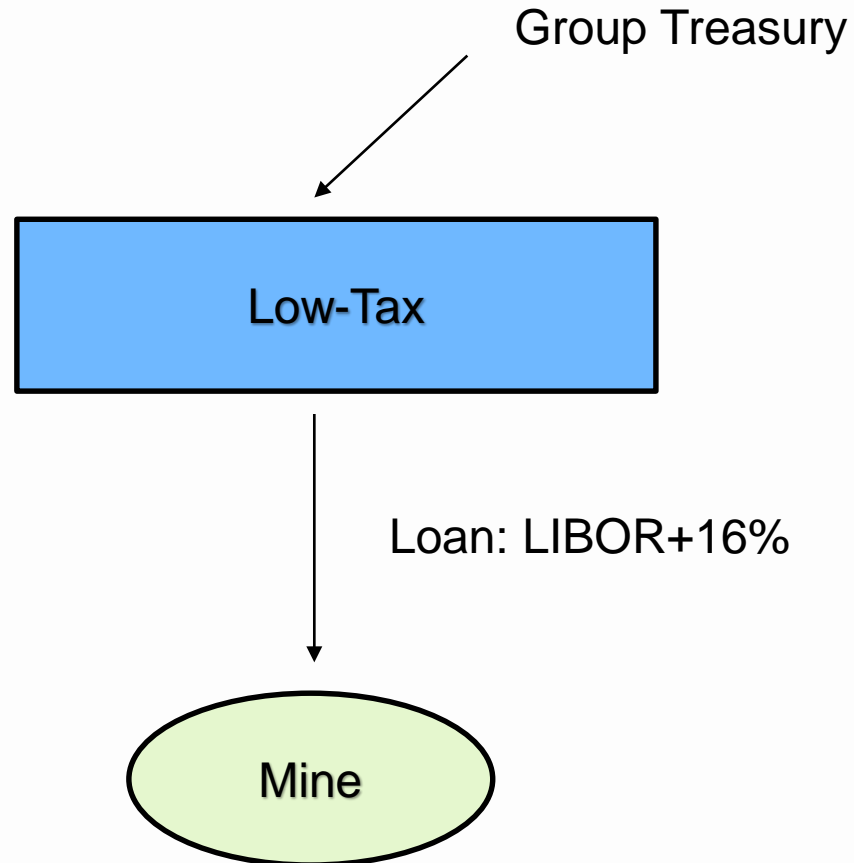
Vulnerability: Risk of offshore indirect transfers



Example: a gold/copper discovery changed market capitalization from 10 mn to 1 bn over 2-year period

Domestic Revenue Mobilization Challenge: Interest deductions

Interest Case 1



Every recent IMF TA report mentions earnings stripping via debt as a vulnerability

Both via high rates, and if that route is closed off, via high quantity

(or both)

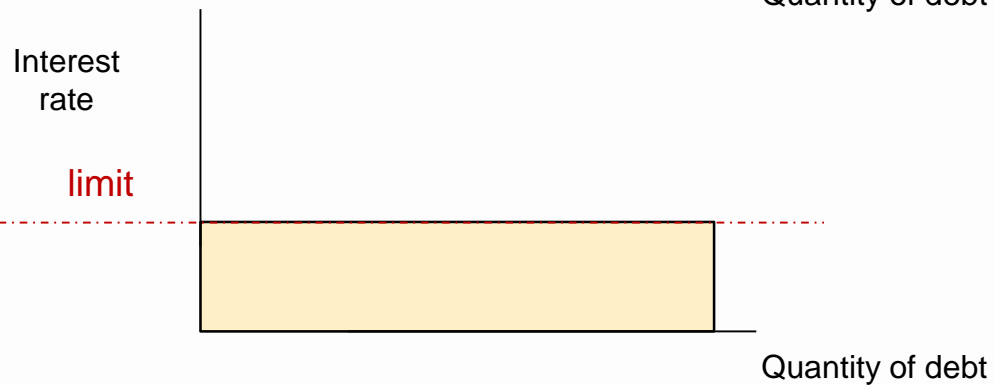
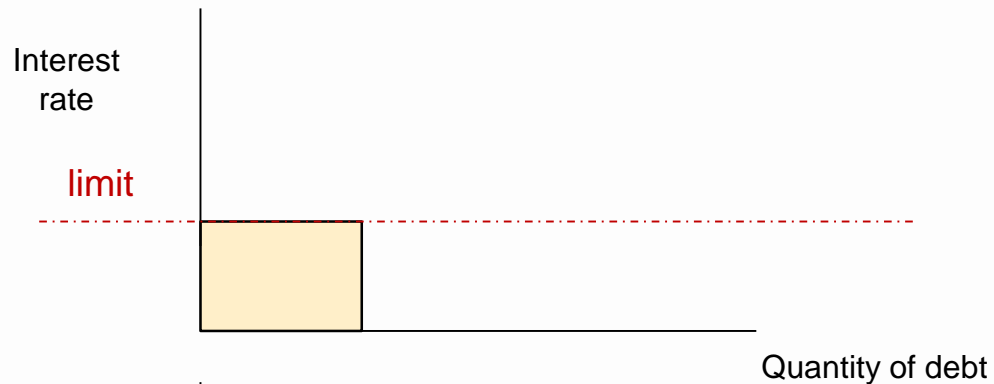
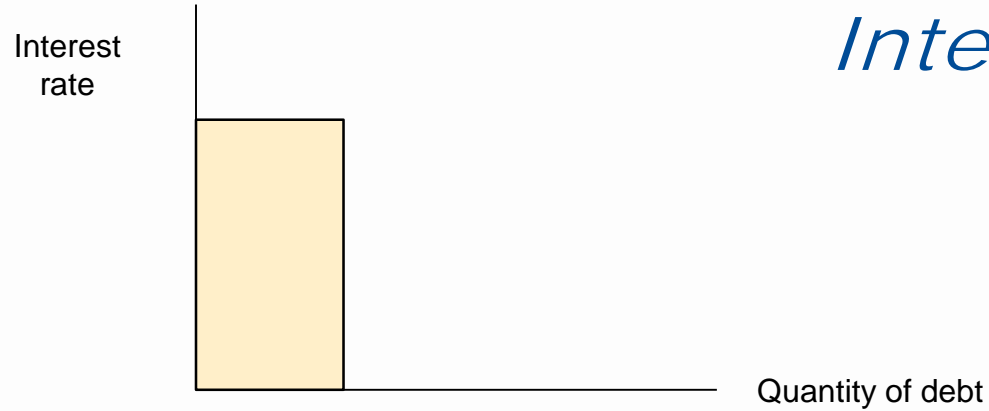
Example note: MNEs can access debt markets at much lower rates

Interest Case 2

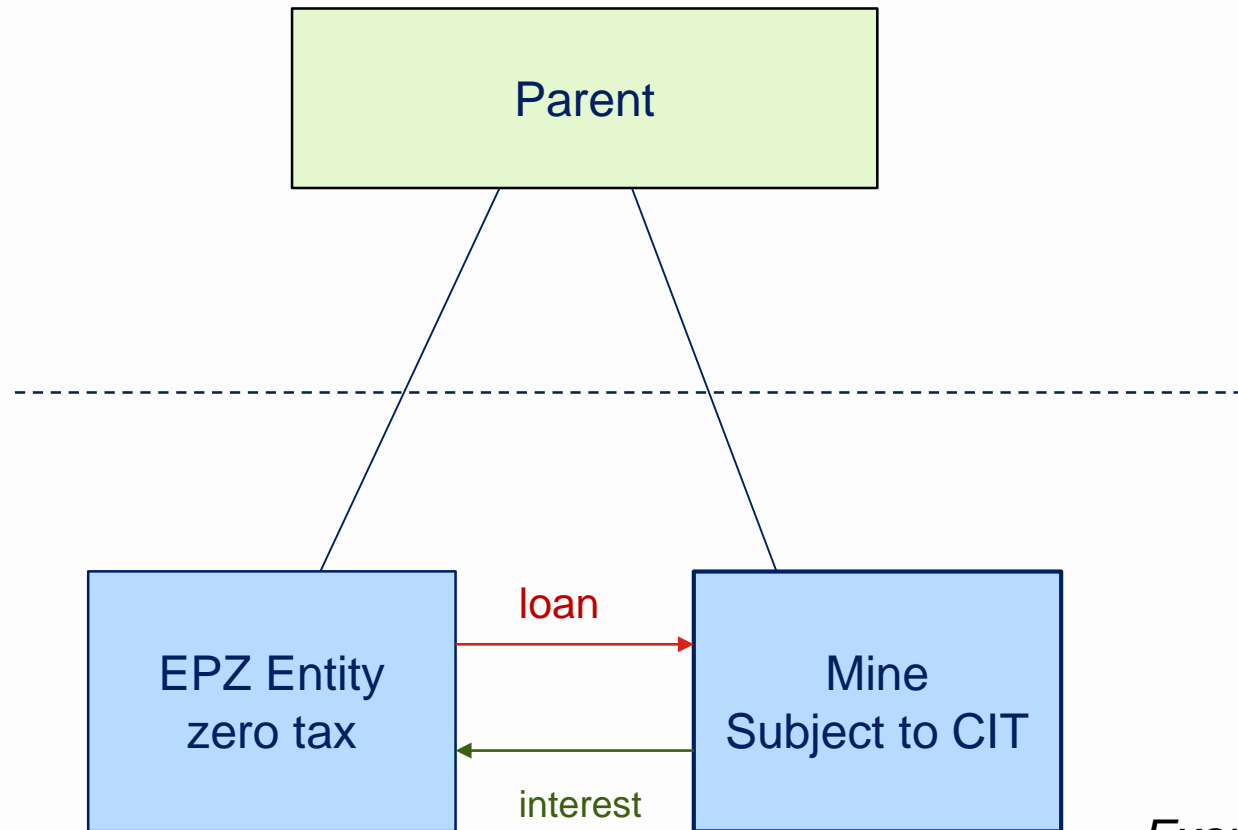
Country imposed an interest rate cap...

...but had no thin capitalization (debt relative to equity) or other limitations

...so the quantity of debt increased significantly.



Interest Case 3



Excessive interest deductions can be used in purely domestic setting

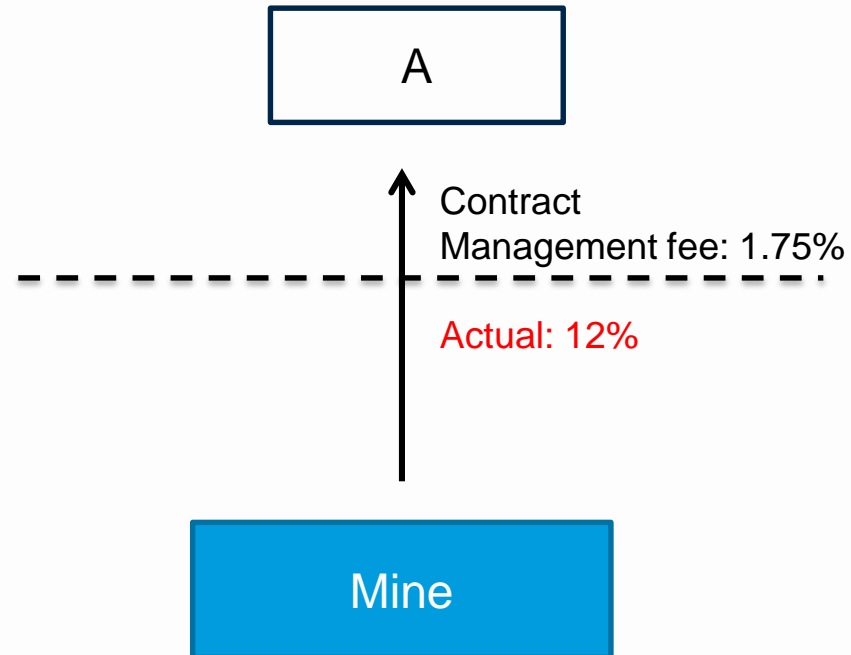
Entities with different tax treatments (e.g. zero-taxed entities in export processing zone) create tax planning opportunities

Example note: Domestic related entities entered into large loan arrangements at tax cost of EUR 20 million per year

Domestic Revenue Mobilization Challenge: Transfer Pricing

Transfer Pricing Case 1

Country Example

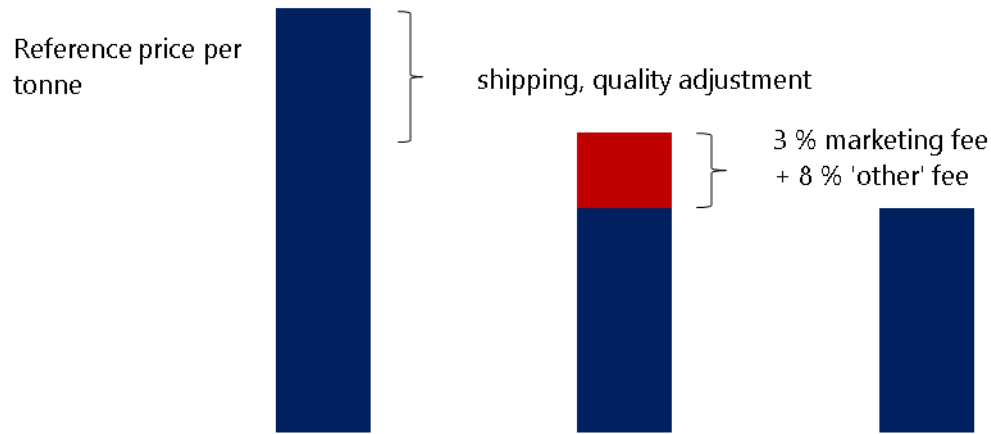


Company contract set a “management fee” at 1.75%

But in tax returns, actual fee charged was 12%

**Cost: USD 9 million tax/year,
risk: 200 million lost over life of mine**

Transfer Pricing Case 2



Product pricing – price penalties and discounts used in sales to related party affiliates in low-tax countries.

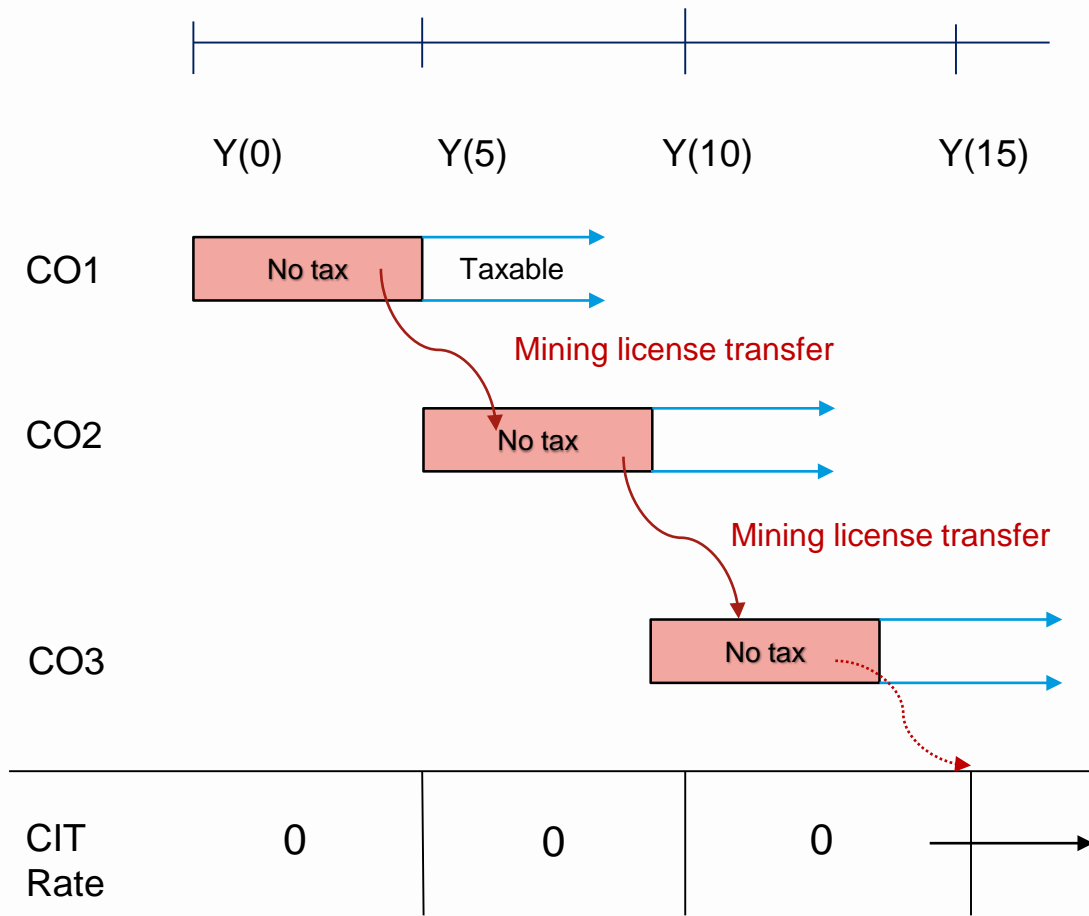
Country example: 8% discount applied to price of all production without explanation, when sold to affiliate in low-tax country.

Included one discount previously denied in an earlier company audit – MNE simply renamed it and continued.

Around 500 million profit (not tax) shifted offshore.

And: Other domestic challenges

Abusive Use of Tax Incentives

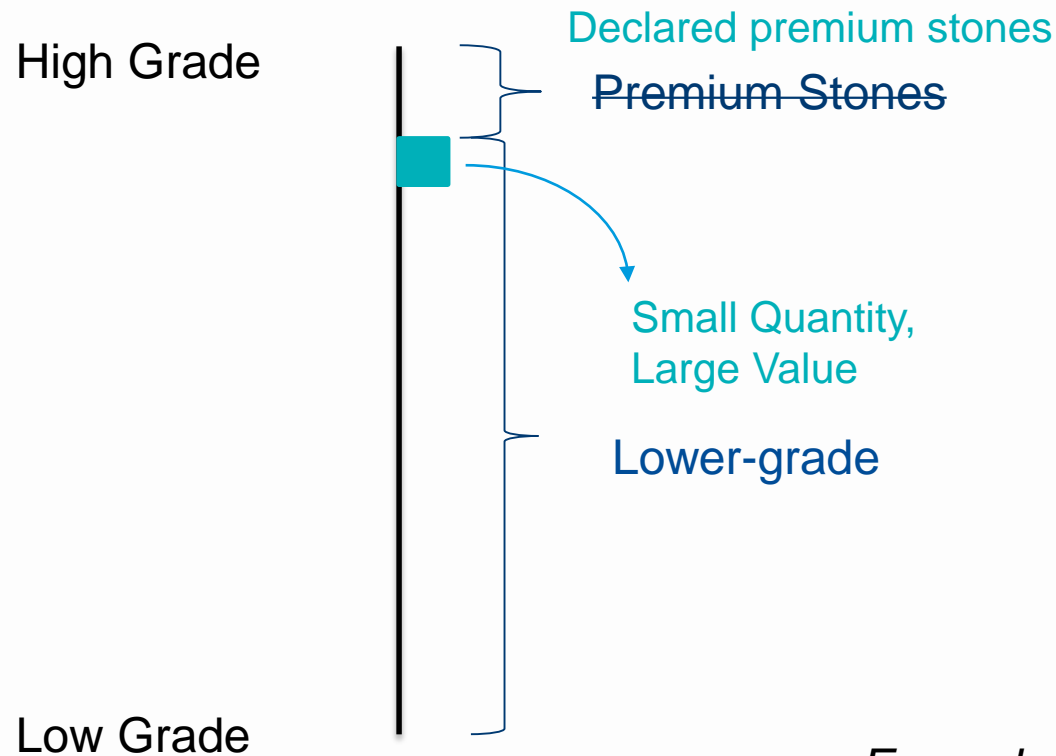


Tax incentives: encouraging domestic tax planning and cost mis-allocation between local entities. Ad-hoc agreements also complicate fiscal settings and potentially reduce scrutiny of settings

Stabilization clauses: hindering corrections to tax law and complicating transition - 30 years in some cases

Example note: Tax holiday afforded to company, not based on mining license - allowed transfer of license to a new company (same owners) every few years, resetting the tax holiday

Capacity Constraints in Tax Administration



Industry expertise: Must understand the industry

Have capacity to control sales, identify risks and detect profit shifting

Capacity gaps: small number of auditors, lack of skills, weak systems, hard to retain staff

Mis-classified gemstones: 4 million lost/year, 100 million over life of mine

Example note: Small number of gemstones mis-classified as non-premium. 4 million tax lost per year, risk of 100 million over life of mine

Final Comments and Discussion

We are seeing progress, however

- ***South Africa: An interest rate cap included as part of formula calculating interest limitation rules.***
- ***Sierra Leone: 2018 law sets fiscal terms for all new resource projects, prohibits special deals.***
- ***Guinea: 2019 Budget closed several avenues for profit shifting, building on improvements in 2013.***
- ***Kenya: Introduced limitation of benefits article in treaties to limit shopping.***
- ***Liberia: introduced stronger transfer pricing legislation and documentation requirements in 2017***
- ***Mali: Introduced thin capitalization restrictions.***

Capacity of authorities must be a priority, but need to make their jobs manageable.

- ***TA remains important part of the way forward***
- ***As well as simplifying measures wherever possible that approximate the right outcome.***

Possible Focus Areas for Discussion

What are the major BEPS risks, where should we focus?

How can those BEPS risks best be addressed in Africa? (are incremental reforms sufficient, or something more radical?)

What about blunt instruments, such as AMTs, safe harbors?

[What are good options at the table in the IF for them, specifically for mining (where reform should strengthen source, not residence or destination)]