TRANSFORMING MINERAL RESOURCES WEALTH INTO SUSTAINABLE DEVELOPMENT

Licences & Contract Negotiation: Basis of Future Revenue

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KEY BENFITS OF THE MINING INDUSTRY

- **FISCAL BENEFITS**

  Mineral Revenue
  (from taxation or other financial provisions)

- **NON FISCAL BENEFITS**

  - **Employment**
  - **Supplies of Goods and Services**
  - **Infrastructural Development**
  - **Training and Technology Transfer**
  - **Value Addition Industries**

KEY INSTRUMENTS

Licences and Contracts are one of the key regulatory instruments used by Governments to implement sector policies and legislation

LICENCES

- Legislative instrument to regulate access to minerals
- Administrative tool to permit mineral activities *(different types of licences)*
- Impose statutory requirements in respect of **fiscal terms**, amongst others
- May be issued subject to an agreed contract *(usually for large-scale mining)*

CONTRACTS

- Consensual contractual relationship between the parties
- Binding terms and conditions, including **fiscal terms**
- Reflect legislative requirements and elaborate upon project specific details
- May form part of terms and conditions of a licence

Licence and Contract Negotiation and needs to be Consistent with National Policies and Legislation

Why Contractual Arrangements in the Mining Sector

Typical circumstances under which contractual relationships between Governments and Mining Companies tend to be entered into:

- where a proper legislative and regulatory framework for mineral exploration and development is either non-existent or inadequate.
- Where relevant mining laws and regulations do exist but investors insist on contractual relationships primarily as a guarantee against perceived investment risks.
- Where the grant of a mineral licence is made under a well-established legislative framework and trusted investment environment but the legislation also allows for the negotiation of certain issues as a measure of flexibility.

ISSUE FOR CONSIDERATION

Whether to establish fiscal terms in legislation or leave them subject to contract negotiation

Governments and investors prefer mineral activities to be conducted in the context of an established legislative framework.

HOWEVER

On a case by case, certain key issues of concern to the Government or an investor can be subject to contract negotiation.

There are Pros and Cons to consider in making a decision on what fiscal terms should be fixed in legislation or subject to contract negotiation

Pros and Cons for fixing Fiscal Terms in Legislation or leaving them subject for contract negotiation

Some Key Attributes of a Modern Mining Fiscal Regime	Fixed Legislative Fiscal terms	Negotiable Fiscal terms
Assured Revenue to Government (Taxes , Royalties, Levies)	+	-
International Competitiveness (Investors Returns and Government Take)	+/-	+
Transparency of Fiscal Terms	+	-
Administration Efficiency	+	-
Fiscal Progressivity (Resource Rent Tax and Variable Income Tax)	+/-	+/-
Predictability of Fiscal Terms	-/+	+
Minimum Government Discretion	-/+	+
Fiscal Stability	-	+

OBJECTIVE

To strike an appropriate balance between fixed and negotiable fiscal terms

There is no best policy prescription on **WHAT SHOULD BE FIXED IN LEGISLATION** and **WHAT SHOULD BE NEGOTIABLE.**

But the approach as set out below provides a reasonable basis to strike an appropriate balance:

- To provide the standard fiscal terms and conditions in the legislation;
- To provide enabling provisions under the legislation which will allow Government the flexibility to enter into and negotiate certain agreements with investors.

The Fiscal Structure for Revenue Sharing

- **Legislated Fixed Fiscal Elements – Royalty, Income Tax, etc**
  - ✓ Transparency
  - ✓ Efficiency
  - ✓ Predictability
  - ✓ Flexibility (fiscal progressivity) – RRT, VRIT

- **Negotiable Fiscal Elements**
  - ✓ Flexibility (biddable element/State Participation)
  - ✓ Stability (freezing applicable tax legislation)

Future Basis of Mineral Revenue Sharing

- Consistent with the fiscal structure discussed, modern mineral taxation trends support the fixing of such elements of the fiscal regime in legislation provided that it delivers a fair and equitable share of fiscal revenue to the Government whilst earning investors internationally competitive returns on their investment

- Contractual negotiation of fiscal elements is concerned with securing stability of fiscal terms in the contract, to the extent that they are fair and equitable.

- In addition to revenue sharing fiscal elements, contract negotiation deals with negotiation of specific technical details of the fiscal elements.

Technical Details of the Fiscal Arrangements

- **Ring-Fencing**

  Providing clear provisions to address operational aspects of the taxable entity (tax unit) (e.g. Licence basis, contract basis)

- **Valuation**

  Application of arm's length pricing principle for determination of the basis on which revenue for tax purposes is calculated.

- **Marketing Arrangements**

  Application of transfer pricing rules in respect of the type of the mineral commodity market and marketing arrangements concerned.

- **Accounting Annex**

  Provides the specific details with respect to the procedure and principles for treatment and accounting of revenues, expenditures, prices, production, etc.

Non-fiscal Aspects of Contract Negotiations

Contract negotiations have been necessary to facilitate major investment in infrastructure required to support a mineral project. Whilst such facilitation may/may not take the form of fiscal concessions, there has been a strong case for Government involvement in such investment where the infrastructure may have wider benefit to the host country.

In such a case, negotiations have invariably dealt with a range of factors, including:

- ❖ Usage of the infrastructure – tariff and open access issues
- ❖ Financing of the infrastructure – availability of concessionary financing and terms and conditions, as well as risk allocation and operational arrangements
- ❖ Public consultations
- ❖ Special investment tax incentive schemes – availability of incentives and justification for it
- ❖ Public Private Participation – terms for State participation and risk/rewards considerations

In Conclusion

- Modern taxation trends in mining taxation demonstrate emphasis on satisfaction of Government’s mineral revenue objective, largely through legislated fiscal terms.

- Increasingly, contract negotiation is concerned with securing fiscal stability within the context of fairness and equity considerations.

- The scope for contract negotiation remains important for settling specific operational details with respect to the determination of revenue.

- Non- fiscal matters are playing a greater role in contract negotiation as investment in infrastructure related to mineral projects create opportunity for Governments to address infrastructure needs of the host country.

THANK YOU