

Taxing the Minerals Sector in South Africa: A comparative analysis of the proposed tax model for South Africa and the models adopted in selected African countries

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ABSTRACT

The State Intervention in the Minerals Sector Report emerged as a resolution during the 3rd National General Council Resolution on Economic Transformation held in 2012, during which the Council stated that: “The ANC’s approach to economic transformation of the South African economy should always be holistic and comprehensive, covering all sectors of the economy. In this regard, the ANC should ensure greater state involvement and control of strategic sectors of the economy, such as mining, energy, the financial sector and others.” It was for this reason that the National General Council mandated the National Executive Committee to ensure that further work be done on ways in which the African National Congress can implement economic transformation in sectors such as the mining industry. It was suggested that methods including research, study tours and discussions be conducted to gather the required information. As a result of the research, *The State Intervention in the Minerals Sector Report* emerged. In *The State Intervention in the Minerals Sector Report*, the mineral sectors of developed as well as developing countries are compared with each other. The developing countries compared included Botswana, Zambia, Ghana, Liberia and Sierra Leone, and these countries have also been selected for the purpose of comparison in the present research.

The goal of this study is to analyse the recommendations made in *The State Intervention in the Minerals Sector Report* regarding State involvement in the minerals sector. To determine whether the economic situation in South Africa is comparable to the five other African countries, an analysis based on demographic indicators, the history of the minerals sector in the various countries, its contribution to the fiscal regime of that country, its economic contribution, as well as the extent of involvement from Government and the model implemented for its involvement, is conducted. According to a work paper published by the World Bank on the world development indicators for 2014, control over metal supply to the economy has been considered vital for political and economic reasons in most societies. It further states that most State-owned mining companies have over the years and, in particular, in developing countries, not been able to operate successfully, leading to privatisation. Poor performance is, however, not necessarily the reason for State ownership. Areas not addressed by this thesis include the Gold Mining industry in South Africa and the Diamond mining industry in Botswana.

Key words: nationalisation; State participation; taxation; the minerals sector;

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CHAPTER 1

INTRODUCTION

1.1 Research context

According to the report “Facing an uncertain future: Government intervention threatens the global mining sector” (Thornton: 2011), the mining industry faces an uncertain future. Increasing and unpredictable Government intervention across the globe is adding further complexity to a sector that is already heavily laden with risk.

The debate in South Africa on the nationalisation of its mining sector was largely spurred on by the African National Congress Youth League. The African National Congress Youth League drew up a document entitled “Towards the transfer of Mineral wealth to the ownership of the people as a whole: A Perspective on Nationalisation of Mines”, (ANC Youth League: 2010), which was discussed at numerous events held by the League throughout the country.

In *The State Intervention in the Minerals Sector Report* (ANC: 2012), on the State intervention in the mineral sector, it was originally proposed that the Government take up a minimum 60% stake in all mining companies currently operating within South Africa. This, it was said, should be done via a State-owned mining company. The remaining 40% would then be owned by the private sector, and should still be subject to and compliant with the regulations set out in the Mining Charter and other legislation that governs the minerals sector.

According to *The State Intervention in the Minerals Sector Report* (ANC: 2012), the reasoning behind the idea of nationalising the mining sector was to ensure that all South Africans enjoy a greater benefit from the profits made by the mining companies. The reasons, according to the report are:

- greater control over one of the largest and most profitable sectors in South Africa;
- to enable the Government to generate additional revenue for the provision of basic services to all South Africans; and

- the alleviation of unemployment, through local beneficiation and industrialisation of mineral resources by the Government.

Although these reasons might appear to be sound, the most obvious flaw in the proposal is that South Africa is a developing country with an emerging economy that is heavily dependent on foreign investors for its economic well-being and growth and cannot afford to lose these investments.

According to Azar Jammine, the director and chief economist at Econometrix (The Daily Maverick, 2011: Online), he explains that the very first thing that would happen if South Africa were to nationalise its mining sector, would be a rapid depreciation of the rand due to substantial outflow of capital from the country, which would then cause high interest rates and inflation in the mid- to long-term. This would then lead to slower economic growth and a loss of jobs, and should that happen, it would have adverse consequences for the South African economy as a whole.

A closer look at the mining sector and the contribution it makes to South Africa is necessary. According to the report "Mining in South Africa: 2013" (Mining Intelligence Database: online), South Africa is a world leader in mining. The country has an abundance of mineral resources, accounting for a significant portion of the world production and reserves, which are seen as some of the world's most valuable minerals. The estimated value of these minerals is in the region of R 20.3 trillion, and it is for this reason that the mining of these minerals in South Africa is a key foundation industry that has made South Africa one of the most industrialised countries on the African continent. Furthermore, due to the number of minerals found in South Africa as well as the amount thereof, the minerals sector within South Africa contributes greatly to the value of its gross domestic product.

In her article Kearney (2012), a reporter for SouthAfrica.info, submits that in recent years, the contributions made by the mining industry to the economy have declined, while there has been growth in South Africa's secondary and tertiary sectors. Nonetheless, the mining sector still accounts for roughly one third of the market capitalisation of the Johannesburg Stock Exchange, and continues to act as a magnet for foreign investment into the country.

In a presentation made by Roger Baxter, Senior Executive of the Chamber of Mines of South Africa (2011), he stated that the mining sector in South Africa plays a vital role in the development and sustainability of the country. It is one of the largest employers of semi-skilled and skilled workers, and acts as a significant multiplier in the rest of the economy through large procurement deals, investments in infrastructure and the economy, and by being a wage spender to locally employed workers.

Kearney (2012) goes on to say that South Africa's economy relies heavily on the mining sector (especially gold and diamond mining) and it is an important foreign exchange earner, with gold accounting for more than one-third of exports. Besides gold, South Africa's diamond industry is the fourth largest in the world, and South Africa is seen as a major producer of coal, manganese and chrome.

It is clear that the contribution that South Africa's mineral sector has and can make to the future development of South Africa is fundamentally important. It is submitted that the real focus should not be on whether or not the South African Government should intervene in the mineral sector, but rather the manner in which it should get involved.

Mining companies currently operating within South Africa (with the exclusion of gold mining companies) are subject to the same taxation structure as is imposed on all other companies in other sectors. This may be a matter for concern, as mining companies should possibly not be treated in the same way for tax purposes, bearing in mind both the positive and negative impact that mining has on the South African environment and the economy. Although mining companies operating in South Africa are contributing extensively in areas such as the development of infrastructure, attracting foreign investment and are large payers of salaries to semi-skilled and skilled workers, the negative effect mining has on South Africa must also be considered. This negative impact is very real and of grave concern to the future sustainability of ecological systems, the environment and the health of people living near these mines and the "rehabilitated mines" in South Africa.

It is submitted, therefore, that mining companies should not be subject to the same taxation model as, for example, a company operating in the financial or logistics sector. Rather, it would appear to be more effective, for the Government to intervene in the minerals sector by way of a unique tax model that applies only to the mineral sector and, in particular, the mines that extract these minerals.

By having the mining companies pay an industry-specific tax, the Government will have access to tax funds collected specifically to address issues pertaining exclusively to this sector. Some of the issues that can be addressed with dedication funds from mining include:

- combating harmful chemicals being released into the air and polluting the atmosphere; and
- creating a rehabilitation fund for victims living near contaminated areas where people show symptoms of extensive over-exposure to the pollution and by-products of mining.

Currently, mining companies earning taxable income derived from mining for diamonds, and other base minerals are taxed on a flat rate basis, of 28% in terms of the Income Tax Act, 58 of 1962, while mining companies earning taxable income derived from mining for gold are taxed on a formula basis. Companies mining for gold do not fall within the scope of the present research.

The current tax model applicable in South Africa, as well as the proposed tax model will be compared to the tax models applied in Zambia, Botswana, Liberia, Ghana and Sierra Leone. All of these countries are situated in Africa, and are classified as developing countries. Each of these countries has a different tax regime. It is essential that the tax model applying to the minerals sector in South Africa should be appropriate to address the concerns of the parties involved and to this end a comparison of various tax models will be made.

1.2 Research goals

The present research aims to draw a comparison between the current tax model for the mining sector used in South Africa, against the tax model proposed in *The State Intervention in the Minerals Sector Report* (ANC:2012) as well as the tax models applying in Zambia, Botswana, Liberia, Ghana and Sierra Leone. In addressing this aim, the following are the sub-goals:

- to discuss the current taxation structure applying to the minerals sector in South Africa as set out in the Income Tax Act;

- to discuss State participation in its various forms and how it is proposed in *The State intervention in the Minerals Sector Report* (ANC:2012) as well as how it is applied in Botswana, Zambia, Ghana, Liberia and Sierra Leone.
- to compare mining activities in South Africa with mining activities in Botswana, Zambia, Ghana, Liberia and Sierra Leone;
- to analyse the taxation models used in Botswana, Zambia, Liberia, Ghana and Sierra Leone;
- to compare the tax models used in South Africa, Botswana, Zambia, Ghana, Liberia and Sierra Leone, to the model proposed in *The State Intervention in the Minerals Sector Report*.

1.3 Research methodology

An interpretive research approach will be adopted for the present research as it seeks to understand and describe (Babbie & Mouton: 2009). The research methodology to be applied can, for the greater part, best be characterised as a doctrinal research methodology. This methodology provides a systematic exposition of the rules governing a particular legal category, the minerals sector of South Africa, Zambia and Botswana; analyses the relationship between the rules, explains areas of difficulty and is based purely on documentary data (McKerchar: 2014).

The documentary data to be used for the research consists of:

- The South African Income Tax Act 58 of 1962;
- The Petroleum Resources and Development Act, No 28 of 2002;
- Mining advocacy organisations (Chamber of Mines): *South Africa, Ghana, Botswana, Zambia*.
- African Economic Outlook Organisation (2012): *Sierra Leone*;
- African Economic Outlook Organisation (2012): *Liberia*;
- Department of Minerals and Energy (2007): *Discussion document – A strategic framework for implementing sustainable development in the South African Minerals Sector. Towards developing sustainable development policy and meeting reporting commitments*;

- ANC (2012): State Intervention in the Minerals Sector. Summary of the Report prepared for the ANC NEC. Maximising the developmental impact of the People's Mineral Assets
- ANC Youth League (2010): *Towards the transfer of Mineral wealth to the ownership of the people as a whole: A Perspective on Nationalisation of Mines.*
- DANIEL et al. (2010): The World Bank Extractive Industries Source Book. State participation in the Natural Resource Sectors: Evolution, Issues and Outlook, in the taxation of Petroleum and Minerals: Principles, Problems and Practice.

The research is conducted in the form of an extended argument, supported by documentary evidence. The validity and reliability of the research and the conclusions will be ensured by:

- adhering to the rules of the statutory interpretation, as established in terms of the statute and common law;
- placing greater evidential weight on legislation and the writings of acknowledged experts in the field;
- discussing opposing viewpoints and concluding, based on a predominance of credible evidence; and
- the rigour of the arguments.

As all the data is in the public domain, no ethical considerations arise. Interviews will not be conducted; opinions will be considered in their written form.

1.4 Structure of the thesis

The remaining chapters of this thesis are structured as follows. Chapter 2 briefly discusses the history of mining activities in South Africa and the contribution the non-gold mining industry has made in South Africa. Chapter 3 looks at the current tax model imposed on the South African mineral mining industry. Chapter 4 presents a detailed review of the report prepared for the ANC on the State Intervention in the minerals sector and the proposed tax model to be imposed. Chapter 5 discusses what, according to the World Bank, needs to be in place when the Government participates with the private sector in the minerals sector, as well as the forms of State participation currently in Zambia, Botswana, Ghana, Liberia and Sierra Leone. In chapter 6 country comparisons are carried out using the history and macroeconomic indicators of the

five African countries identified (Zambia, Botswana, Ghana, Liberia and Sierra Leone) against that of South Africa. Chapter 7 discusses the tax models imposed on the mining sectors of Botswana and Zambia, Ghana, Liberia and Sierra Leone. Chapter 8 concludes the thesis with a summary of the goals, findings, and limitations of the research.

Due to the fact that the tax calculation applicable to mining for gold in South Africa and mining for diamonds in Botswana differs from the tax calculation used in mining for other minerals, these two sectors have been excluded from the current research so as to limit the scope of the research.

CHAPTER 2

INTRODUCTION AND BRIEF HISTORY OF MINING ACTIVITIES IN SOUTH AFRICA AND THE CONTRIBUTIONS THE NON-GOLD MINING INDUSTRY HAS MADE TO SOUTH AFRICA

2.1 Introduction

In order to discuss the future impact that the mining and minerals industry will have on South Africa, it is important to understand what the mining industry has meant for South Africa in the past.

According to the report on mining in South Africa, (Mining Intelligence Database, 2013:online), mining in South Africa has been the main driving force behind the history and development of Africa's most advanced and wealthiest economy and "directly contributed to the establishment of the Johannesburg Stock Exchange in the late nineteenth century."

It is submitted that mining in South Africa has not only impacted the mining sphere, but has helped shaped South Africa's history as a whole. It is due to this impact as well as the opportunities that the mining industry hold that there is so much focus and interest in the industry as well as the control of its resources and revenues.

This chapter will explore the different ways in which the mining industry has helped shaped the country in the past as well as the potential it holds for its future.

2.2 History of the mining industry of South Africa

Information obtained from Wikipedia (Online) "Mining industry of South Africa" reveals that it was the discovery of a diamond on the banks of the Orange River in 1867 by Erasmus Jacobs that began large scale and profitable mining in South Africa. Thereafter, when an area northeast of Cape Town, Kimberley, was found to have rich diamond deposits, thousands migrated there to try to profit from the discovery. Later on, Griqualand West, which was the area surrounding Kimberley and the diamond fields, was annexed by the British. When the Republic attempted to annex areas near newly discovered diamond fields in 1868, the nearby British colonial government protested, leading to the First Boer War of 1880-1881.

Wikipedia (Online) further reports that the discovery of gold resulted in people rushing to the Pilgrim's Rest and Barberton areas, but the biggest gold discovery of all was in the Witwatersrand when Gerhardus Oosthuizen discovered the Main Reef Leader on Portion C of his farm "Langlaagte". This discovery of gold triggered the Witwatersrand Gold Rush of 1886, and, as in the case of the discovery of diamonds, in the migration of hundreds of foreign expatriates to the region. This contributed to heightened political tensions in the area and ultimately led to the Second Boer War in 1899.

Furthermore, according to the report on mining in South Africa, (Mining Intelligence Database, 2013: Online), the Anglo-Boer War, now known as the South African War, which led to this country becoming part of the British Empire from 1910-61, was triggered by the discovery of the world's largest gold deposits in the Witwatersrand, and the huge potential for mining in South Africa. It was also during this period that dangerous labour practices and old techniques such as using living canaries as gas detectors were replaced by more advanced mining methods. These included sophisticated ventilation and, in time, chemical extraction of minerals from low-grade ore. As the growth of the South African mining industry demanded such a high level of industrial support, it stimulated the economy and turned South Africa into a mining country. This report goes on to state that gold mining peaked in 1970 in South Africa and contributed 68% of global production for that year. By 2001, a total of 51% of global platinum group metals ever mined had been produced in South Africa.

Today there are numerous multinational mining companies, that have roots on the continent and abroad, that can be found in South Africa. Some of the largest include BHP Billiton, Anglo American and Xstrata. According to Mining Intelligence Database (2013: Online), these companies are currently mining vast amounts of minerals in the country and are worth an estimate well in excess of US\$200 Billion.

In a report drafted for the Gauteng Department of Agriculture, Environment and Conservation (Digby Wells and Associates: 2008), South Africa's amazing variety of minerals has been a catalyst in changing it from an economy based on agriculture, to one based on mining and industry.

According to *The State Intervention in the Minerals Sector Report* (ANC,2012:4), the minerals found in South Africa "include some of the largest reserves of the platinum group metals, ... gold, chromite, manganese, vanadium and refractory minerals", as

well as large deposits of “coal, iron ore, titanium, zirconium, nickel, vermiculite, phosphate and many other minerals.”

The State Intervention in the Minerals Sector Report (ANC, 2012: 4) also included results of a study based on the 2009 mineral production rate indicating that South Africa’s reserves for all minerals will last for several hundred years if no further resources are delineated, except for gold, lead and zirconium. (Department of Mineral Resources: 2009)

Table 1

South Africa’s Mineral Reserves, World Ranking, 2009 Production & Nominal Life (assuming no further reserves) at 2009 Extraction Rates

Mineral	Unit	RESERVES			PRODUCTION 2009			LIFE Years
		mass	%World	Rank	Mass	%World	Rank	
Alumino-silicates	Mt	51	*	*	0.265	60.2	1	192
Antimony	kt	350	16.7	3	3	1.6	3	117
Chromium Ore	Mt	5500	72.4	1	6.762	*	1	813
Coal	Mt	30408	7.4	6	250.6	3.6	7	121
Copper	Mt	13	2.4	6	0.089	*	*	146
Fluorspar	Mt	80	17	2	0.18	3.5	5	444
Gold	t	6000	12.7	1	197	7.8	5	30
Iron Ore	Mt	1500	0.8	13	55.4	3.5	6	27
Iron Ore - including BC	Mt	25000	~10	*	55.4	3.5	6	451
Lead	kt	3000	2.1	6	49	1.2	10	61
Manganese Ore	Mt	4000	80	1	4.576	17.1	2	874
Nickel	Mt	3.7	5.2	8	0.0346	2.4	12	107
PGMs	t	70000	87.7	1	271	58.7	1	258
Phosphate Rock	Mt	2500	5.3	4	2.237	1.4	11	1118
Titanium Minerals	Mt	71	9.8	2	1.1	19.2	2	65
Titanium- including BC	Mt	400	65	1	1.1	19.2	2	364
Uranium	kt	435	8	4	0.623	1.3	10	698
Vanadium	kt	12000	32	2	11.6	25.4	1	1034
Vermiculite	Mt	80	40	2	0.1943	35	1	412
Zinc	Mt	15	3.3	8	0.029	0.2	25	517
Zirconium	Mt	14	25	2	0.395	32	2	35

Source: SAMI 2009/2010, DMR 2010; and Wilson & Anhaeusser 1998: “The Mineral Resources of South Africa”, CGS Pretoria (for BC- Bushveld Complex)

In a presentation to the South Africa’s Mining Industry, Roger Baxter, Senior Executive of the Chamber of Mines of South Africa noted that the mining sector in South Africa plays a vital role in the development and sustainability of the country. It is one of the largest employers of semi-skilled and skilled workers, and acts as a significant multiplier in the rest of the economy through large procurement deals, investments in

infrastructure and the economy, and by being a wage spender to locally employed workers. (Baxter, 2011: 6)

2.3 Mining contribution to South Africa's development, economy and fiscal Position

Information obtained from the report on mining in South Africa, (Mining Intelligence Database, 2013: Online) states that even now the mining industry in South Africa is a significant factor in the history and development of the country and as a leading economy in Africa. It further states that the sector has provided the critical mass for several other industries that either supply the mines or use their products. Some of these industries are specialist seismic geological and metallurgical services, water and engineering services, energy, and financial services.

To summarise, the mining industry has acted as a base for the development of other industries in South Africa, and in this way contributed indirectly to the South African economy.

2.4 South Africa's mineral wealth

Kearney (2012) states that South Africa is home to the largest reserves of manganese and platinum group metals, and among the world's largest reserves of gold, diamonds, chromite ore and vanadium are found here. With an estimated worth of R 20.3 trillion (\$2.5 trillion), South Africa's total reserves remain some of the world's most precious, and, in terms of gross domestic product value, it is estimated that South Africa has the fifth largest mining sector in the world.

Kearney (2012) goes on to say that South Africa's economy relies heavily on the mining sector (especially gold and diamond mining) and it is an important foreign exchange earner, with gold accounting for more than one-third of exports. Besides gold, South Africa's diamond industry is the fourth largest in the world, and the country is seen as a major producer of coal, manganese and chrome. In the tables below the importance of South Africa's mining industry is depicted.

Table 2

The South African mining industry is the world's fifth largest by GDP value...

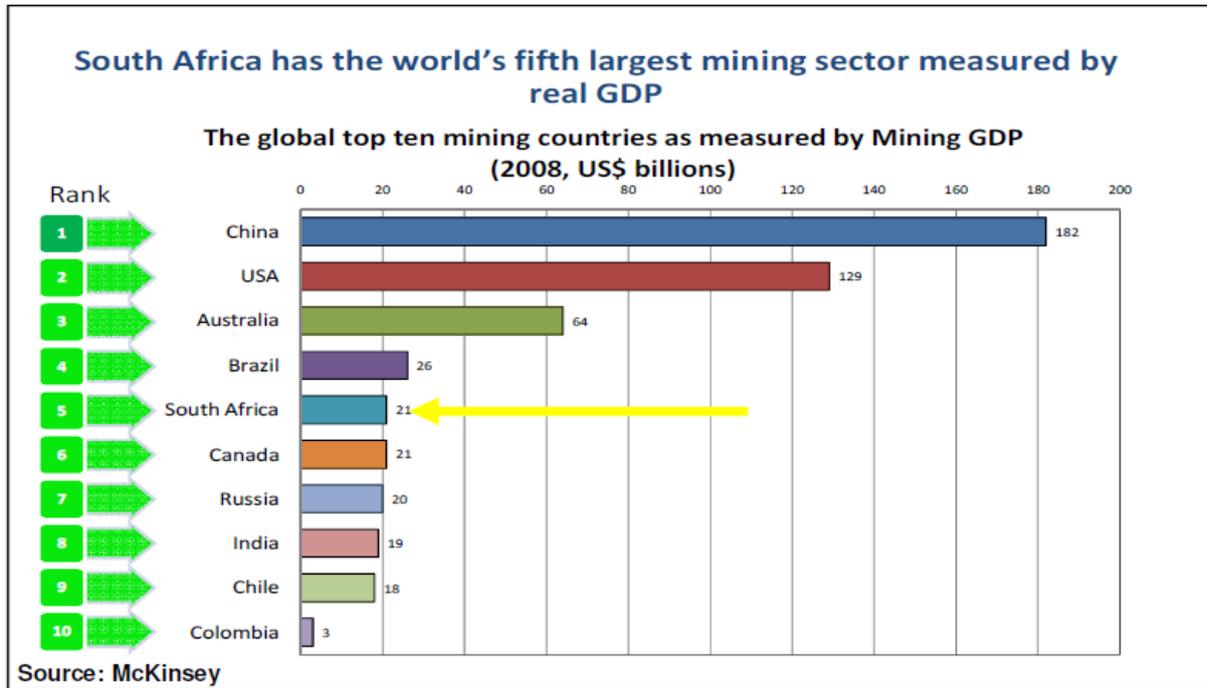


Table 3

South Africa has most of the World's Top Mining Companies participating in the country

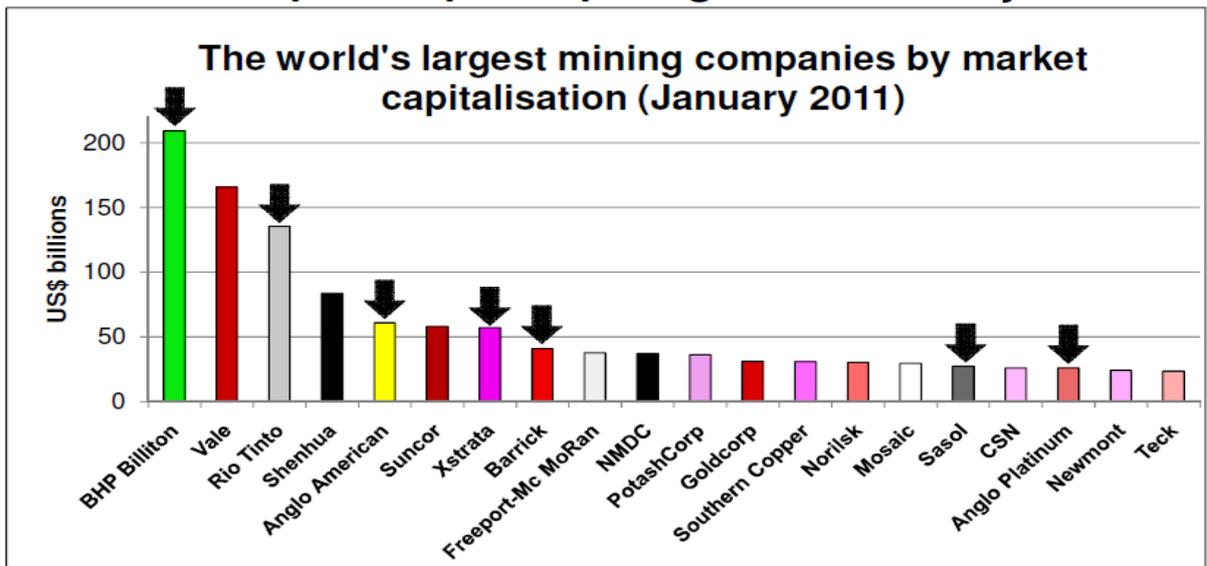
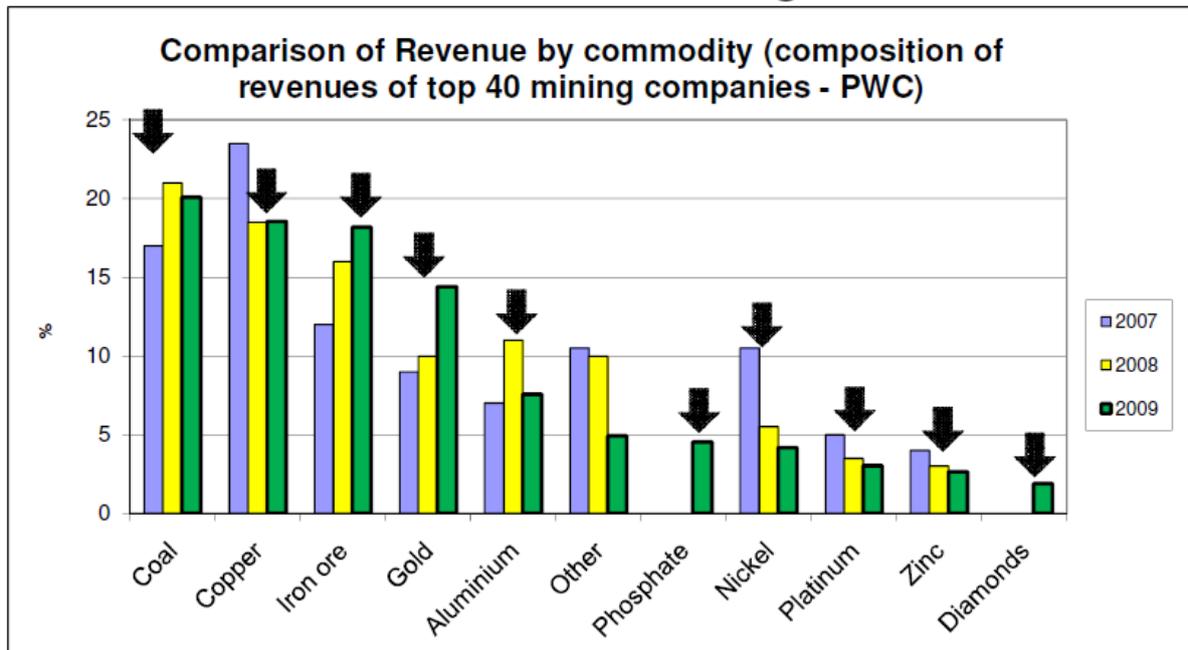


Table 4

South Africa has exposure to most of the top 10 minerals in demand at the global level

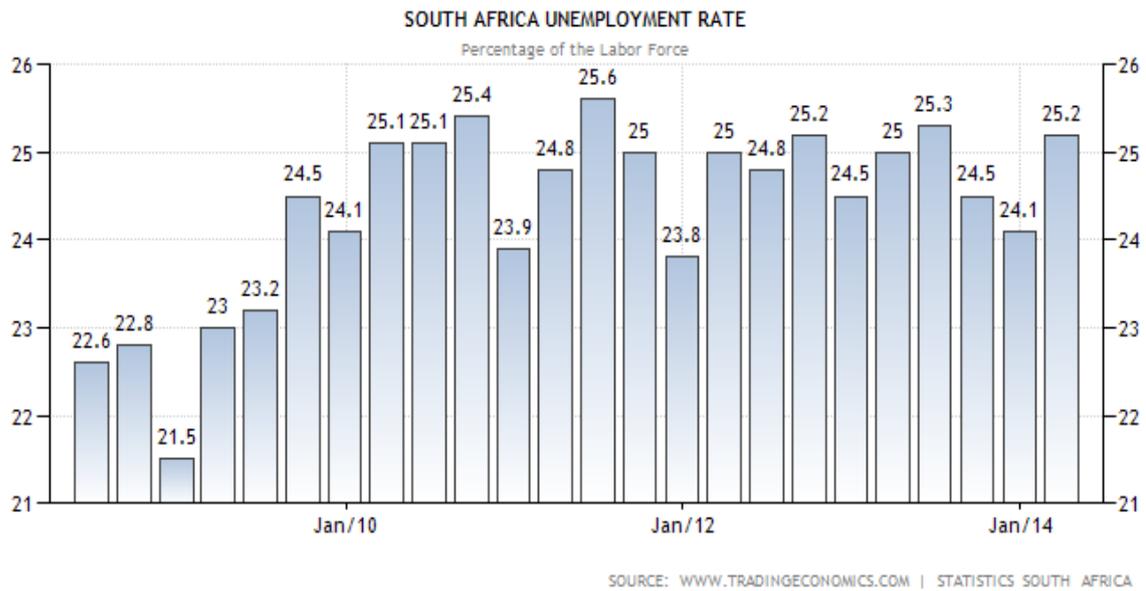


2.5 Mining contribution to sustainability and Broad-Based Black Economic Empowerment (BBBEE)

According to the article on South Africa’s unemployment rate, (Trading Economics, 2014: online) the “unemployment rate in South Africa increased to 25.2% in the first quarter of 2014 from 24.1% in the fourth quarter of 2013.”

Fin 24(2014: online) reports that “South Africa has the third highest unemployment rate in the world for people between the ages of 15 to 24, according to the World Economic Forum Global Risk 2014 report.”

Table 5



According to an article on how the black economic empowerment social programme works, (Black Economic Empowerment South Africa Group Initiative:2014:1), broad based black economic empowerment “is an initiative launched by the South African Government to address the restrictions that exist within the country for black individuals to participate fairly in the economy.”

The initiative, (Black Economic Empowerment South Africa Group Initiative: 2014:1) further explains that it is important to note that black economic empowerment is an exercise in reporting and fosters specific activity in a business. It is, however, a quantitative measure and disregards any qualitative elements. The business will struggle to maintain their black economic empowerment score if transformation is not achieved. Essentially, transformation should establish a fair working environment as well as remove preconceptions and assumptions.

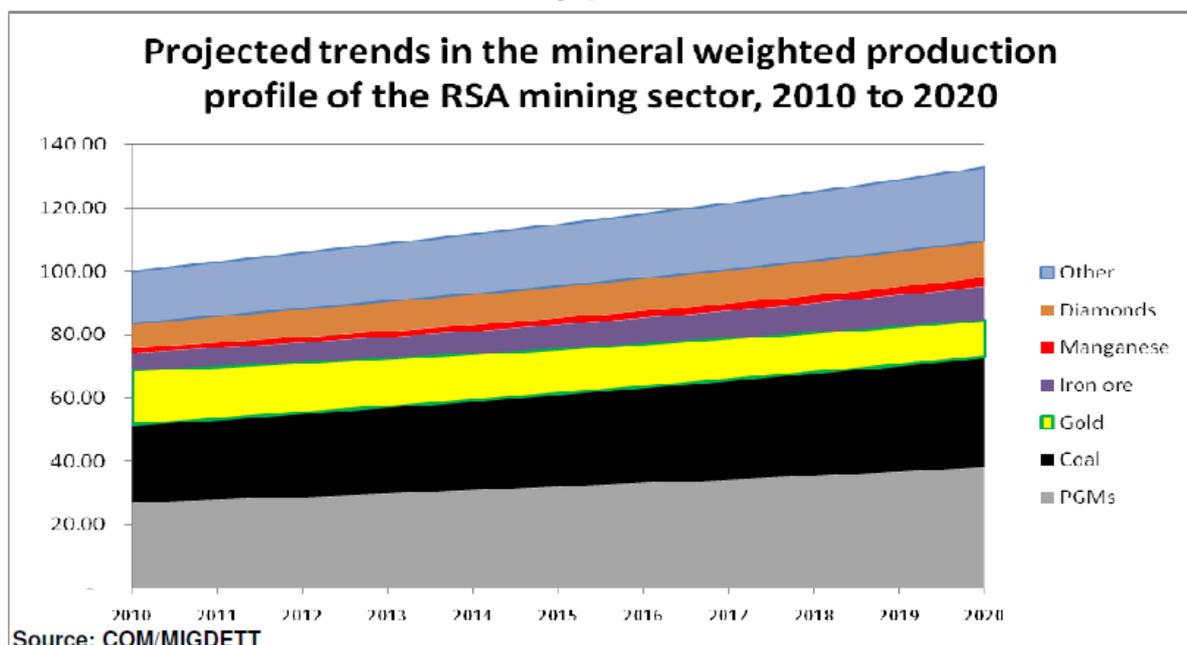
By the end of 2011, the largest contributor of economic transformation in this country was the mining sector as it had completed R150 billion worth of broad based black economic empowerment deals. All companies in South Africa are subject to black economic empowerment targets allowing black South Africans to own a certain percentage of local assets (Kearney:2012).

In the *State Intervention in the Minerals Sector Report* (2012:22), it is claimed that if appropriately configured, one of the few economic activities that can forge strong

infrastructure links to local, provincial, national and regional economies as well as its immediate surroundings, is mining. Therefore, the mineral industry can be regarded as a development catalyst for providing basic infrastructure that can either enhance existing areas of low economic activity or open up previously isolated areas.

Table 6: Projected trends in the mineral weighted production profile of the RSA mining sector, 2010 to 2020

For period 2010 to 2020, conservative modeling indicates that a 3%-4% growth rate & 100 000 jobs for the RSA mining sector is realistically possible.....



2.6 Conclusion

South Africa’s variety of minerals has been a catalyst in changing it from an economy based on agriculture, to one based on mining and industry. (Gauteng Department of Agriculture, Environment and Conservation: 2008).

It would appear that some of the minerals found in South Africa include large quantities of what is considered to be some of the most precious metals worldwide. The contribution made by the mining sector in South Africa can be seen across all sectors of the economy and includes direct contributions such as employment of skilled as well as semi-skilled individuals, but also indirectly through its contributions to better infrastructure and attracting foreign investments to South Africa.

It can therefore be concluded that because of the impact that the mining industry has had on the development of South Africa up to date, and its contributions, both directly and indirectly to the economy that so much focus has been placed on the mining industry as a whole. It is also due to this fact that the Government has probed the National Executive Committee to conduct a study in which it tries to explore the different ways in which the government can gain more leverage in this industry.

The next chapter will discuss the South African Tax model currently applicable to the mining sector of South Africa as set out in the Income Tax Act 58 of 1962.

CHAPTER 3

CURRENT TAX MODEL IMPOSED ON THE MINING INDUSTRY

3.1 Introduction

The previous chapter described the history as well as the current contributions that the mining sector has made to South Africa.

What follows is a summary of the taxation model imposed on the mining sector in accordance to the Income Tax Act, 58 of 1962. It is important to understand the current tax model imposed on the mining sector, so as to better compare it to the tax models used in the other African countries (Botswana, Zambia, Ghana, Liberia and Sierra Leone) as well as the proposed tax model as per the *State Intervention in the Minerals Sector Report* (ANC: 2012) to be discussed later.

According to the South African Revenue Services website (online), Corporate Income Tax; also known as business tax “is imposed on businesses incorporated under the laws of the Republic of South Africa and which derive income from within the Republic or through a branch or permanent establishment within the Republic.”

Before being able to establish whether an operation is seen as a mining operation and therefore taxed as such, it is important to first understand the definition of a mineral and of mining operations. Once an operation is defined as a mining operation in terms of the definitions (discussed in paragraph 3.2.1), the next step is to get an understanding of what is seen as mining income, and mining expenses (income expenses and expenses of a capital nature) as well as the allowances and recoupments and the taxation imposed thereon.

3. 2 Petroleum Resources and Development Act

To establish the definition of a mineral and of mining operations, reference to the Petroleum Resources and Development Act, No. 28 of 2002 is required.

3.2.1 Definitions

Mineral

According to section 1 of the Petroleum Resources and Development Act, a Mineral may be defined as:

any substance, whether in solid, liquid or gaseous form, occurring naturally in or on the earth or in or under water which was formed by or subjected to a geological process, and includes sand, rock, stone, clay, gravel or soil, and any mineral occurring in residue stockpiles or in any residue deposits, but excludes –

- water, other than water taken from land or sea for the extraction of any mineral from such water;
- petroleum; or
- peat.

Mining operations and mining

Also, in terms of section 1 of the Petroleum Resources and Development Act, “mining operations” and “mining” include every method or process by which any mineral, including natural oil, is won from the soil or from any substance or constituent thereof.

3.3 Income Tax Act 58 of 1962

3.3.1 Definitions

Taxable income

According to section 1 of the Income Tax Act, taxable income may be defined as the aggregate of –

- (a) the amount remaining after deducting from the income of any person all the amounts
- (b) allowed under Part I of Chapter II to be deducted from or set off against such income; and
- (c) all amounts to be included or deemed to be included in the taxable income of any person in terms of this Act;

It would thus appear that taxable income is the gross receipts and accruals of an income nature, from a source within or deemed to be in the Republic of South Africa. In addition there are special inclusions in gross income and further additions in taxable income. Next exempt income is deducted and finally deducting therefrom what are called the general and special deductions. If the process described above is followed, one derives a taxable income or assessed loss.

3.3.2 Income related to mining activities

In his presentation at the World Mining Congress held in London, Diliza (2008) stated that a mining company may derive income from mining for gold, or from operations other than mining for gold, as well as from non-mining operations. Different rules and tax rates are applied with respect to these different sources of income. In this regard, it is important to have an understanding of the definitions of mining for minerals other than gold.

In his presentation, Diliza (2008) goes on further to explain that Income received or accrued in respect of the use of the capital or working assets of a mine would be considered as mining income, and when obtained from other assets, would tend to be non-mining income. Non-mining income includes investment income acquired from liquid funds held pending minor expenditure projects or dividend payouts, returns on investment in other companies, banker's acceptances and various other discount instruments. In the case of rentals, if an asset has not been used for mining purposes for a particular period, the income gained from it is not mining income. However, it might have to be taken into account in the determination of the mining tax liability as it is likely to constitute a capital or revenue recoupment.

3.3.3 Expenditure relating to mining activities

Diliza (2008) further stated that a mining company incurs expenditure, which can be classed as either being mining or non-mining in nature. The reason why it is important to group all the different expenses is because of the various tax rates that will apply to these as well as the countless restrictions that will apply to deductions made against mining income. According to general rule, a distinction should also be made between expenses of a revenue nature and those of a capital nature. Working costs are not restricted to being of a revenue nature. For tax purposes it is, therefore, necessary to

also separate costs into capital costs and revenue costs. Revenue costs are deductible in terms of the general deduction formula contained in Section 11(a) of the Income Tax Act. Capital costs are deductible in terms of capital expenditure provisions. This measure represents an exception to the general deduction formula as set out in Section 11(a) of The Act which states that for expenditure to be deductible, it must not be of a capital nature. Working costs typically include salaries and wages, ropes, pipes and steel, electrical power and electrical and mechanical equipment, explosives and other construction and mining costs.

3.3.4 Capital expenditure relating to mining activities

Subject to certain limitations, mining entities are permitted to deduct capital expenditure incurred from taxable income gained from mining operations. However, the capital expenditure incurred on a particular mine is confined to the taxable income obtained from that mine only.

Section 15 of the Income Tax Act

Section 15 of the Income Tax Act provides for the immediate deduction of the following amounts from the income derived by a taxpayer from mining operations:

There shall be allowed to be deducted from the income derived by the taxpayer from mining operations-

- (a) an amount to be ascertained under the provisions of section 36, in lieu of the allowances in section 11 (e), (f), (gA) and (o); [Para. (a) substituted by s. 20 of Act 55 of 1966 and by s. 18 of Act 129 of 1991.]
- (b) any expenditure incurred by the taxpayer during the year of assessment on prospecting operations (including surveys, boreholes, trenches, pits and other exploratory work preliminary to the establishment of a mine) in respect of any area within the Republic together with any other expenditure which is incidental to such operations: Provided that-
 - (i) except in the case of any person who derives income from mining for diamonds in the Republic, the Commissioner may determine that any expenditure referred to in 148 this paragraph shall be deducted in a series of annual instalments, so that only a portion of such expenditure is deducted in the year of assessment in which it is incurred, and the residue in such

- subsequent years of assessment and in such proportions as the Commissioner may determine, until the expenditure is extinguished
- (ii) in the case of any company which derives income from different classes of mining operations, the deduction under this paragraph shall be made from the income derived from such class or classes of mining operations and in such proportions as the Commissioner may determine
 - (iii) any expenditure which has been allowed to be deducted from the income of any person in terms of this paragraph shall not be included in such person's capital expenditure as defined in subsection (11) of section thirty-six.

It is therefore submitted that section 15 of the Act, aims to assist mining operations in allowing the deduction of certain costs associated with prospecting. It is for the Commissioner to determine the proportion of the amount to be deducted in the year of assessment. Expenses may only be deducted from the class of mining operations in which they were incurred, unless otherwise decided by the Commissioner. This measure ensures that mining expenses from an unproductive mine are not used to decrease the taxable income of a more prosperous mine.

The Minister of Finance may rule that these costs can be offset against the income of another mine.

Section 36 of the Income Tax Act

It is submitted that in order to better understand capital expenditure in terms of mining operations, section 36(7C), (7E) and 7(F) needs to be discussed.

(7C) Subject to the provisions of subsections (7E), (7F) and (7G), the amounts to be deducted under section 15(a) from income derived from the working of any producing mine shall be the amount of capital expenditure incurred.

It is submitted that a mining operation can only deduct actual expenditure incurred in the production of mining activities.

(7E) The aggregate of the amounts of capital expenditure determined under subsection (7C) in respect of any year of assessment in relation to any mine or mines shall not exceed the taxable income (as determined before the deduction of any amount allowable under section 15 (a), but after the set-off of any balance of assessed loss incurred by the taxpayer in relation to such mine or mines in any previous year which has been carried forward from the preceding year of assessment) derived by the taxpayer from mining, and any amount

by which the said aggregate would, but for the provisions of this subsection, have exceeded such taxable income as so determined, shall be carried forward and be deemed to be an amount of capital expenditure incurred during the next succeeding year of assessment in respect of the mine or mines to which such capital expenditure relates.

It would appear that capital expenses to be deducted by a mine or mines cannot exceed the taxable income of that mine. As such, the capital deductions may not be used to create a taxable loss for the mining operation. In the event that the actual capital expenses do exceed the taxable income of the mining operations that expenditure shall be carried forward to the next year of assessment and will be deemed to be an expense incurred during that year.

Capital expenditure, according to section 36(11) of the Income Tax Act includes the following:

- i) Expenditure (other than interest or finance charges) on shaft sinking and mine equipment (other than certain expenditure qualifying only for a partial annual redemption referred to below); and
- ii) Expenditure on development, general administration and management (including any interest and other charges payable after 31 December 1950, on loans utilised for mining purposes) prior to the commencement of production or during any period of non-production, and;
- iii) A capital allowance in the case of qualifying gold mines and natural oil mines; and
- iv) Expenditure (excluding the price of land, surface rights and servitudes), the payment of which has become due in or after 1 July 1989 in respect of the acquisition, erection, construction, improvement or laying out of various assets qualifying for partial annual redemption.

The term “capital expenditure incurred” is defined in section 36 and, consists of the amount which remains after deducting mining recoupments from current capital expenditure incurred.

Diliza (2008:2) states that “capital expenditure as defined is deductible instantly from income derived by a taxpayer from mining operations, but may only be claimed once production has begun.” Prior to commencement of production, capital expenditure is carried forward to future years and then redeemed against mining income as and when the income is earned.

Diliza (2008) stated that, however, there are assets which qualify only for partial annual redemption. These consist of housing for residential occupation by the taxpayer's employees and the furniture thereof, infrastructure in respect of residential areas developed for sale to the taxpayer's employees, a school, hospital, shop or similar amenity owned and operated by the taxpayer mainly for the use of his employees or any garage or carport for any motor vehicle, recreational buildings and facilities owned and operated by a taxpayer mainly for the use of its employees, any railway line or system having a similar function for the transport of minerals from a mine to the nearest public transport system or outlet and motor vehicles intended for the private or partly-private use of the taxpayer's employees. Expenditure on these assets is deemed to be payable in ten successive equal instalments, or in the case of motor vehicles, in five successive equal annual instalments.

Section 37 of the Income Tax Act

Section 37 of the Income Tax Act deals with the calculation of capital expenditure on the sale, transfer, lease or cession of mining property. For the purpose of this section, "mining property" is defined as being -

- (a) any land on which mining is carried on; or
- (b) any right to minerals (including any right to mine for minerals) and a lease or sub-lease of such a right.

According to section 37(1), whenever a taxpayer sells, transfers or cedes any mining property, and disposes of any assets as described above under section 36(11), as a consequence of a sale, transfer, lease or cession, it would be deemed that the person who is acquiring such assets has acquired it at a cost equal to the effective value of the assets on the effective date of the sale, transfer, lease or cession. Such costs will be deemed to be an expenditure incurred by the person during the period of assessment in which the sale, transfer, lease or cession had taken place as per the definition of "capital expenditure incurred" in section 36(11), referred to above.

It is therefore submitted that the person acquiring the capital assets will acquire the assets at a cost equal to the value that the assets hold on the date of the sale, transfer, lease or cession. The expense incurred by the taxpayer that will be deductible as per

section 36, will be deemed to have been incurred by the taxpayer on the date on which the taxpayer had entered into the sale, transfer, lease or cession.

Section 37(1A) states that if any consideration is given by the person who is acquiring the disposed capital assets (as discussed above), but the value of the capital assets acquired exceeds the consideration paid for it, the amount of the cost and expenditure in respect of such capital assets will be deemed for the purposes of this subsection to be the amount that bears the total amount paid (consideration) the same ratio as the effective value of the capital assets bear to the effective value that the capital assets held by the person that has disposed of it.

Subsection (2), then goes on to state that in accordance to paragraph (j) of the definition of “gross income” and section 36, when a taxpayer disposes of any capital assets as defined in subsection 37(1), it would be assumed that the taxpayer has disposed of such capital assets for a consideration that is equal in value to the costs of the person acquiring the capital assets as per subsections (1A) and (1). Furthermore, the consideration paid will be deemed to have been received by or to have accrued to the taxpayer on the effective date on which the agreement of sale, transfer, lease or cession had taken place.

Subsections 1(A) and (2) discuss the scenario where the taxpayer who is acquiring the capital assets receives such assets at a consideration which is less than the value of the acquired assets. These subsections hold that if the value of the assets acquired by the taxpayer exceed the consideration paid, the assets would be deemed to have been received by the person who has acquired it at a cost equal to the value of the assets as on the date of the sale, transfer, lease or cession.

3.3.5 Environmental Management Trust Fund

The Income Tax Act provides for a deduction of amounts paid by a taxpayer engaged in mining, prospecting, quarrying or similar operations to an organisation referred to in section 10(l)(cH). As such, section 10(1)(cH) exempts the receipts and accruals of mining rehabilitation funds or entities.

Section 37A of the Income Tax Act

Section 37A(1) of the Act allows a deduction in the determination of the taxable income of a taxpayer, carrying on a trade, of the amounts of cash paid to a company or trust:

(a) If the sole object of the company or trust is to apply its property solely for rehabilitation upon premature closure, decommissioning and final closure, and post closure coverage of any latent and residual environmental impacts on the area covered in terms of any permit, right, reservation or permission contemplated in the section to restore one or more areas to their 'natural or predetermined state', or to a land use which conforms to the 'generally accepted principle of sustainable development'.

(b) that company or trust holds assets solely for purposes contained in paragraph (a);

(c) that company or trust makes contributions solely for purposes contemplated in paragraph (a) or subsection (3) and (4).

(d) that person (i) holds a (aa) permit or right in respect of prospecting, exploration, mining or production or (bb) is engaged in prospecting, exploration, mining or production in terms of any permit, right, reservation or permission

The purpose of section 37A, ensure that mining operations in South Africa sets aside money for the purposes of rehabilitating the environment in which it operates when mining operations ceases to occur due to either premature closure, final closure, decommissioning as well as after the mine has already closed. All amounts paid over to the rehabilitation company or trust is exempt from tax if it complies with section 37A. This is provided as an incentive to ensure that mining operations do acquire some money to be used to rehabilitate the area in which the mine operated in to ensure that the environment is left in a state so that it is no longer harmful to the people living in close proximity to the area where the mining operations has taken place.

3.3.6 Mining Recoupments

In his presentation Diliza (2008) explains that where a mine has not been allowed a deduction in respect of expenditure, for example on land, the recovery or recoupment of this expenditure has no tax consequences.

Section 23B of the Income Tax Act however, stipulates that where the expenditure has been allowed in terms of the general deduction formula, or as a specific deduction in

terms of the capital redemption provisions, any receipt or accrual of an amount comprising a refund or recoupment in respect of such expenditure, must be added to current income by virtue of a special formula.

3.3.7 Tax levied on mines other than gold mines

Direct Tax Rates

Mines other than gold mines

Section 5(1)(d) of the Income Tax Act states that –

Subject to the provisions of the Fourth Schedule there shall be paid annually for the benefit of the National Revenue Fund, an income tax (in this Act referred to as the normal tax) in respect of the taxable income received by or accrued to or in favour of—

(d) any company during every financial year of such company.

Mining companies earning taxable income derived from mining for diamonds, and other minerals and base minerals are taxed on a standard corporate income tax rate of 28%. This rate is reviewed on an annual basis by the Minister of Finance and the National Treasury, and realised during the annual budget speech delivered during the first quarter of the year.

Secondary tax on companies is governed by sections 64B of the Income Tax Act. Secondary tax on companies was payable by South African resident companies at a rate of 10% on dividends declared on or before 31 March 2012. Secondary tax on companies was replaced with dividends tax on 1 April 2012 and is levied at a rate of 15% on dividends paid by a company.

In his presentation, Diliza (2008) describes that the Income Tax Act has a ring-fencing arrangement, whereby capital expenditure in relation to a mine is restricted to the taxable income of that mine and not to other mines owned by the same company. However, the Minister of Finance can rule that company costs can be offset against another mine; mining companies can then transfer up to 25 per cent of the capital exemption from unprofitable mines to offset income from profitable mines.

Indirect taxes levied on mines other than gold mines

- Value-Added Tax

Mining companies are liable to VAT on goods and services supplied to them, but in terms of section 11(2) of the Value-Added Tax Act, No. 89 of 1991, exports are zero-rated. This means that a mining company which exports all its products, for example, would not pay VAT on its exports sales, but would be entitled to a refund in respect of all input taxes paid by it.

- Royalties

The rate of royalties' payable by mines varies depending on the earnings before interest and taxation and gross sales. The rates for the mineral and petroleum resource royalties are determined according to a formula contemplated in subsections (1) and (2) of section 4 of the Mineral and Petroleum Resources Royalties Act, 2008 to differentiate between the refined and unrefined conditions of the resources, and are currently –

- for refined mineral resources: the minimum of 0.5% to a maximum of 5%
- for unrefined mineral resources: the minimum of 0.5% to a maximum of 7%

3.4 Conclusion

The Income Tax Act provides for the tax liability imposed on individuals and businesses. Annually, the tax rates applicable to all residents of South Africa are reviewed during the Budget Speech made by the Minister of Finance. The above taxes discussed are all the taxes mining companies are currently liable for, depending on the type of mining company it is and its profitability.

The tax model proposed in the *State Intervention in the Minerals Sector* (ANC:2012) plan, does not state that any of the above taxes discussed will fall away, or even decrease, it is proposed that extra taxes be introduced to companies earning their taxable income through mining activities.

The next chapter will discuss the proposed tax model as per *The State Intervention in the Minerals Sector Report* (ANC, 2012).

CHAPTER 4

DISCUSSION OF THE REPORT PREPARED FOR THE ANC ON THE STATE PARTICIPATION IN THE MINERALS SECTOR AND THE PROPOSED TAX MODEL TO BE IMPOSED

4.1 Introduction

According to a report by Grant Thornton (2011:1), “the mining sector faces an uncertain future. Increasing and unpredictable government intervention across the globe is adding further complexity to a sector that is already heavily laden with risk.”

The debate in South Africa on the nationalisation of its mining sector was largely spurred on by the African National Congress Youth League. The African National Congress Youth League drew up a document entitled “Towards the transfer of Mineral wealth to the ownership of the people as a whole: A Perspective on Nationalisation of Mines” (ANC Youth League, 2010: online), which was discussed at numerous events held by the League throughout the country.

It is submitted that due to the significant array of precious metals found in South Africa, and the revenues associated with mining operations, it is easy to understand why there is such a significant interest in the prospect of intervening in the minerals sector and to possibly share in the wealth this sector holds.

In *The State Intervention in the Minerals Sector Report* (ANC:2012), it was originally proposed that the Government take up a minimum 60% stake in all mining companies currently operating within South Africa. This, it was said, should be done via a State-owned mining company. The remaining 40% would then be owned by the private sector, and should still be subject to and compliant with the regulations set out in the Mining Charter and other legislation that governs the minerals sector.

To summarise, the aim of *The State Intervention in the Minerals Sector Report* (ANC:2012) is to explore the possible ways in which Government can intervene in the minerals sector. This is done by firstly looking at the possibility of Government taking full or shared ownership of the minerals sector, followed by looking at the different types of state intervention found in developed and developing countries worldwide. Lastly, *The State Intervention in the Minerals Sector Report* (ANC:2012) looks at the

goals Government wants to achieve (linkages) through the intervention, and the possible structures that would need to be put in place to achieve this.

4.2 Government's reason for the proposed intervention

According to *The State Intervention in the Minerals Sector Report* (ANC: 2012) the reasoning behind the idea of nationalising the mining sector was to ensure that all South Africans enjoy a greater benefit from the profits made by the mining companies. The reasons, according to the report are:

- greater control over one of the largest and most profitable sectors in South Africa;
- to enable the Government to generate additional revenue for the provision of basic services to all South Africans; and
- the alleviation of unemployment, through local beneficiation and the industrialisation of mineral resources by the Government.

The State Intervention in the Minerals Sector Report (ANC: 2012) goes on to say that South Africa is the most developed country on the African continent, but when compared with other developing countries around the world, it is still struggling with issues such as unemployment, crime, corruption and a poor educational system. These issues have prevented South Africa from developing its full potential and of moving forward in becoming a developed country.

In the process of developing the intervention proposal, numerous examples of countries where the Government has participated, as well as the method of participation, were examined. In the present research, focus will be placed on the following African countries identified in *The State Intervention in the Minerals Sector Report* (ANC: 2012) - South Africa, Botswana, Zambia, Ghana, Liberia and Sierra Leone.

4.3 The two major ways that mining activities impact negatively on South Africa's environment and people

It is submitted that various negative impacts are associated with mining operations. Due to the nature of and size mining operations usually comprise of, these affects

effect the environment and the people living in close proximity to the mining operations.

According to *The State Intervention in the Minerals Sector Report* (ANC: 2012) the two major negative impacts as identified that have affected South Africa the most are:

1. Water contamination

During the apartheid era, the mining industry failed to adequately prepare for the closure and the disposal of mine water and waste in ways that are consistent with current international best practice. The present government now faces conflict caused by the legacy of weak regulation that has exacerbated problems associated with limited natural resources. In particular, the problems of modified water tables, contaminated ground water sources, acidic mine drainage, and ground instability, that have resulted in cumulative harm to off-mine populations, must be addressed before they lead to even more devastating socioeconomic, political, and environmental damage. Clearly, the issue of water is critical to the mining industry and has direct linkages to the local communities that live in close proximity to mines. More importantly, both the legislation and the scarcity of water will pose constraints on new mines and possibly hinder the expansion of the minerals industry.

2. Local Economic Development

According to *The State Intervention in the Minerals Sector Report* (ANC: 2012), mining has a direct effect on the local mine communities as well as impacting on the related communities. Many mining ghost towns have been left behind in South Africa in the last century due to the country's mining activities. Very few of these towns have participated consistently in community upliftment programmes. In a mining charter impact assessment report conducted by the Department of Mineral Resources (Department of Mineral Resources: 2009), it was found that less than half of the mineral companies participated in designing Integrated Development Plans. In actual fact, proof only came from 37% of these. Only 14% included integrated development plans for their labour communities and there was minimal local economic development. Apart from underdeveloped communities, the mining industry in South Africa leads to almost inhumane living conditions for mainly the multitudes of workers. These inhumane living conditions contribute to the spread of HIV/AIDS, other diseases

and to drug and alcohol abuse as well as to the disintegration of family and social systems. The results of the mining charter impact assessment report (Department of Mineral Resources: 2009) also showed that only a quarter of the mining companies had provided houses for their employees, and only 34%, had helped them to take advantage of home ownership schemes. In addition, the report observes that, in terms of housing, the upgrading process is still “unsuitably low”. With regard to nutrition, only 29% of the mines were administering nutrition programmes for their employees, and, generally speaking, employees also did not have adequate facilities in which to prepare their own meals. Most mining companies give their employees “living out” allowances but these have generally led to increased formation of informal settlements further fostering crime, substance abuse and the spread of diseases.

Sustainable Development can be defined as: “development that meets the needs of the present without compromising the ability of future generations to meet their own needs.” (The Brundtland Commission: 1987).

It is therefore submitted that more should be done to ensure that the above mentioned impacts are properly addressed by mining operations.

In a discussion document on the strategic framework for implementing sustainable development in the South African minerals sector (Department of Minerals and Energy: 2007), it was said that the above definition can be regarded as a process of continually reaching for a dynamic balance between the people, the planet and prosperity through:

- the wise use and protection of the physical and natural environment and its resources, by ensuring current and future equitable and sustainable use of natural resources
- the creation of equitable and viable economic systems with an ethical basis by ensuring economic growth with greater equity and self-reliance; and
- the acknowledgment and guidance of social and cultural systems and values leading towards increased equity, responsibility and human welfare by improving the health, income and living conditions of the poor majority.

Mosetlhi, Managing Director of DARA Consulting (Pty) Ltd, wrote in an article (2013: Online), that the moral argument to be made is that mining houses should take an

active role in improving access to health care, education and that they should seek to address other socioeconomic issues due to the effect that their operations have on the communities directly abutting their operations. This argument goes beyond addressing these concerns to gaining regulatory approvals and increasing their profits. This will help mining houses increase their access to more qualified employees instead of importing management from abroad, and this will also reduce the stoppages that have been seen in the past that results in violent and deadly clashes between the mining companies and their employees.

It would appear that if mining houses ensured better basic needs for their employees, by attending to enhance their working and living conditions as well as their nutritional needs that this could lead to less frustration in the mining industry, which could possibly lead to less strikes and violent clashes between the two parties.

Furthermore, Mosetlhi (2013) goes on to say that after centuries of mining operations in South Africa, there is an urgent need for mining houses to play an active role in discussions with the relevant local authorities, non-governmental organisations, communities and employees, to collectively decide on what funds are going to be committed to address the needs of the communities. This alone will go a long way in changing the negative perceptions that are currently associated with the mining industry. Through open and honest dialogue between these stakeholders, the communities themselves will feel that they have been heard and understood, and also, they will be confident that emphasis will be placed on the value of preserving the land for their own sustainability.

Mosetlhi (2013) is of the opinion that the cause of many problems in mining communities is rooted in the deteriorating social conditions related to the lack of services, crime and ill-health. Other issues which must be urgently addressed by mining houses relate to housing and employment. Curiously, these issues are largely ignored in annual reports and corporate social responsibility reports. Mining companies should be more dedicated in addressing these two issues. For those mining houses engaged in corporate social responsibility there is a need to reduce the gap between the ever increasing needs of the community and their corporate social responsibility initiatives. With the move away from hostel dwelling to informal settlements around mines, mining companies need a more transparent and

sustainable housing policy. This may require a more collaborative approach to address the needs uniquely experienced in informal settlements.

It is submitted that active engagement between the mining houses, local government and representatives of the mine workers could help dissolve any issues that may arise quickly and in a manner that would avoid the issue escalating to a place where it can no longer be resolved through talks. Such engagement can also assist in generating ideas on how to enhance the work and living environments in a way that adds value to both the mining house and its employees.

According to the report by the Mining Intelligence Database (2013: Online), the mining sector has contributed substantially towards the economic development in South Africa as it boasts a total annual income exceeding R330 billion, and is one of the country's major employers.

As such a vital player in the economy, the mining industry more than any other, has the potential to substantially contribute to and impact the development of South Africa. This can be achieved by creating a more cooperative corporate social responsibility policy, to better meet the needs of the people living around the mines. Also, the industry can help to minimize the negative impact it has on the natural resources, and rehabilitate those local areas.

4.4 Proposal for the intervention of the State into the mineral sector of South Africa

As discussed above, according to *The State Intervention in the Minerals Sector Report* (ANC: 2012), the main reasons why the Government wants to intervene in the mineral sector are threefold:

Firstly, by means of a more aggressive taxation model imposed on the sector the State aims to generate a bigger sturdier flow of income into its own reserves.

Secondly, it also, together with mine unions, and the current Broad Based Black Economic Empowerment legislation, wants to gain more control over the sector, aiming to own a controlling 51% in certain mines.

Lastly, the aim of the intervention is to redistribute the wealth created from this sector more evenly so that all South Africans may benefit from the resource that is considered to belong to all South Africa's citizens.

The taxation model proposed by *The State Intervention in the Minerals Sector Report* (ANC: 2012) makes provision for additional taxes to be imposed on the mining industry. As such, mines will still be liable for taxes based on the current model at 28% per annum, but in terms of the new proposal would also pay additional taxes. According to *The State Intervention in the Minerals Sector Report* (ANC: 2012), these taxes collected through the new models will be utilised by the State for the benefit of South Africans through improving the infrastructure and living conditions of the people directly affected by the mining operations, to enhance the conservation of the environment and the well-being of all South African citizens.

4.5 The proposed taxation model

4.5.1 Income Tax

According to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 37), the mining sector will continue to pay the normal 28% income tax payable by corporate institutions. Every year, during the budget speech given by the Minister of Finance in conjunction with the South African Revenue Services, this percentage is established and can change due to several factors.

4.5.2 Capital Gains Tax

In order to prevent and discourage the speculation and prospecting of mineral rights, the State wants to impose an additional capital gains tax of 50% (ANC, 2012: 34). Should the mining rights of any mine, or potential mine, changes hands/owners before mining actually commences this tax will become payable. This will serve to encourage genuine mineral property developers rather than just speculators. Furthermore, all amendments or changes to any mineral right must be approved by the State.

4.5.3 Minerals Resource Rent Tax

According to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 36) the aim of creating the mineral resource rent tax is to ensure that all South Africans, as resource owners, are getting a fair share of those profits. Resource rent is the surplus

value, that is, the difference between the price at which a resource can be sold, and its extraction costs, including normal returns. As such, resource rents are exceptional profits embodied in the people's mineral asset and consequently should be shared between the mining company and the people.

In many of the models studied, resource rents are captured and taxed in the hands of the mining companies. The model proposed is based on some of the models used in various other countries such as Australia, for example.

Generally, resource rent is taxed at between 50% and 90% on the excess profits made by the mine. Minerals resource rent tax will only be applied once the investor/mine has made a reasonable profit. This ensures that the proposed minerals resource rent tax will not deter investors, particularly for marginal deposits or deposits with an average return.

4.5.4 Royalties Tax

The State Intervention in the Minerals Sector Report (ANC, 2012: 37) states that mineral royalties on production adds to costs and it also increases the cut-off grade and sterilises the people's mineral assets. Once the proposed mineral resource rent tax has been imposed, the State will consider reducing the mineral royalties' tax (as discussed in the previous chapter).

It is proposed that this royalties tax should reduce to 1% of revenue so as to enhance optimal resource extraction. However, the fiscal impact should be neutralised by compensating the fiscus with an equivalent value from the mineral resource rent tax.

The remaining royalties should be ring-fenced and used to:

- fund the Minerals Commission
- fund the rehabilitation of ownerless mines and to remedy historical damage
- invest in local sustainable economic development.

To summarise, the royalty tax levied on the production of mining operations will largely be put aside for rehabilitation purposes, and to ensure effective sustainable

development by focusing on the development of local communities situated near the mining operations.

4.5.5 Mineral foreign shareholding withholding tax

In *The State Intervention in the Minerals Sector Report* (ANC, 2012: 37), the State propose to introduce a “mineral foreign shareholding withholding tax” to encourage direct investment from their primary listing country, and if the foreign mining company is held in a “tax haven”, then the rate should be 30%. For those that are not, the normal rate of 10% should apply.

4.6 Proposal for the monitoring of the State intervention in the Minerals Sector

The objective of the State, according *The State Intervention in the Minerals Sector Report* (ANC, 2012: 27) is to maximise the developmental impact of the minerals industry through labour-absorbing growth and development, and amongst other things, to capture the resource rents, to invest in long term knowledge and physical infrastructure, and also to industrialise, diversify and to increase employment by maximising the mineral linkages.

To do this, the State needs to set the minerals industry at the heart of its National Development Strategy, as it is South Africa’s only natural resource sector that could be regarded as outstanding in global terms and is its strongest competitive advantage. The minerals sector must be harnessed in order to better build South Africa’s domestic economic potential, to realise its competitive strengths globally, and to overcome the vast unemployment problem. This requires that South Africa’s economic policy development and implementation be aligned to the actual structure of the economy. South Africa will need to have better coordination between the different government departments responsible for minerals, energy, industrial development and technology for the State to achieve this alignment successfully.

The State must ensure that sufficient and sustained long term investments are made in research and development, and other areas such as technical knowledge.

Finally, to enable the State to effectively and efficiently intervene in the minerals industry, it is proposed that better partnerships be created between the private and

public sectors. For these partnerships to excel, full transparency from both parties on what is expected will have to be established.

4.6.1 Section 25 of the South African Constitution

In terms of section 25 of the Bill of Rights, 108 of 1996, nationalisation of the mining companies, either for a public purpose or in the public interest is subject to compensation. However, according to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 28), it is estimated it would cost just under R1 trillion should the Government wish to acquire 100% of all the mining companies listed on the Johannesburg Stock Exchange. As this amount exceeds the entire Government budget, this renders the process impossible. Even should the Government wish to acquire 51% of all the listed mining companies, at R500 billion it would be unaffordable. That could cause the country to lose fiscal sovereignty and it would then have to follow the dictates of the Bretton Woods Institutions under a Structural Adjustment Programme which would be untenable. Information obtained from Wikipedia (Online) defines Bretton Woods Institutions as “the World Bank, and the International Monetary Fund”, while structural adjustment programs are defined as “consisting of loans provided by the International Monetary Fund and the World Bank to countries that experienced economic crises.”

4.6.2 Nationalisation without compensation

In *The State Intervention in the Minerals Sector Report* (ANC, 2012: 28), the Government also considered the option of obtaining majority shareholding in, or nationalising the South African mining sector without any compensation. To do this, aspects of the Bill of Rights would need to be changed but this would unquestionably result in a near collapse of foreign investment and access to finance. It would also incur widespread litigation by foreign investors domiciled in states with which South Africa has trade and investment agreements. To take this option would clearly be an economic disaster for South Africa and its people.

4.7 Proposed structures to be put in place

4.7.1 The creation of a State Minerals Company

The State Intervention in the Minerals Sector Report (ANC, 2012: 29) proposes the creation of State Minerals Companies. The State Minerals Company's Mandate would include, in partnership with other investors if necessary, the development of certain "strategic minerals", in order to supply them to the domestic market at competitive or utility prices. Furthermore, the State Minerals Company will hold the exploration rights to these "strategic minerals" through having first sight of all new state-financed geo-data. Together with broad based black economic empowerment enterprises, it would also be tasked with the development of other minerals, by taking a minority share and transferring skills. Finally, a major element of its mandate would be to facilitate mineral knowledge linkages by making appropriate investments into technical human resource development as well as research and development.

The State Intervention in the Minerals Sector Report (ANC, 2012: 29) further proposed that South Africa uses a combination of state and pension schemes to gain control over key mining companies, as is done in Finland and Brazil, for example. In fact, in various mining companies there already exists a combination of state and union holdings, but generally these union holdings are managed by private sector fund managers and this gives little scope for direct influence on the mining companies. Therefore, it is recommended that the unions together with the State pool their mineral holdings to create a special purpose vehicle that would exert a considerable influence on the mining companies, and which then could be used to maximise the economic linkages.

Furthermore, *The State Intervention in the Minerals Sector Report* (ANC, 2012: 29) suggested that a further advantage could be gained by the State also collaborating with the broad based black economic empowerment strategies in the mining sector. This could be facilitated by increasing the combined broad based black economic empowerment and State minimum holding to 30% of voting shares. Ultimately, the State holdings are owned by the people and arguably constitute the greatest broad based black economic empowerment holding possible. Accordingly, *The State*

Intervention in the Minerals Sector Report (ANC, 2012: 29) proposed to amend the Mining Charter to include State holdings in a new increased broad based black economic empowerment equity target of 30%. This will assist the black economic empowerment companies in realising extensive broad-based empowerment by maximising mineral economic linkages and creating job opportunities in and linked to the mining company concerned.

To conclude, by adjusting the Mining Charter to increase the broad base black economic empowerment holding and collaborating with pension schemes, the Government wants to increase its influencing power on mining companies to achieve the goals it has set out to achieve. It is submitted that by making use of this collaboration, mining companies would be forced into making certain strategic decisions, and as such mining companies could become reluctant to continue its operations within South Africa.

4.7.2 The governance of the mineral assets.

In *The State Intervention in the Minerals Sector Report* (ANC, 2012: 30) most of the research conducted into the State intervention models used in other countries, it was found that the majority have managed to realise their mineral resource economic linkages, and have consequently industrialised them, by combining the governance of minerals and industry.

According to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 29), one of South Africa's main challenges in terms of governance, is the lack of communication and coordination between the different departments due to the way the departments are currently set up. This lack of coordination and strategy alignment between such vital areas as the Departments of Mineral Resources and of Trade and Industry has probably been the main cause of the minimal progress in developing the forward and backward linkages and creating potential job opportunities within their spheres.

In the proposed intervention document prepared for the Government, it is suggested that minerals governance combine with industry governance to maximise the national industrial benefits and jobs arising from our mineral assets.

4.7.3 Creating a ‘Super Ministry’

According to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 29), in order for the State to maximise the resource linkages with the rest of the economy, a merger of various departments within the government should take place. Through this closer cooperation the Government will be able to better monitor and coordinate the management of the mining industry. This ‘super ministry’ will be comprised of the following departments:

- Ministry of Mineral Resources
- Ministry of Economic Development
- Ministry of Public Enterprises
- Ministry of Energy
- Ministry of Trade and Industry.

This merger will ensure better integration and communication between the different departments and the ultimate goal of this ‘super ministry’ would be to ensure that the Government’s needs are better met. By pooling all of the Government’s resources together, problems such as unemployment, education, and socioeconomic needs such as housing and sanitary infrastructure will be easier to tackle.

It is submitted that the creation of a super ministry could help by focusing on shared goals such as reducing unemployment, upgrading infrastructure and the fair trade and industry in the mining industry.

4.7.4 Establishing a professional “Minerals Commission”

According *The State Intervention in the Minerals Sector Report* (ANC, 2012: 32), up until now, the granting, monitoring and evaluation processes of the mineral licences have not been carried out in a way that maximises the development and employment objectives as originally planned. *The State Intervention in the Minerals Sector Report* (ANC: 2012) therefore suggests that a separate agency be created based on the model of the South Africa Revenue Services that falls under the Minister of Finance.

This commission will serve to ensure that all South Africans benefit from the exploration of the country's minerals as opposed to only a selected few.

The Minerals Commission would then also be responsible for regulating and administering the mineral rights within South Africa.

4.8 Outcomes which the State hopes to achieve

There are definite outcomes outlined in *The State Intervention in the Minerals Sector Report* (ANC, 2012: 44-47) which the intervention proposal aims to achieve. With the monies received through the different taxes, the Government aims to establish a Pilot Beneficiation Hub. It is recommended that two or three of these hubs need to be established in areas that struggle with severe unemployment and underdevelopment. Other developments that it aims to create are as follows:

- the creation of a 'Retrenchment Safety-Net fund' which will assist workers who have lost their jobs from within the mineral sector, by paying them a salary for a period of three years after their retrenchment. The salary paid out by the retrenchment safety-net fund is structured to depreciate from 90% of their pre-retrenchment salary the first year, to 80% and 70% in the second and third years respectively
- a "Re-Skilling Fund" will be established to aid retrenched employees in attaining a new set of skills that will assist them to find new employment through which they further contribute to the economy.
- Twelve-and-a-half percent of the money gained through the mineral resource rent tax will be used to invest in the development of technical capabilities necessary for the Mineral Energy Complex. The mineral energy complex will then further be responsible to use the money they receive towards education, in particular to increase the number of students taking mathematics and science as subjects up to grade 12 levels. Study loans will be granted more readily to students studying mathematical or scientific degrees, while financial assistance will also be provided to the engineering and science faculties at universities.

It is submitted that by focusing on the above set out goals, the Government would be addressing some of South Africa's biggest economic problems. By investing in the education and re-employment of retrenched employees, the Government hopes to

significantly reduce the unemployment rate of South Africa, and will also help increase the number of grade 12 students matriculating with maths and science as subjects. This will ensure that more matriculated students can enrol in engineering fields, which would ultimately benefit the mining industry as well.

4.8.1 The establishment of a “Sovereign Wealth Fund”

The State Intervention in the Minerals Sector Report (ANC, 2012: 38) suggests that the Government to use some of the money it will be receiving through the newly proposed tax system to invest in a sovereign wealth fund. This money will then be used to make off-shore international investments which will act as a buffer fund:

- stabilising the Rand in times of economic uncertainty
- developing infrastructure for Southern Africa; and
- exploring and developing new mineral resources.

4.8.2 Outcome of intervention

When analysing the information contained in *The State Intervention in the Minerals Sector Report* (ANC: 2012), it is noted that some of the major outcomes hoped to be achieved by having Government participation is the stimulation of the country's economy, the elimination of unemployment, sustainable development and to benefit the citizens of that country.

In all the countries and international surveys used in the case study mentioned in *The State Intervention in the Minerals Sector Report* (ANC: 2012), it was clearly indicated that resource-based industrialisation and job creation depends upon establishing the crucial mineral economic linkages. These include: Fiscal Linkages (resource rent capture); Backward Linkages (upstream mining supplier industries); Forward Linkages (downstream mineral beneficiation); Knowledge Linkages (sidestream mineral human resource development, and also research and development) and the Spatial Linkages (sidestream being collateral use of mineral infrastructure and local economic development).

The case studies conducted as part of its research in *The State Intervention in the Minerals Sector Report* (ANC: 2012) also show that countries that had succeeded at technical training and technology development, had also successfully utilised their

natural endowment for developmental purposes. This is a necessity for taking advantage of the other minerals economic linkage opportunities. The countries included Sweden, Finland, China, Malaysia, Australia, and more recently, Brazil and Chile, but they are still lagging well behind the Nordic countries. For a country to effectively use its mineral resources as drivers of development it needs to have adequate human and technology development, something with which South Africa is still struggling.

According to *The State Intervention in the Minerals Sector Report* (ANC, 2012: 9) global data on the success/failures of state mineral companies shows both widespread failures and successes. However, success does appear to correlate with the overall level of economic development of the country. Nevertheless, there are key issues that appear to be essential for profitable State mining companies worldwide:

- a clear distinction between the State as a regulator and an owner
- clear communication lines between the company and the owner
- the company should not form part of the Treasury
- absolute transparency
- clearly defined and transparent developmental goals; and
- listing as a State-owned company.

Over the past few years, with the surge in commodity prices, particularly in developing countries, there has been renewed interest and enthusiasm to increase State participation in the mining sector. However, the nature of the State participation will vary considerably by country and type of mineral concerned.

4.9 Conclusion

The State Intervention in the Minerals Sector Report (ANC: 2012) emerged as a resolution during the 3rd National General Council Resolution on Economic Transformation held in 2012. The National General Council mandated the National Executive Committee to ensure that further work be done on ways in which the African National Congress can implement economic transformation in sectors such as the mining sector. As a result of this research, *The State Intervention in the Minerals Sector Report* (ANC: 2012) emerged.

In *The State Intervention in the Minerals Sector Report* (ANC: 2012) the National Executive Committee looks at different state participation models used in countries across the world, which includes developing countries such as Zambia, Botswana, Ghana, Liberia and Sierra Leone; as well as developed countries such as Sweden, Canada, Norway and Denmark. The main purpose of *The State Intervention in the Minerals Sector Report* (ANC: 2012), is to compare the mineral sectors of developed as well as developing countries with each other in order to try and compare the different types of State intervention, the impact it has on the country, as well as the benefits each type of State intervention has on the country's economic development, its people and the contribution by the mineral sector to the country's gross domestic product.

For the purposes of the present research, the current South African tax model will be compared to the model proposed in *The State Intervention in the Minerals Sector Report* (ANC: 2012) as well as to the tax models used in the following African Countries – Zambia, Botswana, Ghana, Liberia and Sierra Leone.

In the document prepared by the Congress (Congress of South African Trade Unions: 2012) it states that what it had expected was an elaboration of the different models of State ownership and their pros and cons. The Congress (Congress of South African Trade Unions: 2012) further states that given this fact, the state intervention in the mineral sector report should have looked for ways in which the mining industry could have been reassigned to the ownership of the South African people, rather than aligning itself with the Minerals and Petroleum Resources Development Act.

It can therefore be concluded that the goal that Government wants to achieve by intervening in the minerals sector of South Africa, is to share in the mineral wealth associated with mining operations, and to use the revenue accumulated to better and enhance the quality of life for the people of South Africa. Aspects such as education at school level, the up-skilling of the current workforce operating in the mineral sector, and better living conditions for the people affected by mining operations are said to gain from the Government intervention in the minerals sector. Although the negative impacts associated with the mining operations are discussed, it is submitted that the report should have addressed the ways in which these impacts will be mitigated.

In the next chapter a discussion will be presented of the history of the mineral sectors, the demographics, and the role that the sectors have played in the development of Zambia, Botswana, Ghana, Liberia and Sierra Leone.

CHAPTER 5

STATE PARTICIPATION IN THE MINERAL SECTOR?

5.1 Introduction

In the World Bank Extractive Industries Source Book (Daniel, Keen, McPherson: 2010); the authors considers the phenomenon of State participation in the mineral sector. State participation is still a reality. Most of the world's mineral deposits and oil reserves are still managed by natural resource companies. In view of this, the Source Book (Daniel et al: 2010) considers the various models of State participation, the issues that have arisen and resulting policy responses.

It is submitted that State participation in the minerals sector is a worldwide phenomenon, and not exclusive to South Africa. There are both stories of success and failure when it comes to State participation in the minerals sector. The present research attempts to look at the tax model proposed in *The State intervention in the Minerals Sector Report* (ANC: 2012) in comparison with the tax models used in Zambia, Botswana, Ghana, Liberia and Sierra Leone. The Source Book (Daniel et al: 2010) is based on the fundamental premise that no one approach will best suit all countries. As such the Source Book (Daniel et al: 2010) is used as a guide to identify best practice and provides structures and possible ways in which Governments' can intervene in the minerals sector and be able to achieve its intended goals while working in partnership with the mining houses.

The information obtained in the Source Book (Daniel et al: 2010) is mainly intended for use by senior government officials, parliamentary decision makers, and also by assisting domestic and international technical specialists. However, the significance of participatory processes to facilitate sustainable development of gas, oil and mining indicates that the Source Book has also been designed to more effectively advise and equip members of international and national civil society groups, industry, communities and indigenous peoples on how to address Government participation in the minerals sector by highlighting certain aspects that needs to be considered when developing a Government participation model. These aspects will be discussed in this chapter.

It can therefore be concluded that making use of best practices as identified by the Source Book (Daniel et al: 2010), Governments can intervene in the minerals sector in a way that will promote collaboration between the Government and the mining houses to achieve the Governments goals without threatening the livelihood of the mining companies.

5.2 Forms of State participation

According to *The State intervention in the Minerals Sector Report* (ANC, 2012: 11),

state participation in mining, through outright ownership or share participation, either on a mandatory basis, or through the exercise of option rights, remains common practice.

It is noted that Governments' participating in the mineral sectors aim to achieve certain goals which may be non-economic (the protection of sovereignty and national interest) or commercial and fiscal (the maximisation of revenue from the natural resource sector).

It is observed that in attention to those objectives, state participation can take the following forms Daniel et al, 2010: Online) -

- *cull equity participation*, whereby a State carries out activity either through its natural resource company alone or by acquiring an interest in a joint business;
- *Carried equity participation* in which an natural resource company teams up with a private investor who advances the funds at the early stages of a project with a possibility of being or not being compensated for the funds'
- *'free' equity participation*, which is a simple grant of an equity interest directly to the State without any financial obligation or compensation to the private investor; or
- *production sharing*, an arrangement similar to 'free' equity participation in which the State gets an equity share income after cost recovery by the private investor without any offsetting financial obligation.

The State intervention in the Minerals Sector Report (ANC: 2012) notes that the nature of the State participation will vary considerably according to the country and mineral involved. This participation can be broadly defined as comprising different options ranging from 100% equity participation, through partial or carried equity arrangements, to equity participation with no financial obligation. Mineral resources have long been regarded as having special strategic significance. The State normally believes that it

should have strict control over the minerals sector as strategic minerals dominate the national economy. (McPherson: 2010, cited in the State intervention in the minerals report: 2012).

It is submitted that no one model of State participation will suit all countries, but that consideration must be given to aspects specific to that country before choosing a model to be imposed on the minerals sector. Issues such as the supply and demand of the minerals found in the country, costs associated with the extraction of the minerals, control structures currently in place and the ability of the Government to successfully implement and monitor a suitable State participation model are all aspects that will need to be considered.

Table 7 Forms of State participation

<p>Forms of state participation</p>
<p>Under all forms of state participation, except the “free” equity form, the most common vehicle for state participation is the state mineral company. In some countries, however, the state has exercised sector participation without the intermediation of a state mineral company.</p>
<p><u>Full equity participation</u></p> <p>In this model, the state could either</p> <ul style="list-style-type: none"> i) go ahead with investments on its own through its state mineral company, without private sector involvement; or ii) it could invest <i>pari passu</i> (literally on an equal footing or basis) with the private sector from the start of operations by acquiring either a majority or minority interest in an incorporated joint enterprise or a participation share in an unincorporated joint venture. In the latter case, the state has less than a 100% share but both spend and receive revenue in full proportion to the share each has. The best examples of the first option are found in Middle

Eastern oil-rich countries and Mexico. Examples of the second option can be found in both the petroleum and mining sectors, although joint enterprise participation is relatively more common in the mining sector while the unincorporated joint venture route is more typical of oil.

Carried equity participation

Carried equity participation may take several forms. The most frequent case is the “partial carry”, usually in the context of a state/private investor unincorporated joint venture. Under this approach, the private investor “carries” or pays the way of its state mineral company partner through the early stages of a project – exploration, appraisal, and possibly even development – after which, the state mineral company spends *pari passu* with the private investor, as under full equity participation. The private investor may or may not be compensated for the funds advanced on behalf of the state, and where compensation does occur, it may be with or without interest reflecting the time value of money, and/or “uplift” in recognition of the risks incurred on the state’s behalf. The ‘uplift’ is an agreed multiple of costs. Where recovery of interest on carried costs is explicitly allowed for, the uplift relates only to compensation for risk. Where interest cost recovery is not explicitly provided for, the uplift is expected to cover both interest and risk. A “full carry” occurs where all costs are borne by the private investor and compensation including interest and/or an uplift is paid out of the project itself.

“Free” equity participation

So-called “free” equity participation is a simple grant of an equity interest directly to the state without any financial obligation or compensation to the private investor. Once a feature in mining, where it was sometimes regarded as a payment for the right to exploit the mineral resource, and is still “on the books” in many countries, it is now found only rarely in new agreements (Ghana has it in both its petroleum and mining agreements.).

Production sharing

Production sharing is a popular form of state participation in oil prospecting or producing developing countries. Production sharing is similar to “free” equity participation in that it provides the state with an equity share income after cost recovery by the private investor, without any offsetting financial obligation. In contrast to “free” equity however, production sharing involves the state, represented by its state mineral company, actively in operations as a commercial party, a regulator and a fiscal agent. As the state representative, the state mineral company participates with private investors in the conduct of operations as it does under full and carried interest equity arrangements. At the same time, however, the state mineral company oversees those operations from a regulator’s point of view and takes responsibility for assessing, collecting and commercialising the production share due to the state and remitting proceeds to the state.

Source: McPherson, (2010)

McPherson (McPherson: 2010, cited in the State intervention in the minerals report: 2012) submits that the extent of State participation in South Africa, Zambia, Botswana, Ghana, Liberia and Sierra Leone can be summarised as follows:

Botswana

In the diamond mining sector of Botswana, the Botswana Government has a joint collaboration agreement in partnership with De Beers through the establishment of the Debswana Diamond Company. The participation on all other minerals is classified as “working or paying interest.”

Ghana

In Ghana the State participation found is classified as being 10% free equity participation by the State and 20% as production sharing between the State and the private investor.

Sierra Leone

In Sierra Leone the State participation found is classified as being 10% free equity participation by the State and 30% as production sharing between the State and the private investor.

South Africa

In South Africa State participation is 15% black ownership as specified in legislation.

Zambia

In Zambia State participation is different to other models used in Africa, as its participation is recognised as being a minority interest.

Liberia

In Liberia the State participation is classified as being 15% free equity participation, but for the mining of Mittal steel, the legislation specifies a 10% participation.

Table 8

Extent of state participation in mining in a sample of developing countries

Country	State participation	Country	State participation
Botswana	Diamonds negotiable WI other minerals	Mongolia	10% local/50% Govt.
Chile	100%-Owned SMC in copper	Namibia	Diamonds – negotiable. New SMC
DRC	5% F/negotiated e equity shares 15% -51%	Papua New Guinea	30%WI (not all mines)
Ghana	10% F /20% WI	Sierra Leone	10% F/30% WI
Guinea	15% F	South Africa	15% black ownership specified in legislation
Kyrgyz Rep.	Variable WI 15%-66%	Zambia	Minority interests
Liberia	15% F/Mittal only Law specifies 10%		

Source: McPherson, 2010. CI: carried interest; WI: working or paying interest; F: "free" equity.

5.3 Opportunities and Challenges

The Source Book (Daniel et al, 2010) goes on to state that resource wealth has the potential to deliver significant benefits for development. In developing countries, gas, oil and mineral resource wealth is widespread and often they account for a very high share of gross domestic product, government revenues and export earnings.

It is therefore submitted that State participation in the minerals sector holds substantial benefits for Government in being able to address national concerns such as unemployment, upgrading the quality of public education and improving the infrastructure and living conditions of people living in informal settlements.

5.3.1 Opportunities

The Source Book (Daniel et al, 2010) further states that wealth, on the scale experienced in resource-rich countries, both absolute and relative, can reasonably be expected to generate significant positive development outcomes. Even in those countries that have a more limited potential in their petroleum or mineral deposits, and so not strictly classified as “resource-rich”, the outcomes from development could be transformative.

The Source Book (Daniel et al, 2010) goes on to explain that revenues resulting directly from the exploitation of resource wealth often exceed official aid flows by a wide margin. This income can be used to meet a wide range of physical and social infrastructure priorities that are common in developing states. These would include areas such as health, education, transport, and telecommunications sectors. Increased, wise public expenditure of these resource revenues can foster both local employment and local ownership in economic activities, contributing to social and political stability as well as economic diversification, growth and security. In the mining sector, these include Ghana, Botswana, and South Africa as good examples of those countries that have used their resource wealth profitably. In both China and India, their access to large amounts of inexpensive energy through coal mining has facilitated their rapid pace of economic growth in recent years.

It is submitted that South Africa struggles with a very high unemployment rate, income inequality where the rich get richer and the poor poorer, and a high crime rate. It would therefore appear that if the Government appropriately use and manage the resource

wealth it would receive from participating in the minerals sector to address the issues discussed above, that South Africans could potentially benefit from State participation in the minerals sector.

5.3.2 Challenges

In the Source Book (Daniel et al, 2010), the authors hold that many observers have noted that ironically, all too often, development outcomes in the extractive industries are different and less beneficial than what had been anticipated. Typically, resource-rich developing countries underperform economically when compared to non-resource-rich peers. They score badly against critical human development indicators, they also experience environmental deterioration and they usually experience more than their fair share of violent conflict as well as social and political instability. Considering these circumstances, some have describe these outcomes as the “Resource Curse”

These negative results have also been attributed to a broad spectrum of both technical and political factors that characterise, and in some cases, are unique to the extractive industries. In chapter 2 of the Source Book (Daniel et al, 2010), the following challenges are listed:

Technical Factors

According to Source Book (Daniel et al, 2010); the three technical factors most commonly identified as contributing to the Resource Curse are: (1) the so-called 'Dutch Disease'; (2) revenue volatility; and (3) resource exhaustion.

- **Dutch Disease**

Dutch Disease (Daniel et al, 2010: Online) involves a significant appreciation of the resource-rich country’s real exchange rate and upward pressure on domestic prices due to a sudden and major inflow of foreign exchange connected with resource exports. As a consequence, non-resource exports lose their competitiveness, and domestic labour and capital shift to the resource and non-tradable sectors.

- **Revenue Volatility**

The volatility of petroleum and mineral prices and revenues is well documented. (Daniel et al, 2010: Online)

It should be noted that South African minerals such as platinum, copper and iron ore are all priced and traded in USDollars, as such the prices are volatile and sensitive to changes in the Rand Dollar exchange rate.

- **Exhaustibility**

Gas, oil, and mineral resources are by their nature exhaustible. This puts a responsibility on policy-makers to plan ahead for a situation of resource decline and the eventual cessation of commercial operations, even though the exact timing of the closure cannot be predicted. However, planning for the decline and eventual end to resource utilisation and associated earnings is a demanding exercise, rarely fulfilled in developing countries but also just as rarely found in developed countries. (Daniel et al, 2010: Online)

Mineral resources exhumed cannot be replaced. As such it is submitted that all minerals have a limit to the amount of resources available. High importance should be placed on the proper procedures regarding the extraction of minerals as well as the rehabilitation of mining sites.

- **Technical Factors**

According to the Source Book (Daniel et al, 2010) include political factors which includes situations where mineral wealth is used for political and personal gain by individuals in powerful positions. In such instances, the interest of the public takes a back seat to the interests of certain elites.

Other challenges

Other challenged highlighted by the Source Book (Daniel et al: 2010) include:

- Appropriation of public wealth, which relates to the challenge of ensuring that the wealth be distributed to the general public in a way that would enhance the quality of life for everyone in that country
- Guarantees of long-term stability, which means that government should provide some form of guarantee to foreign investors on how long term stability in the industry will be sustained
- Energy Conservation and Environmental Protection, relates to the plans Government has in place to help reduce emissions and other negative impacts that mining operations have on the environment.

5.4 Policy, Legal and Contractual Framework

The Source Book (Daniel et al: 2010) states that mining laws require that international resource companies adopt some degree of commitment towards supporting local goods and services. Aside from stakeholders such as local businesses, entrepreneurs and communities which would then benefit directly from access to capital, technology, productivity, diversity of markets and business opportunities, there are also wider benefits.

It is submitted that Government should ensure that international and local mining companies operating in South Africa should increase its commitment towards supporting the development of local communities. By doing this, mining companies will assist the Government in creating more employment opportunities and improving the skills of the current workforce. Other benefits include improving the growth in domestic and foreign investment, and transferring valuable knowledge from foreign companies to teach locals.

Chapter 5 of the Source Book, (Daniel et al: 2010) holds that extractive Industry contracts and licensing procedures tend to be extensive and complicated. They require specialised skills in their negotiation and in the handling and resolution of the almost inevitable disputes. Both topics are addressed below.

Negotiations

Negotiations in the extractive industry sector primarily focus on contracting between a government or its agent, and the investor. However, the introduction of new legislation and regulations, revisions to laws, or laws related to local content may also necessitate negotiation. Given the complexity of the issues involved and their significance in terms of revenue and other benefits, governments should place a high priority on the development of internal negotiation potential and access to informed external expertise. This is vital given the substantial information, skills, and resources generally available to the opposing negotiator. (Daniel et al, 2010: Online)

It would appear that the Government will need to make sure that it has the correct legal expertise, either internally or contracted externally to negotiate on its behalf with mining companies when it comes to the intervention structures as well as the

ownership and management functions of the company. Aspects such as the roles which the different stakeholders will play and the influence exercised will need to be addressed early on in the negotiations.

Disputes

Prior to the commencement of extractive industry operations, during contract negotiations, the parties will need to decide how to settle any conflicts that may arise during the long-term project. There are certain accepted ways of settling these disputes appropriately and timeously including mediation, conciliation, or cooling-off periods. Failing these, parties may choose to pursue more formal and binding legal proceedings. This may require the dispute to be heard by the local courts, but more often the parties will choose to submit their conflicts to international arbitration, to a neutral court. (Daniel et al, 2010: Online)

It is submitted that a formal dispute resolution agreement and policy should be put in place, according to which all disputes will be dealt with. By stipulating and documenting the process all parties are familiar with the process and how to deal with any disputes. Effective and speedy resolution of disputes will ensure that the parties to the contract can focus on more important issues, while being assured that the dispute resolution process is effective in resolving differences.

5.5 Institutional structures

In chapter 6 of the Source Book (Daniel et al: 2010), the authors go on to say that key institutions which share responsibility in extractive industry sector management, its impact on the economy, environment and society, are comprised of the following:

- legislative bodies;
- executive bodies;
- extractive industry sector ministries;
- regulatory agencies;
- national resource companies;
- finance ministry;
- taxation authority;
- the central bank;
- economic planning ministry; and
- the environmental ministry.

The differing roles and responsibilities of the various agencies need to be clearly defined and enforced in practice. Accurate definition of roles and responsibilities of these agencies is required so as to:

- avoid overlapping or conflicting roles; and
- prevent gaps in regulatory responsibility at the same time.

Although difficult to achieve, close coordination among all the listed agencies is essential to effective extractive industry sector management.

For each of these agencies, institutional capacity equivalent to the technical intricacies of the extractive industry sectors deserves primary attention. More often than not, requisite capacity is lacking. Therefore, the responsibilities and roles of these particular institutions are discussed and reviewed with an emphasis on capacity requirements. The role of each of the identified institutional bodies is discussed.

It would appear that in order for State participation in the minerals sector to be successful, certain structures need to be put in place to help with the implementation, management, regulation and supervision of the State participation plan.

5.5.1 Legislative Bodies

Although often neglected and hampered by weak institutional capacity and more powerful executive bodies, legislatures have the potential to play a significant role in effective management of the extractive industry sectors. Through their principal law-making function, legislatures are responsible for reviewing bills and enacting the legislation that is necessary to support the extractive industry sector.

Legislatures also assist in a supervisory role that allows them, and especially their committees, to:

- instil accountability through appraisal of extractive industry sector issues; and
- scrutinise government activities and the allotment of funds

Finally, in their representative role, legislatures can secure public participation in the political processes relating to the extractive industry sectors. (Daniel et al, 2010: Online)

It is submitted that proper legislation regarding describing the extent and way in which the State will participate is important. Legislation will also assist in ensuring that the

funds received by Government is apportioned and distributed through the right channels and for its intended purposes.

5.5.2 Executive Bodies

Typically, the presidency and executive cabinet, known as the executive, often reserves for itself the final decisions on critical extractive industry sector issues such as licensing rounds, state participation, and the establishment of extractive industry sector-related funds. (Daniel et al, 2010: Online)

It would appear that an executive committee consisting of the President of South Africa, and other executive consisting of ministers from critical departments should form a committee where final decisions regarding the issues related to the State participation can be resolved.

5.5.3 Regulatory Agency

According to the Source Book (Daniel et al, 2010: online),

the extractive industry sector ministry should be authorised and expected to designate regulatory functions to a subordinate and quasi-independent agency. Normally that agency would then report to the extractive industry sector ministry and have supervision of:

- the development of technical specifications and standards
- technical oversight of extractive industry sector operations
- oversight of company operations in accordance with contracts and legislation
- metering and monitoring of production, technical data analysis, and storage
- recording of licenses and ownership interests
- contributions to economic planning; and
- environmental and social protection in coordination with relevant authorities.

It is submitted that the regulatory agency should be separate from the ministry as to ensure its autonomy. The agency would be responsible for the day-to-day activities and management of the administrative duties concerning the collection, storage, and analysis of the mineral sector data, samples, and the preparation and safe keeping of records on the mining rights and agreements in place.

5.5.4 National Resource Companies

National resource companies play an influential, and sometimes controversial, role in extractive industry sector management in many states. Normally, they are accountable for commercial operations and the development of a shared national capacity in the extractive industry sector. (Daniel et al, 2010: Online)

It would appear that National Resource Companies act as consultants to the mineral industry as well as the Government. As such, National Resource Companies consist of individuals with extensive knowledge on the minerals sector, ranging from legislation, extraction of the minerals, safety on the mines and environmental issues.

5.5.5 Finance Ministry

In almost all states there are certain tasks that fall exclusively within the traditional competence of a ministry of finance. These usually include:

- tax policy and the proposal of tax legislation
- resource revenue forecasting
- revenue management; and
- expenditures or budget allocations.

Taxation Authority

In most states, there is an income authority that is responsible for assessing and collecting taxes and for undertaking tax audits. Similarly, most states also have a customs authority that is responsible for import duties. With regard to petroleum and mining taxation, the finance ministry is responsible for tax policy and for proposing tax legislation. All extractive industry sector ministries and authorities must have strong extractive industry sector expertise to do their work efficiently and effectively. (Daniel et al, 2010: Online)

Within South Africa the South African Revenue Services is responsible for collecting the taxes. It would appear that in order for State participation to be effective, close cooperation between the South African Revenue Services and extractive industry sector ministries would be required, as the South African Revenue Services would need to depend upon an accurate understanding of the minerals sector to be provided by the ministry.

5.5.7 Central Bank

The central bank of a resource-rich state plays a pivotal role in the tracking, reporting, and reconciling of fiscal and financial flows in the extractive industry sector despite not being expected to play a proactive role in its management. Central banks in these states are also likely to play a significant role in setting monetary and exchange rate policies. Their major role relates to requirements for repatriation of funds by extractive industry sector investors. The central bank, too, will often determine policy concerning the percentage of export revenues that must be brought onshore and the percentage that may remain offshore. (Daniel et al, 2010: Online)

It is submitted that within the South African context, this role is already fulfilled by the South African Reserve Bank. The South African Reserve Bank is responsible for tracking, reporting and reconciling the flow of funds within South Africa. It also controls exchange rate policies and regulates exports and imports to South Africa.

5.5.8 Economic Planning Ministry

Especially in states where economic dependence on the extractive industry sectors is high, their performance becomes critically important to overall macroeconomic planning. (Daniel et al, 2010: Online)

It is submitted that the mining industry within South Africa contributed greatly to its economy, as such, it would be necessary to ensure that proper planning and management of the sector be put in place.

5.5.9 Environment Ministry

Mining activities are often associated with considerable environmental and social “footprints”. Good practice would recommend that addressing the issues arising from those footprints, although the responsibility of the extractive industry sector ministry should go to specialised ministries. The environment ministry and ministries dealing with labour and local community matters would be ideal. It is also recommended that a small unit be established within the extractive industry sector ministry to coordinate with the specialised environmental and social issue ministries. (Daniel et al, 2010: Online)

It would appear that the existence of an environmental ministry would be vital in South Africa. Acid water contaminating the fresh water supplies especially in rural areas where people as well as livestock are dependent on sometimes only local rivers are

the most at risk. Other environmental concerns include harmful gasses released in the air.

5.6 Taxation design and Administration

In Chapter 7 of the Source Book (Daniel et al: 2010), the authors state that the efficiency of an extractive industry sector fiscal regime depends on the goals established for that regime, on the fiscal instruments selected to attain those goals, and on the calibre of fiscal administration. Both the design and application of extractive industry sector fiscal regimes are complicated, requiring suitable skill.

Mining specifics

Tax design and administration specifically focusing on the mining sector are explained as follows (Daniel et al, 2010: Online) -

- Despite the fact that so many are currently regressive, it is recommended that fiscal mining regimes should be progressive, that is, that the proportion of income accruing to the State treasury should increase with greater profitability, rather than decline. With this system, Governments participate more in the benefits of mineral booms; the disadvantage is a lesser share of reduced income during downturns.
- Recommended fiscally progressive 'Additional Taxation' instruments include: variable income tax linked to profitability currently law in South Africa, Uganda, Botswana and Zambia; and rate of return, or Resource Rent Tax, currently law in Liberia, Malawi, and Zimbabwe. This involves calculating the internal rate of return of a project and then increasing the marginal tax rate during times when a pre-determined 'hurdle' rate of return is exceeded.
- Inter-affiliate agreements can be used to move profit from one associate to another thereby reducing the tax liabilities of the mining company in the host country. The most common inter-affiliate transactions are product sales from one associate to another, but there are many other kinds of transactions including sales of goods and services, and provision of short- and long-term financing. Monitoring and policing inter-affiliate agreements can be an extremely arduous task. Good practice recommends that the tax authority sets clear rules and procedures for the taxing of inter-affiliate transactions and to properly monitor these. Mining companies typically will 'game' tax holidays by distorting production decisions and reducing State revenues; this must be avoided.

- Good practice recommends that the mining tax regime is in the law and regulations and is not modified in separate contracts, especially if they are kept confidential.
- States should be wary of falling foul of gamed-scenarios particularly where influential subsidiary companies use excessive debt to reduce tax assessments even though their parent firms maintain sensible debt levels. To prevent this, Governments may limit the amount of interest payments or debt that qualifies for tax deduction purposes.
- States should be wary of the tax avoidance practice of 'Treaty Shopping'. This occurs in situations where tax treaties are not in place to prevent double taxation, and where a parent company owning a subsidiary firm operating in the territory of a host country government, establishes an intermediary 'paper' company in a tax haven as a tax avoidance strategy. Effective and enforced State legislation to both prohibit and penalise this should be in place.
- Tax administration involves auditing tax returns, assessing and collecting taxes. Taxation instruments generally fall into two categories, either administratively uncomplicated but regressive, that is, a royalty per unit, or administratively more complicated but progressive, that is with a Resource Rent Tax or Sliding Scale Royalty. Good practice recommends that there exists the administrative capacity to execute more complex tax regimes.
- Good practice recommends that the tax authority undertakes field tax audits of mining enterprises, led by experienced and qualified staff, to obstruct the chance of fraud.
- Mining involves various tasks including exploration and mine development work, overburden removal, reclamation and restoration, all of which are not experienced in other businesses and for which the accounting treatment may have particular ramifications for tax assessments. Therefore, good practice recommends that the Tax Authority agrees on a detailed accounting treatment for mining companies with regard to these and other mining-related activities.
- The appeal of tax-free export processing zones for Governments is their potential to stimulate expansion in local employment and exports.
- However, such an approach is unsuitable for mineral or metal processing since the process is capital intensive rather than labour intensive and offers relatively little increase in employment; also, the processing will in any event take place as it saves the costs of transporting lower grade materials, and the metal itself definitely will be exported meaning that there will be little in the way of incremental exports.

It is submitted that South Africa has adopted a progressive tax system, which is based on the principle that the more a person earns the higher percentage tax they pay. This however is only applicable to natural persons and not companies. It would therefore be submitted that perhaps having a similar tax system in place in the minerals sector would stand to be beneficial. Resource rent tax as discussed earlier is a possible tax model that would impose additional taxes on profitable mines. Where the mining company is a foreign company, South Africa has double tax agreements in place, in terms of which, the profits made by a foreign company will be taxed in South Africa if the foreign company carries on a business in South Africa through a “permanent establishment.”

5.7 Revenue Management and Distribution

The Source Book (Daniel et al: 2010) goes on to state that once extractive industry revenues have been generated and collected, Government must decide on their management and allocation. Options include either spending or saving, with decisions required on suitable avenues or structures for each. The changeability of resource revenues presents a unique challenge, dealt with in many countries through resource funds. Sharing of resource revenues among levels of Government and regions is increasingly common and needs careful balancing of pros and cons.

It would appear that in South Africa, the revenues collected through State participation will be used to address the pending economic problems facing the country. Revenues should be used firstly for upgrading the standards of the public education sector, to ensure the quality of schooling available to all South Africans, this will include school infrastructure, supplies and a higher level of knowledgeable teachers. Addressing unemployment and the public health care system in South Africa should also be priority.

Failure to manage and distribute the wealth arising from gas, oil and mining operations can lead to increasing social and economic inequalities, the support of corrupt practices and the engendering of intra-state or even inter-state conflicts. Transparency has been identified as a cross-cutting topic and is critical to achieving success in these areas.

5.8 Conclusion

The World Bank Extractive Industries Source Book (Daniel et al: 2010) investigates the phenomenon of State participation in the mining industry. Especially in mineral-rich developing countries where the government wants to share in the wealth created by the minerals exhumed as well as the associated benefits created by the mineral industry, State participation is a common practice.

The Source Book (Daniel et al: 2010) proposes a more proactive approach ensuring that governments look at all the different models of State participation as well as the opportunities and challenges that occur in participating together with the private sector in the minerals industry. It further suggests certain institutional structures to be established to ensure the proper administration and allocation of resources and responsibilities within the Government. This will maximise the impact and benefits for the host country, and ensure that the influence the mining industry has on the environment, economy and society is managed properly to guarantee that the country benefits from it, and that the minerals sector is managed in a sustainable manner, and recommends that changes be made to the fiscal policy of host countries to make sure that it is beneficial and able to reach its goals. It is also important that the wealth generated by the mineral sector be governed in a way that will benefit everyone and also contributes positively in reducing the economic inequalities that may exist in the country.

It can be concluded that there are numerous benefits associated with State participation in the minerals sector of a country. Sharing in the mineral wealth can help Governments enhance the quality of living standards for its citizens through improving education, creating job opportunities and bettering the countries' infrastructure. It should however be noted that in order for State participation to be successful and to be sustainable, certain legislative structures and legislative bodies would need to be put in place. Furthermore, the effective management of the mineral wealth needs to be managed properly to ensure that the funds are used for its indented purpose.

The next chapter will look at a comparison between South Africa, Zambia, Botswana, Ghana, Liberia and Sierra Leone in terms of history and macroeconomics.

CHAPTER 6

COUNTRY COMPARISONS: ZAMBIA, BOTSWANA, GHANA, LIBERIA AND SIERRA LEONE

6.1 Introduction

The goal of this thesis is to compare the proposed tax model for the minerals sector, as suggested in *The State Intervention in the Mineral Sector Report* (ANC: 2012), with the tax models imposed in other developing African countries to determine if they are similar, and to investigate how the proposed tax model differs from the current taxes imposed on the South African minerals sector.

The countries used in this comparison are some of those used in *The State Intervention in the Mineral Sector Report* (ANC: 2012), namely, Zambia, Botswana, Ghana, Liberia and Sierra Leone. These countries were identified in this report as benchmark examples of those countries where State participation is visible, albeit to varying extents, and their use of different tax models.

To determine whether this State participation in the minerals sector in these countries can be applied in South Africa or compared to the model proposed in *The State Intervention in the Mineral Sector Report* (ANC: 2012), it is necessary to establish their comparability.

In this chapter the history of the mining sectors, the macroeconomic indicators, as well as the form of State participation currently in force in Zambia, Botswana, Ghana, Liberia and Sierra Leone will be discussed to determine whether it is similar to or different from South Africa.

6.2 History of the mining sectors

Zambia

According to the article on the privatisation of mines in Zambia (Chamber of Mines of Zambia: 2007), private investors started mining zinc and lead in 1904 in the Central Province at Broken Hill, now Kabwe. Zambia's first commercial copper was produced in the North West Province at Kansanshi in 1908 and from Roan Antelope Mine in 1911 and the first concentrate was produced at Bwana Mkubwa in 1913. Over the

years, it spread to other places on the Copperbelt and the North Western Province. However, in 1964 following the country's attainment of independence, a socialist type of political governance system was adopted, as was the trend then for most of the newly independent African states. Zambia adopted a public sector led economic philosophy as a way to accelerate economic growth and to also promote local ownership, of which the mining sector was no exception. In 1972 the sector was nationalised and subsequently in 1982 all mining activities were vested into one parastatal conglomerate known as the Zambia Consolidated Copper Mines Limited.

According to the article (Chamber of Mines of Zambia: 2007), during the period of nationalisation from 1973 to 1997, the mining sector was characterised by significant declines in several performance areas such as metal production volume, profit margins, sales receipts, and productivity, among others. This resulted in a severe contraction in the economy as a whole, as well as the sector share of the national gross domestic product. The situation was exacerbated by the marginal dedication to exploration activities as indicated by the fact that no new mines were being established during that time. Several factors, both endogenous and exogenous to Zambia, were widely thought to have been responsible for the situation. As oil plays a significant role in the copper production process, the rise in its price on the international market and the drastic fall in the price of copper significantly reduced profit margins. Furthermore, the management of the mines opted to primarily meet the social responsibilities of the State rather than the mining business objectives, which further exacerbated the poor performance of the mines. The result was the deterioration in the value of the mining assets which required substantial capital investment, and this could not be managed within the prevailing arrangement. As a result of this trend and the declining general living standards of the Zambian people, the Government decided by 1989 to return to a private sector driven economy and so liberalisation and privatisation of mining activities was initiated. The privatisation of the mining industry was completed in March 2000.

The article (Chamber of Mines of Zambia: 2007) goes further to explain that in an effort to attract investments into the mining sector, Government approved a new Mines and Minerals Act in 1995. This new Act specifically detailed development agreements. These contracts, which the Government signed with the new mining investors, were intended to protect both the Zambian people and the new investors. The State was

committed to offering stability periods while, on the other hand, the new investors committed themselves to bringing the much needed foreign direct investment into the country to revitalise the mining industry. Since the completion of the privatisation process, new mine owners have invested approximately US\$2.1 billion in plant expansions and rehabilitations, while the production of copper in Zambia has also increased. Apart from its contribution to Government revenue, the mining industry has provided economic growth, employment creation and poverty reduction through advancing private sector development. The creation of employment and direct initiatives through social responsibility activities to the vulnerable households in the community has seen a dramatic rise in the living standards of the average Zambian. Skills training programmes are established to improve the employment rate of the local population.

Botswana

In his article, Cann (2008: Online), a reporter for Infomine.com, notes that Botswana has been an established mining province for close to 40 years. Botswana is a haven for foreign investment, in contrast to many of the war-torn and politically fragile countries elsewhere in Africa. Botswana is most famous for its diamond industry, which is dominated by De Beers, the South African diamond giant, in partnership with the Botswana Government.

According to a report on Botswana's mineral investment promotion (Botswana Chamber of Mines: 2008), exploration of the country's mineral resources has been a key factor for the country since Botswana's independence in 1966. Since then, mining in Botswana has steadily overtaken the agricultural industry in its contribution to the nation's gross domestic product.

Cann (2008) continues that De Beers began exploring for diamonds in Botswana in 1955, at a time when the country's economy survived on agriculture. The Orapa pipe, which is currently the second largest pipe in the world with a surface diameter of 262 acres, was discovered in 1967, a year after Botswana's independence, and a year after that, two smaller pipes were found 40km away from Letlhakane. The Jwaneng discovery followed in 1972, one year after the Orapa mine was commissioned, and four years later in 1975, the Letlhakane mine was commissioned. De Beers agreed to build the Jwaneng mine in 1987 in partnership with the Botswana Government. At this

time Debswana, a separate entity, was established by De Beers and the Government with equal ownership and it holds the diamond mining rights of the nation. This agreement ensures that De Beers and the Botswana Government work together as a strategic partnership in the exploration, manufacturing process and trading of diamonds.

In an article from the Natural Resource Charter (2010: Online) a global initiative designed to help governments and societies effectively harness the opportunities created by natural resources, the success of the initial negotiations and subsequent development of the partnership has been due to two key factors:

- Botswana has maintained a Government legitimised by democracy and highly rated for its honesty and transparency, allowing commercial negotiations to proceed with public confidence
- both parties recognised that other options could have had a far worse outcome with the structure of the diamond industry particularly being radically different had nearly half of Botswana's supply of the Diamond Trading Company's sales not been marketed via that organisation

As a result of the Debswana Diamond Company, this joint effort and collaboration between De Beers and the Botswana Government, has seen diamond mining produce 70% of the country's export earnings.

The report on Botswana's mineral investment promotion (Botswana Chamber of Mines: 2008) states that the Botswana Government's main objective for the minerals sector is to continue to get the maximum economic benefits from the sector for the nation, while also enabling private investors to earn competitive returns. Government policy encourages prospecting and new mine development, and it encourages opportunities for linkages to the rest of the economy to increase value-added activities, especially through the downstream processing of minerals, where this is commercially viable.

This report (Botswana Chamber of Mines: 2008) further states that the Mines and Mineral Act of 1999 is a modern mining law which compares favourably with some of the better mineral legislation around the world. All mineral rights in Botswana are owned by the state and their Minister of Minerals, Energy and Water Resources

ensures that the mineral resources of the Republic are investigated and exploited in the most efficient, beneficial and timeous manner so as to meet the public interest. To do this correctly, the minister needs to ensure that the rule of law prevails and that investors are fairly treated through the development and implementation of the fiscal and legal policy framework for mineral development, which aims to make Botswana's mining industry more competitive and attractive to investors.

According to the Botswana's mineral investment promotion report (Botswana Chamber of Mines, 2008: 3), the major highlights in the new Mines and Minerals Act of 1999 of Botswana are as follows:

- the abolition of the government's right to a 15% free equity participation in all new mining projects was replaced by an option to acquire up to a 15% working interest participation in proposed mines on mutually-agreed commercial terms. The Government is obligated in the same manner as other shareholders to contribute working interest
- a downward revision of royalty rates payable on the sale of all minerals or mineral products from 5% to 3% except for on precious stones and precious metals, which will remain at 10% and 5% respectively
- the introduction of a new variable rate income tax formula that is applicable to all non-diamond mining operations. However, diamond being a strategic mineral to the economy of Botswana, determines that diamond mining licences are negotiated, in good faith, between Government and the applicant covering all technical, financial and commercial aspects of the proposed project including Government participation
- the grant, renewal and transfer of mineral licences have been simplified, to make the process more predictable and transparent, thereby improving the security of tenure of mineral concessions holders in Botswana
- restrictions on the transfer of mineral concessions have been liberalised
- the introduction of a new type of mineral concession, the retention licence, allows an investor that has completed an exploration programme and confirmed the discovery of a mineral deposit to retain rights over it for renewable periods, should prevailing market conditions make immediate exploration of the deposit economically unviable.

Although Botswana's mining industry is largely focused on mining for diamonds, other minerals mined in Botswana include: gold, nickel, copper, coal and soda ash. These

minerals are traditionally mined, and produce only a fraction of the total revenue from mining in Botswana.

Ghana

In the article by author Kwei Quartey (2013) on the legal and illegal mining in Ghana, the author states that until Ghana became independent in 1957 and assumed its modern name, it was called the Gold Coast. Europeans in the fifteenth century knew the West African coastal area as the source of the gold that reached North Africa via the trans-Saharan trade routes. For centuries, gold was panned and mined from the quartz reefs of Ashanti by local gold seekers called “galamsey”. In the 1870s, Marie Joseph Bonnat, a Frenchman who died in 1882, exploited gold concessions on the Ankobra River, but it was only toward the end of the nineteenth century that the concept of systematic and extensive mining began to gain strength. By 1890, three Ghanaian entrepreneurs, Messrs Biney, Ellis and Brown, had founded the Ashanti Goldfields Corporation. In November 1897 about 44 tons of heavy mining machinery arrived at Cape Coast Castle, a large commercial fort in Ghana built by European traders. Using labourers to carry the parts through dense forests and across powerful rivers, the company transported all the equipment from the coast to begin work in the Obuasi district some 120 miles north.

Quartey (2013) goes on to state that in 1896, after the overthrow of the Ashanti King, the Ashanti peoples came directly under British control, and the London-based firm Smith & Cade was authorised to mine the region for gold. From March 1898 to June 1899, 3426 tons of ore yielded 2544 ounces of gold. During the 1900 uprising led by the Ashanti Queen Mother against the British, these gold mining operations came to an abrupt halt. By 1904-5, there was great dismay in Ghana over the declining gold reserves. After the Second World War, many Ashanti gold mines had closed down and the industry was in a state of collapse. By then, Sir Edward Spears who lived abroad and rarely visited the company’s operations, headed up the Ashanti Gold Company. From 1966 when Dr Kwame Nkrumah was overthrown by the military until the 1982 regime of Flight Lieutenant Jerry Rawlings, Spears was deposed from his position by the London and Rhodesia Mining and Land Company. During Rawlings’s rule, the Ashanti Gold Company began to recover, and Sam Jonah, the new managing director and first Ghanaian chief executive, oversaw a radical improvement that began

in 1986. The Ashanti Gold Company's most productive mine is Obuasi, which is still one of the best-performing mines in the world and the largest mine in Africa outside of South Africa, despite over 100 years of continuous operation. More than a century after its constitution, Ashanti Gold Company Limited of Accra remains one of the largest producers of gold in the world, achieving an annual production of 1.74 million ounces in 2000. It is also one of Ghana's most successful earners of foreign revenue. In 2004, AngloGold Ashanti Limited was formed by the merger of Anglo Gold and the Ashanti Goldfields Corporation and is a global gold mining company.

"For more than a decade, southern Ghana has been one of the world's most prolific regions in terms of gold discoveries and production growth" (Perseus Mining Limited, 2014: Online). From 2005 to 2012, approximately 20 new mines opened in West Africa, making it an exceptional gold-producing region.

In an article by assistant-editor for Mining.com, Ana Komnenic (Mining.com, 2014: Online), she states that Africa's second largest gold producer, Ghana, has seen a large reduction in gold production. Ghana's output of the precious metal declined by 18% during the third quarter of 2013, as weak prices forced some miners to cut production and costs. As the gold price has dropped by an average of 28% last year, many mining companies have had to cut back. Newmont Mining, a major gold producer employing about 2500 people in Ghana, announced in mid-2013 that it would lay off 300 employees as a result of streamlining procedures. Similarly, in December 2013, Ashanti Gold announced that it would retrench more than 400 workers from its Obuasi mine.

Liberia

According to the investor-focused website (Africanmining.com: 2014) that has profiles of over 500 mining companies and countries in Africa, Liberia, is a small country and in its 161 years of existence as a republic, is the only country in Sub-Saharan Africa never to have known colonial rule. Historically Liberia has been a stable and productive democracy. The country is rich in natural resources such as gold, diamonds, iron ore and bauxite which are highly forthcoming and are currently underexplored. From 2012 to 2014 a strategic two-year work plan was devised for incentivising the Extractive Industries Transparency Initiative in Liberia. The Extractive Industries Transparency website (EITI.Org: 2014) reports that Liberia is rich in iron

ore, diamonds, gold, timber and rubber. All of these industries suffered seriously during the civil war that ended in 2003. During the fourteen years of war, all major mines were shut down and the mineral sector's contribution to the economy became virtually non-existent.

According to a United States Geographical Survey conducted by Yadira Soto-Viruet (2012), Liberia made significant progress in 2010 in reviving the mining industry. Before 1990 the sector had contributed more than 65% of the country's export earnings and represented about 25% of the country's gross domestic product. In 2010 the contribution of the mining industry was 0.9%.

The survey (Yadira Soto-Viruet: 2012) carries on to state that government continued to vigorously seek investment in the redevelopment of the country's extensive iron ore deposits. A campaign to upgrade mining-related infrastructure included the joint venture of Severstal Resources (a division of OAO Severstal) of Russia and African Aura Mining Inc. of Canada to develop the Putu iron ore project in Grand Gedeh Country, the Luxembourg-based ArcelorMittal to develop the western iron ore deposits in Nimba country, and the Israel-based Elenilto Minerals & Mining Ltd to develop the Western Cluster Iron Ore projects. In 2010, the Government also signed mineral development contracts with private companies to develop and operate gold and diamond mines.

The Extractive Industries Transparency Initiative (Africanmining.com: 2014) further states that the mineral commodities produced included diamond, gold and cement. Liberia's undeveloped mineral assets included base metals, such as manganese, lead, cobalt, nickel and tin. The agricultural sector continues to be the principal sponsor of the country's growth followed by the services sector. The mining industry's assistance to growth has tripled from 3.7% in 2011 to 10.4% in 2012, due to the increase in iron ore production.

Africanmining.com (2014) further states that the chief position of iron ore mining in the economy has largely obscured the value of other potential mineral assets, particularly in the fields of diamond, gold, and manganese, to name but a few.

Sierra Leone

In his article, author Eric Johnson (2002), states that the history of diamond mining began in Sierra Leone in 1935 when De Beers legally took total control of the mining prospects in the country for the next 99 years. Despite De Beers' presence, Lebanese merchants within Sierra Leone soon discovered the enormous profits that could be made by smuggling diamonds out of the country. As a result, illegal mining and trading quickly grew throughout Sierra Leone. By the 1950s the Sierra Leone Government had all but abandoned policing most of its diamond industry. All foreign investors were required to provide their own security guards for both the mines and their staff. However, the Government also increased their security measures, in that they strengthened their presence in the Kono diamond district and also in Freetown at the diamond export centre. This resulted in illegitimate diamonds being redirected away from the high security sites and taken to Liberia. Thus, an illegal diamond pipeline was born between Sierra Leone and Liberia. The government unwittingly took further measures to swell illegal mining by introducing the Alluvial Mining Scheme in 1956. This scheme allowed local miners to receive mining and trading licenses and the tally of illegal miners increased by more than 75 000 people.

Johnson (2002) continues by explaining that Sierra Leone gained independence from Great Britain in 1961. After gaining independence diamond smuggling became a political issue as well as an economic one. Populist Siaka Stevens became prime minister in 1968, bringing the country to a one-party rule. Stevens was the first person who officially connected political power and profit to the diamond mines and he fostered illegal mining to gain political ascendancy. He nationalised the diamond mines and De Beers Sierra Leone Selection Trust by creating the National Diamond Mining Company. Through this company, Stevens gave himself and his principal right hand man, Lebanese businessman Jamil Mohammed, total command of the diamond mines. Under Stevens' jurisdiction, the legal diamond trade dropped from more than two million carats in 1970 to 595 000 carats in 1980 and only 48 000 carats in 1988. At the end of Stevens' seventeen year rule, De Beers withdrew from Sierra Leone. The company sold its remaining shares to the Precious Metals Mining Company controlled by Mohammed in 1984. A year later, Stevens retired and Joseph Momoh, his successor, took control of Sierra Leone. With few political or leadership skills, he gave even more control over to Mohammed. Consequently illicit diamond mining within

Sierra Leone mushroomed. By 1991, Sierra Leone had an unscrupulous government and blatantly illicit diamond trading and these circumstances made it a susceptible and tempting site for armed rebellion. Civil war started when a group of 100 fighters from Sierra Leone and Liberia, the Revolutionary United Front, invaded east Sierra Leone on 23rd March. The Revolutionary United Front was led by an ex-army sergeant, Foday Sankoh. He said he represented the deprived city peoples and promised destitute agricultural workers a greater percentage of the mineral wealth squandered by the corrupt Government. However, Sankoh used cruel schemes against these same peasant workers to ostensibly expose the government's powerlessness to protect its citizens.

According to Johnson (2002), during all nine years of the war, conflict was concentrated in and around the diamond areas. Sankoh was very conscious of the fact that whoever controlled the diamond mines controlled the country, and funds gained from smuggled diamonds financed the war. Since the civil war began, Sierra Leone has suffered absolute devastation. It is totally dependent on external support from Great Britain, Nigeria and South Africa's security forces, as its own defence force is corrupt. Finally, under pressure from the United Nations and the United States Government, in July 1999 Sankoh and Sierra Leone's president, Ahmad Tejan Kabbah, signed the Lome Peace Accord. The Revolutionary United Front undertook to surrender its troops for a place in the Government, and as a concession to them, Sankoh was delivered from the death sentence he deserved for his war crimes and he was made chairman of the Strategic Mineral Resources Commission, a position in which he controlled most of Sierra Leone's diamond exports. Although the agreement was long in coming, it brought only a short peace. Just seven months after it was signed In January 2000, the Revolutionary United Front revived its attacks on Freetown and Sierra Leone's government and despite, its promises to surrender its forces, never did. Now Sierra Leone is once again struggling, and the issue of command of the diamond mines is still at the centre of the conflict. As a result, the United Nations finally issued a ban on non-governmental diamonds from Sierra Leone.

6.3 Macroeconomic indicators

Macroeconomics is defined by the BusinessDictionary.com (online) as:

the study of the behaviour of the entire economics or economical systems instead of the behaviour of individuals, individual firms, or markets. Macroeconomics is concerned primarily with the forecasting of national income, through the analysis of major economic factors that show predictable patterns and trends, and of their influence on one another. These factors include the level of employment/unemployment, gross domestic product, and prices affected by either inflation or deflation. Macroeconomics also covers the role of fiscal and monetary policies, economic growth, and determination of consumption and investment levels.

6.3.1 Population

According to the World Development Indicators (World Bank 2014:18), population is defined as follows:

based on the de facto definition of population, which counts all residents regardless of legal status or citizenship – except for refugees not permanently settled in the country of asylum. They (Refugees) are generally still considered to form part of the population of their country of origin. The values shown are midyear estimates.

Table 6.1 below depicts the population figures for the African countries in 2012 according to the annual report on the world development indicators by The World Bank (World Bank, 2014: 12) as follows:

Table 9: The World Bank Population statistics for the 6 African countries

<u>Country</u>	<u>Population in millions</u>	<u>Surface area in thousand square km</u>	<u>Population density measured in people per square km</u>	<u>Urban population measured as a % of total population</u>
South Africa	52.3	1219.1	43	62
Zambia	14.1	752.6	19	40
Botswana	2.0	581.7	4	62
Ghana	25.4	238.5	111	53
Liberia	4.2	111.4	44	49
Sierra Leone	6.0	71.7	83	40

6.3.2 Unemployment

Unemployment is defined by the International Labour Organization (World Bank Report: 2014) as members of the economically active population who are without work but available for and seeking work, including people who have lost their jobs or who have voluntarily left work. Some unemployment is unavoidable.

Changes in unemployment over time may reflect changes in the demand for and supply of labour, but they may also reflect changes in the reporting practices.

South Africa

According to a report by Bertelsmann Stiftung's Transformation Index (2012), unlike many African countries, South Africa has never experienced a socialist experiment. Before 1994 State intervention was used for political reasons to protect the white working class against labour market competition.

For this reason State and market-based parastatal companies still play a vital role. The essentials of a market economy are entrenched in South Africa and when compared to other African countries, the informal sector is relatively small, comprising approximately only 16% of employment.

The report (Bertelsmann Stiftung's Transformation Index: 2012) further states that South Africa's official unemployment rate is given as a rate of 25%, but if a more extensive definition is used, which includes discouraged jobseekers, the figure would be closer to 40%. Unemployment may become the downfall of South Africa's economy. During the financial and economic crisis in 2008 the inflation rate increased to 9.5% after which it dropped again to 6.8% in 2009. This was a large increase in relation to the comparatively moderate rate of around 5% in previous years. This increase was more due to external influences, such as the prices of fuel and food commodities, rather than to domestic incentives, which could be managed through interest rates. The situation recently improved as in 2010 the inflation rate dropped to 4%. The Government and the central South African Reserve Bank's goal of holding inflation in a range between 3% and 6% was met but, largely due to the increase in the price of oil, it was projected to peak at just under 6% by the end of 2011. The headline inflation rate is currently 5, 9%.

Zambia

According to the economic brief on Zambia by the World Bank (2013), Zambia's population is overwhelmingly young. According to 2010 estimates, 82% of the population was 35 years or younger, and 66% was 24 years or younger. Unemployment is an issue afflicting mainly the urban youth. In 2010 about 8.5% of Zambians in the working-age group reported themselves as unemployed. There was a pronounced urban-rural difference, with the urban unemployment rate at 19.6% which is more than six times the rural rate of 3.1% and 27.4% of urban youth in the 15 to 35 year old age group were unemployed, compared to just 4.4% in the rural areas.

Botswana

According to another report by the World Bank on Botswana, (2013), in 2010 the unemployment rate of Botswana was 17.8%. This estimate excludes discouraged job seekers. But if they were included, the unemployment rate would nearly double. In Botswana, unemployment among women is higher at 21.4% than the 14.5% rate experienced among men. This is so even though women have lower participation rates than men, at 71.6% versus 81.5%. In 2010 the 'formal labour force' numbered 378,832 workers, and of these, 51% or 192,598 worked in the public sector. In 2011 the total labour force was 1.1 million meaning that 18% of the labour force and one-half of the

'formal' labour force worked for the Government. Those outside the formal labour force number approximately 677,857 workers, many of whom are in low-productivity activities in the informal sector. Indeed, about 70% of rural households still depend partly on agriculture for their existence and this is subject to low and erratic rainfall, limited inputs, poor soil, and rain-fed systems of low productivity. The 677,857 workers in the informal sector are likely to include the estimated 148,470 poor between the ages of 21 and 64 years old.

Ghana

In the report by African Economic Outlook (2012) on Ghana, it states that as is typical of low-income countries, Ghana's population is regarded as young and growing. Youth account for an estimated 33% of its 22 million people and unemployment is rife within this segment of the population. Data shows that the younger age group of between 15 and 24 has an unemployment rate of 25.6% which is twice that of the 25 to 44 years age group and three times that of the 45 to 64 years old group. Recent gains in Ghana's economic growth have not converted satisfactorily into job opportunities in the formal sector. Only 11.5% are working in the formal sector with an estimated 54% of the labour force engaged in informal economic activities. Youth account for only 14% of the regular wage earners in formal sector employment, showing that they are unable to find jobs in this sector. This means that they must create economic opportunities for themselves in the informal sector as domestic employees, own-account workers, unpaid family workers or apprentices. The informal sector employs an estimated 22% of youth.

Liberia

According to a report by Bertelsmann Stiftung's Transformation Index (2014), unemployment levels in Liberia remain high with an estimated 85% of the population without formal employment. Poverty remains a major problem with 84% of the people living on less than \$1.25 per day. According to the Multidimensional Poverty Index 57.5%, or more than half the population, live in extreme poverty. Given the inadequate ability of the formal economy, most employment is in the informal sector, mainly in subsistence farming and petty trading. However, paid employment can be found with non-governmental organisations and state institutions. The rationalisation steps undertaken by the President Ellen Johnson Sirleaf administration in the government

sector have led to cuts in public sector employment. The high numbers of unemployed youth continues to constitute the most critical problem. Informal groups of young men, many of them ex-fighters, are not only regarded as real threats to security, but also underlines the problematic issues of reintegration and the unemployment of young men.

Sierra Leone

In a report by the African Economic Outlook (2012:14), it states that youth unemployment is a challenging social problem in Sierra Leone. The country's youth unemployment rate "is amongst the highest in the West African sub-region, standing at 45.8% of the total unemployment figure in 2008 (Ministry of Labour and Social Security, 2008)." This considerable unemployment rate for youth reveals only part of the challenge they face in the sub-region with extraordinary levels of underemployment, inactivity, and inferior working conditions with long hours and low pay; the huge majority have minimal chance of finding a stable job. Sierra Leone is a post-conflict country and during the time of war, major economic activities including food production, private investment, transport, communication and training came to a standstill, while valuable resources such as infrastructure, buildings, factories and institutions were either damaged or destroyed. Aside from these factors relating to the frailty of the country, the inadequate ability of the private sector and a typically challenging economic environment, aggravated by the international economic reversal and its effects on the country's labour market and economy, have made the situation worse.

Sierra Leone has a very young population with 60% of its people between the ages of 15 and 34, of these 65% are of working age. This fuels the shortage of permanent jobs and has countless socioeconomic and security repercussions for the country.

6.3.3 Poverty

Poverty, is defined by BusinessDictionary.com (Online),

as the condition where a person's primary needs for clothing, food and shelter are not met. Typically, there are two levels of poverty:

- Absolute poverty is equivalent to complete destitution and occurs when people cannot procure sufficient nutrition and calories to support a minimum level of physical health.
- Relative poverty occurs when people do not attain to a certain base level of living standards as determined by a Government and which would be available to the majority of the population. These usually vary from country to country but sometimes even within the same country.

Table 10: The World Bank Poverty statistics for the 6 African countries

<u>Country</u>	<u>Survey year</u>	<u>Population below \$1.25 a day measured as a %</u>	<u>Population below \$2 a day measured as a %</u>
South Africa	2009	13.8	31.3
Zambia	2010	74.5	86.6
Botswana	1994	31.2	49.4
Ghana	2006	28.6	51.8
Liberia	2007	83.8	94.9
Sierra Leone	2011	51.7	79.6

Source: World Bank report (2014)

It would appear that, looking at the above information, that poverty in South Africa is far less than in the other 5 countries.

6.3.4 Economic growth

Economic growth is defined by BusinessDictionary.com (online) as the increase in a country's productive ability, as measured by comparing gross domestic product in a year with the gross domestic product of the previous year.

Gross domestic product is defined as follows: at purchase prices, the sum of gross value added by all resident producers in the economy plus any product taxes, excluding subsidies, not included in the valuation of output. It is calculated without deducting depreciation of fabricated capital assets or for depletion and degradation of natural resources. Value added is the net output of an industry after adding up all outputs and subtracting intermediate inputs (The World Bank Report: 2014)

Table 11: The World Bank Economic growth statistics for the 6 African Countries

<u>Country</u>	<u>Gross domestic product 2012-2013</u> average annual % growth	<u>Gross domestic product 2013-2014</u> average annual % growth	<u>Gross savings – 2012</u> % of GDP	<u>Central Government cash surplus or deficit – 2012</u> % of GDP
South Africa	1.9	2.7	13.2	-4.4
Zambia	6.0	6.5	24.7	5.0
Botswana	4.6	4.9	40.7	-1.9
Ghana	7.4	7.4	21.5	-3.9
Liberia	7.9	7.5	31.4	-2.6
Sierra Leone	17.0	14.1	10.2	-5.2

Source: World Bank report (2014)

It would appear that the average annual growth in gross domestic product for South Africa is less than that of the other 5 countries.

6.3.5 Income and wealth distribution (Gini index)

The Gini index is defined by BusinessDictionary.com (online) as the standard economic measure of income inequality, based on the Lorenz Curve. A society that scores 0.0 on the Gini index has a perfect equality in income distribution. The higher the number above 0 the greater is the level of inequality. A score of 1.0 (100) indicates total inequality where only one person has all the income.

South Africa

According to the Bertelsmann Stiftung's Transformation Index (2012) report, South Africa is categorised as a middle income country with a robust industrial sector and a well-developed infrastructure. The Bertelsmann Stiftung's Transformation Index is responsible for analysing and evaluating the quality of democracy, market economy and the political management of 129 developing and transition countries. Since 1995 its Human Development Index has dropped steadily. According to information

obtained from Wikipedia (Online), the Human Development Index can be defined as “a composite statistic of life expectancy, education, and income indices used to rank countries into four tiers of human development”. In 2008 it decreased from 0.67 where it was ranked 125 out of 177 countries, to 0.60 in 2010 and was ranked 110 out of 169 countries. Relative to other countries with a similar GDP the South African Human Development Index performance is low, particularly given the adverse effect of HIV on life expectancy. The high GDP per capita conceals huge income inequalities.

South Africa, in 2000, had one of the most unequal income distributions in the world as the Gini coefficient stood at 0.68, but by 2008, this score had increased further to 0.70 according to a recent study (Stats SA: 2000; National Income Dynamics Study: 2008). Since democratisation in 1994, income polarity within the different race groups, especially within the black population group, has escalated dramatically. According to the latest figures from the World Bank (World Development Indicators: 2014), 31.3% of South Africans are regarded as poor, with less than \$2 a day to live on. The vast majority of these are black South Africans.

Zambia

A report by the Food Security Research Project (2011), states that income inequality remains very high in Zambia despite the growth in the gross domestic product over the past five years. Based on the Gini coefficient, the income imbalance has increased slightly over time, from 0.64 in 2001 and 2004, to 0.67 in 2008. It further states that the benefits from general economic progress in the country are not effective so far in reducing the inequality gap.

Botswana

According to the Bertelsmann Stiftung’s Transformation Index (2012) on Botswana, the Gini coefficient shows Botswana to be one of the most unequal societies in the world. Its Gini coefficient is 60 with a Human Development Index of 0.663. Botswana is ranked at 98 out of the 169 countries listed in the 2010 Human Development Index, but this still represents an improvement from being ranked 126 in 2008.

Ghana

In the Bertelsmann Stiftung's Transformation Index (2012) report on Ghana, it describes the economic development in Ghana as being irregular. The Gini coefficient for Ghana is a little more than 40, but particularly growth in agricultural products has spread benefits across a broader sector of the population. In the 2010 Human Development Index Ghana ranked 130 out of 169 countries.

Liberia

According to the Bertelsmann Stiftung's Transformation Index (2012) report on Liberia, inequality and poverty are basically ingrained in Liberia. The country's Gini coefficient is 52.6 and it ranked 156 out of 169 countries in the 2010 Human Development Index.

Sierra Leone

The Bertelsmann Stiftung's Transformation Index (2012) report on Sierra Leone states that Sierra Leone suffers from rampant malnourishment, mass deprivation, inadequate infrastructure and scant availability of fundamental medical services. The Gini coefficient is 62.9 and Sierra Leone is ranked 158 out of 169 countries.

6.3.6 Mining contribution to the economy

The economic growth of a country is an important macroeconomic indicator. In order to understand the value that of mining in the economy, it is imperative to understand how the industry contributes to the economy.

South Africa

In her report on mining and minerals in South Africa, Kearney (2012), explains that the expansion of South Africa's secondary and tertiary industries, as well as the corresponding contribution of mining to South Africa's gross domestic product, has declined during the last 10 to 20 years. Nonetheless, the mining industry is constantly adjusting to evolving local and international world conditions, and it continues to be a pillar of the economy, making a major contribution to job creation, economic activity, and foreign exchange earnings. Mining and its related industries are also crucial to South Africa's socioeconomic development.

Kearney (2012) further submits that in recent years, the benefits of the mining industry to the economy have declined, despite the fact that there has been progress in South Africa's secondary and tertiary sectors. Nonetheless, the mining industry continues to act as a magnet for foreign investment into the country as well as still accounting for roughly one third of the market capitalisation of the Johannesburg stock exchange.

In a presentation done by Senior Executive of the Chamber of Mines of South Africa; Baxter (2011), he stated that the mining industry in South Africa plays a pivotal role in the development and sustainability of the country. It is probably this country's key foundation industry, as it has helped South Africa develop into the most industrialised country in Africa. It is one of the largest employers of semi-skilled and skilled workers, and acts as a significant multiplier in the rest of the economy through large procurement deals, investments in infrastructure and the economy, and by being a wage spender to locally employed workers. Equally important, is the fact that the various companies currently operating in mining activities in South Africa are very large magnets for foreign investment inflows, which helps considerably with funding our current account. In this regard, the mining industry is also critically important as a nett generator of foreign exchange for South Africa. The sector also accounts for roughly one-third of the market capitalisation of the Johannesburg stock exchange, and continues to act as a magnet for foreign investment into the country.

Kearney (2012) states that mining has contributed to South Africa's economy in the following ways:

- the mining industry has directly and indirectly created one million jobs in an equal ratio
- it accounts for roughly 18.6% of South Africa's Johannesburg stock exchange, 8.6% directly and 10% indirectly
- it is a critical earner of foreign exchange contributing more than 50% of the total raised
- accounts for 20% of all investments in South Africa, of which 12% is directly and 8% indirectly
- it attracts significant amounts in foreign savings, that is R1.9 trillion or 43% of the total value of the Johannesburg stock exchange

- total corporate taxes from the mining industry account for 13,2% of all corporate tax receipts, which translates to R17 billion for the 2010 tax year
- total amount from royalties for the 2010 tax year amounted to R6 billion
- total amount of expenditure spent by the mining industry amounted to R441 billion, and of this amount, R407 billion was spent locally
- it accounts for 50% of the total volume of Transnet's rail and ports freight
- 94% of all electricity generation via coal power plants are accounted for by the mining industry
- the electricity consumed by the mining industry accounts for roughly 15%; and
- it accounts for about 37% of the country's liquid fuels via coal, which, when translated in monetary terms is estimated at roughly R30 billion.

Kearney (2012) also reported the breakdown of expenditure made by the mining industry for the 2010 tax year. The total of all the expenditures amounts to R441 billion, and is summarised as follows:

- R228.4 billion was spent on purchases and operating costs such as steel explosives, timber, transport, electricity, uniforms etc
- R78.4 billion was spent on paying the wages and salaries for the employees of the mines
- R49 billion was spent on Capex which is the lifeblood of mining. It can be defined as capital expenditures incurred to create future benefits
- R17 billion was spent in corporate taxation
- R16.2 billion in dividends to its shareholders
- R38 billion on depreciation and impairments; and
- R13 billion on interest to the banks.

According to Kearney (2012), roughly 90% of this, or R409 billion, was spent locally, and the spending multipliers created as much economic value and work opportunities as the direct mining sector contributed. In addition, the listed mining companies represent more than 30% of the market capitalisation of the Johannesburg stock exchange. There are also other benefits to the economy: extraction-related industries are an essential driver of the Johannesburg Stock Exchange, representing R1.9 trillion, or 42% of its value. Mining also provides the feedstock for about 94% of the country's electricity generating ability. The total value of sales increased by 24.8% to

R302.2 billion (\$37 billion) in 2010, and the three top-selling materials – gold, platinum group metals, and coal – accounted for 66.3% of total mineral sales.

Zambia

According to a report by the International Council on Mining and Metals (2014:43) regarding the impact that the contributions by the mining industry has had on the Zambian economy and society, it comments that “Zambia had the second highest levels of “mineral export dependence” anywhere in the world in 2010.” Relaying information obtained from the United Nations Conference on Trade and Development, mineral exports accounted for around 80% of the US\$9 billion total exports in that year. The rapid growth in export earnings since 2002 has been dominated by non-ferrous metals, especially copper, and it reflects a combination of increased international copper prices and increased production fuelled by large investments in the privatised mining sector. From 1970’s through to the 1990’s, the share of total investments in Zambia’s gross domestic product remained low in absolute terms but also almost flat in relative terms. After privatisation, this situation changed when the investment share of gross domestic product rapidly rose to more than 25% by the mid-2000’s as mining companies recapitalised operations so as to take advantage of higher mineral prices. A precise understanding of mining’s contribution to Zambia’s gross domestic product matters, as by definition it represents the gross incomes produced by the mining industry, mainly composed of labour incomes and profits. The unofficial evaluation of the contribution made by the mining sector to Zambia’s gross domestic product is said to be around 12% in current prices. This is in contrast to the existing official estimate of less than 4%.

Botswana

According to a report by African Economic Outlook (2012:2), “Botswana’s economy remains one of Africa’s success stories, having transformed itself from a Least Developed Country at the time of independence in 1966 to a Middle Income Country within three decades.” Aided by improved global demand for diamonds which are the country’s major export commodity, Botswana’s economy rebounded strongly from the 2009 economic crisis. The mining sector’s contribution to the gross domestic product declined from 46.1% of the gross domestic product in 2006 to 34.7% in 2010. Having said this, Botswana’s medium term economic potential continues to depend on

improved private sector investment, and on global demand for its major exports, notably diamonds. In the wake of larger budget deficits caused by the global financial crisis, Botswana is undergoing financial consolidation. The government is committed to reducing the budget deficit and achieving a balanced budget by 2012/13. This will be accomplished through enhanced revenue collection and moderate repetitive development expenditures, while maintaining economic growth. The budget deficit is thus expected to narrow from 8.1% of gross domestic product in 2010/11 to 5.2% in 2011/12 and on to a balanced budget in 2012/13.

Ghana

In a report published by the Ghana Chamber of Mines (2012), it states that the country's mining industry performed fairly well in 2012. Predictably, gold led the way in performance by mineral type. As stated in the Gold Fields Mineral Survey, Ghana was the 8th leading producer of gold worldwide as its yield increased by 6% to 96.8 tonnes, regaining its 2010 position. This was better than the 9th position it attained in 2011. The improved performance of the mining sector reflected in its major contributions to the country's economy in 2012. The Bank of Ghana has reported that in 2012, the mining sector's contribution to gross product export earnings was about 43%. In 2012, the Ghana Statistical Service stated that the mining sub-sector grew by 23.5%. This compares well with the 18.8% it achieved in 2011. Furthermore, the Ghana Revenue Authority has stated that in 2012 the mining sub-sector held its position as the principal contributor to the Authority's domestic tax collections. In 2012, the mining industry again made a positive impact on the Ghanaian economy. Aside from its direct contribution to the general growth of the economy and to the GRA's treasury, the mining industry's impact was felt in various aspects of the country's business environment. Producing member companies returned about 72% of their mineral income to the country. Of this, an average of 17% was returned through the Bank of Ghana and 55% through Commercial Banks with which they did business.

Liberia

According to a report on Liberia by African Economic Outlook (2012), in 2011 Liberia recorded its eighth consecutive year of post-war economic expansion fostered by the first iron ore exports since the war ended, greater output of timber and higher rubber exports due to vigorous international prices. In 2011 real gross domestic product is

estimated to have increased by 6,9%, and is projected to be 8,8% in 2012 and 7,2% in 2013 mainly supported by the first full year of iron ore exports in 2012 and ongoing direct foreign investment. In 2011 consumer price inflation is expected to be 8.5%, mostly reflecting the range of international fuel and food prices and also insufficient domestic market supply due to poor farm-to-market road infrastructure.

The report (African Economic Outlook: 2012) further states that the industrial sector will increase considerably in the next few years due to the growth in iron ore mining. In 2011 the mining and panning sector is expected to increase from about 1% of GDP to more than 20% of gross domestic product by 2015. Exports of iron ore from the Yekepa mine run by Arcelor Mittal began in September 2011, and the company expects to export four million tonnes annually. The Liberian economy is exceedingly vulnerable to international shocks. It is defenceless against commodity price fluctuations, particularly for its rubber and iron ore exports. As much of its iron ore is of low-grade, mining is only profitable when prices are favourable.

Sierra Leone

According to the report by African Economic Outlook (2012), it states that encouraged by the mining sector, real gross domestic product growth accelerated from 6% in 2011 to 16.7% in 2012, mostly as a result of iron ore production. It has also been supported by agriculture, services and an increase in construction. Gross domestic product growth is projected to settle around 7.2% in 2013 before growing in 2014 to 12.1% as iron ore projects become completely functional. This vigorous economic growth has been complemented by a tight fiscal policy that has minimised inflationary pressures. The expansion of the extractive sector as well as recent discoveries of iron ore mines in Sierra Leone have launched a structural reconstruction of the economy with a change of productivity from agriculture to mining and construction enterprises that are now the principal energisers of the gross domestic product. However, due to the fact that extractive activities and construction are capital intensive industries, transfer of labour to these sectors is slow. Under its new development strategy, "Agenda for Prosperity 2013-17", the Government plans to enhance revenue collection and improve its administration of natural resources.

The report (African Economic Outlook: 2012) continues by stating that the mining and quarrying sector is thriving and will continue to be one of the principal drivers of gross

domestic product growth in the coming years. In 2012 its share in the gross domestic product has more than doubled with 12.1% compared to 5.4% in 2011. Three large mining projects, namely Tonkolili, Marampa and Bembeye, began in 2012 and will increase iron ore exports in 2013 and 2014 thus making Sierra Leone one of Africa's largest producers of iron ore within five years. This will inevitably enhance the country's trade balance and boost their tax collection efforts. In addition, the extension of this sector contributes to revamping infrastructure as the foreign mining company, African Minerals Limited that operates the Marampa and Tonkolili iron ore mines, plans to invest in transport facilities to link the mines to the country's maritime port.

Table 12: Summary of macroeconomic indicators as per the 2014 World Development Indicators report

Country	Unemployment rate	Gini Coefficient	Poverty % of people living on under \$2 a day	Population in millions	Mining contribution to economy	Economic growth GDP 2013-2014 average annual % growth
South Africa	25%	70.0	31.3	52.3	20%	2.7
Zambia	13%	67.0	86.6	14.1	12%	6.5
Botswana	17.8%	60.0	49.4	2.0	34.7%	4.9
Ghana	12.9%	40.0	51.8	25.4	43%	7.4
Liberia	3.7%	52.6	94.9	4.2	1%	7.5
Sierra Leone	3.4%	62.9	79.6	6.0	12.1%	14.1

Source: *The World Bank report*

6.5 Conclusion

In this chapter the history of the five African countries referred to in *The State Intervention in the Minerals Sector Report* (ANC: 2012) were discussed. Furthermore, macroeconomic indicators such as population, poverty, gross domestic product and

mining's contribution to the economy, as well as the forms of state participation for the five countries as well as that of South Africa were compared to determine similarities and differences between them.

The analysis provided insight into the challenges facing the countries in Africa, and the impact that the mining industry has on the livelihood of these countries. The challenges all the countries face are generally the same, it is only the impact of these challenges that differs, and the effects that it has on the country as a whole.

In terms of the data discussed above, South Africa is the biggest (both in population and land area) of the six African countries being compared, with 52.3 million people, followed in second place by Ghana, with less than half the population size of South Africa. In 2012, South Africa's unemployment rate was 25% (excluding discouraged jobseekers) which is the highest out of all the African countries compared. This is coupled with 31.3% of people living on under \$2 a day, and a Gini coefficient of 70.0.

The contribution made by the mining industry within South Africa is relatively in line with that of the contributions made by the mining industry in the other African countries. In all the other countries, foreign investment in their economies plays a major part, and nationalisation could certainly decrease foreign investment in South Africa's economy.

The challenge that South Africa currently faces is to look at ways in which it can successfully address issues such as poverty, unemployment and the uneven distribution of income, through better management of the processes and procedures already in place in its mineral and other vital industries.

In the next chapter a breakdown of the taxation models imposed on the mineral industries of the five African countries will be analysed to compare the fiscal regimes currently in place.

CHAPTER 7

TAX MODELS IMPOSED ON THE MINERAL SECTORS IN ZAMBIA, BOTSWANA, GHANA, LIBERIA AND SIERRA LEONE

7.1 Introduction

Taxes are the

main source of revenue for most governments. Tax revenue as a share of gross domestic product provides a quick overview of the fiscal obligations and incentives facing the private sector across countries (World Bank Report, 2014: 104).

The table below (World Bank Report, 2014:74) shows only central government information, which may notably understate the total tax burden, especially in countries where provincial and municipal governments are large or have significant tax authority. Low ratios of tax income to gross domestic product may mirror weak administration and extensive tax avoidance or evasion. Low ratios may also reflect a substantial parallel economy with unrecorded and undisclosed incomes. Tax revenue ratios tend to rise with income, as higher income countries rely on taxes to fund a much wider range of social services and social security than lower income countries are able to do.

It is submitted that because no two countries are the same, it is important to look at all the factors that influence each country's particular tax method and the outcomes it achieved from the model used. The tax models to be discussed below are that of Zambia, Botswana, Ghana, Liberia and Sierra Leone. The discussion will include corporate tax, withholding taxes, royalty tax and value added tax as well as the deductions allowed against income. The tax models will then be compared against the model currently in place in South Africa, as well as the tax model proposed in *The State Intervention in the Minerals Sector Report* (ANC: 2012)

Table 13: Tax revenue collected by central Governments

<u>Country</u>	<u>Tax revenue collected by central government</u> % of GDP 2012
South Africa	26.4
Zambia	19.7 <i>b</i>
Botswana	27.2 <i>b</i>
Ghana	14.9 <i>b</i>
Liberia	20.9 <i>b</i>
Sierra Leone	10.9 <i>b</i>

Source: World Bank report (2014)

b. Data were reported on a cash basis and have been adjusted to the accrual framework of the International Monetary Fund's Government Finance Statistics Manual 2001

7.2 A summary of the fiscal regimes of Zambia, Botswana, Ghana, Liberia and Sierra Leone

Zambia

According to the Zambia Tax Highlights report (Deloitte International Tax: 2012) on the Zambian tax system, Zambia's fiscal regime compares well with other countries with similar mining activities but also boasts a number of financial incentives to encourage foreign investments into the country.

The following information was obtained from the Ministry of Mines and Minerals Development (Zambiamining.com, 2012: Online):

- Corporate Tax

Exporters of copper and cobalt are subject to a levy of 35% of taxable income, whereas the exporters of other minerals and "non-traditional" commodities attract a levy of only 15%. Companies listed on the Lusaka Stock Exchange are levied at 30% of taxable income.

- Relief from Income Tax

Investments in mining, including prospecting, attract deductions from income tax on the following expenditures:

- capital expenditure, allowances of 25% on plant, machinery and commercial vehicles
- 20% on non-commercial vehicles; 5% on industrial buildings
- prospecting expenditure under special circumstances
- mining expenditure under special circumstances
- mining expenditure on a non-producing mine
- mining expenses incurred by a mine of irregular production close to the end of its life
- 100% deduction of pre-production expenses and other capital expenditures as defined in the Income Tax Act; and
- Accelerated depreciation for expenditure on equipment and machinery which does not qualify for the 100% deduction.

- Allowable losses

These are losses incurred while mining for any mineral in Zambia and are unlimited. They can be carried forward to the next year and be offset against any profit that the company may make in the future.

- Royalties

A royalty is payable calculated as 2% of the market value of the minerals freight on board, less the cost of smelting, refining, insurance, handling and transport from the mining area to the point of export or delivery within Zambia. Royalty payments may be deferred if the cash operating margin falls below zero for holders of Large Scale Mining Licences.

- Import duty

Import duties are charged on specific items and they vary from 20% to 40%. Certain essential goods are exempt from import duty, including crude oil for example.

- Relief from other surcharges

A holder of a mining right is exempt from customs, excise and value-added tax duties in respect of all equipment and machinery required for exploration or mining activities.

- Remission

There are no restrictions in respect of the amount of profits, dividends, or royalties that may be externalised, although a withholding tax of 15% is levied.

Botswana

According to the Botswana Tax Highlights report (Deloitte International Tax: 2013) on the tax system in Botswana, there are both direct tax and indirect taxes levied on the mining industry, and are in certain cases specific to the kind of mineral exhumed.

The following is an extract of Botswana's fiscal regime as per the Chamber of Mines (Botswana Mineral Investment Promotion: 2008):

- Variable Income Tax Rate

The income tax rate levied will be different depending on the minerals a mining company exhumes.

In Botswana, diamond mining is not subject to the same tax model as other minerals, as the diamond tax regime is negotiated between the Government and the third party. In certain cases a variable income tax rate can be applied if there is an agreement between the parties involved.

Of all the other minerals, the tax levied is at a variable tax rate, varying anywhere from the lowest rate of 22% to the highest rate of 55%. The tax rate applicable is derived by using the following formula:

$$70-1500/x;$$

Where x (%) equals taxable income/gross income of the company, pertaining to the mineral mined in Botswana.

- Capital allowances

100% depreciation of capital expenses is deductible.

- Allowable losses

The deduction of losses incurred while mining for any mineral is unlimited. It can be carried forward to the next year and be offset against any future profits that the company may make.

- Dividend Withholding Tax

A withholding tax of 7, 5% is levied on all dividends paid by a resident company to a resident of Botswana or non-resident.

- Value-Added Tax

VAT of 10% applies on all items except zero-rated items, which include exports of minerals. Value added tax refunds are available upon re-export within six months of items brought into the country.

- Mineral Royalty Rates

Different royalty rates apply to different types of minerals. For precious stones like diamonds, the rate is 10%. Rates of 5% apply for precious metals and 3% for all other minerals. The rate is calculated on the gross market value of the mineral sales at the “Mine gate”, called an “arms-length transaction”.

- Import Duty

Duties are payable on all imports except for mining equipment and spares, which are zero-rated.

- Taxation for downstream processing, that is: cutting, polishing and refining of minerals

A tax of 15% will be levied. This amount is comprised of a basic rate of 5% and an additional company tax rate of 10%.

Ghana

A similar report on the Tax Highlights of Ghana (Deloitte International Tax: 2012), states that a company is a resident in Ghana if, at any time during a year of assessment, it is incorporated under the laws of the country. Resident companies are

taxed on their global income. However, income sourced outside of the country is only taxed in Ghana if it is brought into or received in the country. Non-resident companies are taxed only on Ghana-source income.

The following data was obtained from the Ghana Tax Highlights report (Deloitte International Tax: 2012):

- Taxable income

Taxable income is based on the operating profit stated in the company's annual financial statements prepared in accordance with accounting standards, as adjusted by any differences between accounting requirements and the tax law. Such differences normally include exempt income, disallowed expenses and special reliefs granted under the tax law.

The corporate income tax rate in Ghana for companies other than mining companies are levied at 25%, while the corporate income tax rate applicable to companies engaged in mining is 35%.

- Capital gains and losses

Capital gains are taxed separately from business income at a rate of 15%. As from November 1990, gains arising from trading on the Ghana stock exchange are exempt from tax for thirty years.

Losses may be carried forward for five years following the year in which they were incurred. This applies to farming, mining, tourism, agro-processing, information communications technology and also to manufacturing companies that manufacture mainly for export. No others are allowed to carry forward losses.

- Dividends

Dividends paid to a resident or non-resident are subject to a withholding tax of 8%.

- Foreign tax credit

Companies can claim a foreign tax credit for taxes imposed on their income in eight countries that have concluded tax treaties with Ghana.

- Interest

Interest paid to a resident or non-resident is subject to an 8% withholding tax but this tax is not levied on interest paid to resident financial institutions.

- Royalties

A final withholding tax of 10% is levied on the payment of royalties to non-residents and royalties paid to residents is subject to 5% withholding tax.

- Branch remittance tax

A 10% tax is imposed on the repatriated profits of branches of non-resident persons operating in Ghana.

- Value Added Tax

VAT is imposed on the supply of goods and services in Ghana and on the import of goods and services. The tax base is generally the amount paid, plus any other duties and taxes, that is, excluding value added tax. For imports, the tax base is the customs value plus any import duties and taxes, except value added tax.

A standard value added tax rate of 12.5% and the National Health Insurance Levy of 2.5% apply, bringing the total to 15%.

Liberia

According to a guide on the tax system in Liberia, (PricewaterhouseCoopers: 2013) an entity is resident for tax purposes if that company:

- is incorporated or formed under the laws of Liberia and either:
 - has its management and control in Liberia; or
 - undertakes the majority of its operations in Liberia;
- is a corporation, registered business company, limited liability company, trust, foundation, limited partnership, or similar arrangement that undertakes some business activity in Liberia and has a majority of shareholders or beneficiaries, either by vote or by value, resident in Liberia; or
- is a general partnership, joint venture or trust and a partner, co-venturer or trustee

is a resident in Liberia.

The following information was obtained from the guide on the tax system in Liberia (PricewaterhouseCooper: 2013):

- Income tax

The income tax rate for mining and petroleum companies operating within Liberia is 30% with an additional 20% surtax. Additional surtaxes are levied on high-yielding mining projects.

Where a natural person or legal entity is expected to earn a gross income of less than LIB\$ 3,000,000 (USD 40,816.3) for a tax year, the person qualifies as a small taxpayer and has an obligation to pay corporate income tax at a rate of 4% of annual turnover in lieu of the income tax.

- Deductions allowed

A taxpayer is permitted a deduction for the ordinary expenses of producing income during the tax year. Such expenses include, among others, depreciation expense or amortisation of capital, losses incurred in a business and sustained during the tax year, or business interest on business indebtedness etc.

- Limitation of Deductions

Limitations to tax deductible expenses from gross income include capital expenditure, personal expenses and Liberian or foreign income tax, among others.

Foreign exchange gains or loss will only be recognized when they are actually realized, that is, when payments are made.

- Special incentive deductions

There are special incentives for qualifying new investors in specified industries such as manufacturing, tourism, health, energy, low and medium income housing, communication, transport, banking, export, agriculture and waste management. To qualify, the capital invested must be at least US\$1 million for foreign owned business and for enterprises with 100% Liberian ownership, a minimum capital investment of US\$300,000. For hospitals or health clinics, the minimum capital investment is

US\$50,000. The special tax incentive runs for five years from the commencement of investment as per the investor's certificate.

- Carry-over of tax losses

A net operating loss incurred in any particular year can be carried forward for a maximum of five years. The earlier losses will be relieved before the later losses. Carrying forward of losses is permitted up to five years for general companies and seven years for mining, petroleum and renewable resources entities.

- Limitation to carry over losses

If within a period of three years there is a change of at least 50% in the underlying ownership or control of a company, no carrying forward is allowed of any losses from prior periods or any concessions made as investment incentives.

- Withholding taxes

Dividends received by a resident corporation from another resident corporation are exempt from tax. However, this will not apply where the dividend received is by virtue of ownership of redeemable shares in the corporation paying the dividend or if the dividend is paid in a dividend stripping arrangement.

Payments by resident and non-resident mining, petroleum and renewable resource projects are levied as follows:

- Interest at 5%;
- Dividends at 5%; and
- Services at 6%

Sierra Leone

In the guide on the tax system in Sierra Leone (PricewaterhouseCoopers: 2012) it is stated that the current tax system in Sierra Leone provides that a company is resident for tax purposes if that company:

- is incorporated or formed under the laws of Sierra Leone;
- has its effective management and control in Sierra Leone; or

- undertakes the majority of its operations in Sierra Leone.

The report (PricewaterhouseCoopers: 2012) discusses the following taxes:

- Income tax

The income tax rate generally applicable to companies is 30%. Mining companies may be subject to any additional tax on profits agreed with the Ministry responsible for mineral resources. In certain circumstances, the tax liability of a company from business activities may be determined with reference to the turnover of the business.

- Deductions allowed

Generally, a taxpayer is allowed a deduction for all outgoings and expenses incurred in the production of assessable income. Allowable deductions generally include:

- Expenses incurred in promoting export quality of Sierra Leonean products; and
- Foreign currency debt losses.

- Capital allowances

Capital allowance deductions are granted for the depreciation of a taxpayer's depreciable assets. 100% of the expenditure on start-up costs of mineral and petroleum prospecting and exploration is deductible.

The capital allowances for production rights and other expenditure incurred on mineral and petroleum development are:

- 40% straight line on initial allowance; and
- 20% straight line on annual allowance.

- Carry-over of tax losses

Up until 1 January 2010, with some restrictions, companies could carry tax losses forward.

However, effective from 1 January 2010, unless a company is engaged in mining, losses incurred in years of assessment cannot be carried forward.

- Dividends

Ordinarily, dividends received from an investment in Sierra Leone by a resident and a non-resident person are subject to a final withholding tax of 10%. The withholding tax on dividends does not apply to a dividend paid by a resident company to another resident company or to a complying retirement fund resident in Sierra Leone.

In certain circumstances, payments other than distributions out of profits may be treated as dividends.

- International transactions

The income of a taxpayer may either be from a source in Sierra Leone or from a foreign source. Incomes from a Sierra Leone source include the following:

- Income derived from an activity which occurs in Sierra Leone;
- Natural resource payment for a natural resource taken from Sierra Leone.

- Income attributable to a permanent establishment or branch

A permanent establishment or branch of a non-resident person in Sierra Leone shall be treated as a resident legal person with respect to the business carried out by that permanent establishment or branch in Sierra Leone.

- Branch profit tax

Repatriated branch profit attracts tax at 10%. This is in addition to the corporate tax that the branch pays.

Branch profits repatriated in any year of assessment are the higher of:

- Funds repatriated in the year out of accumulated profits; and
- Chargeable income of the branch, less income tax paid on the chargeable income and any profits reinvested or retained in the branch.

7.3 Conclusion

This chapter focused on describing the tax models found in Zambia, Botswana, Ghana, Liberia and Sierra Leone.

The tax models imposed on the mining industries in the six African countries are very similar in terms of the percentages levied. Additional taxes are levied in certain countries on profit, while other countries provide greater relief or deductions on expenses incurred in the mining sector.

Below is a summary of the taxes discussed in comparison with each other.

Table 14: Summary of taxes discussed for the 6 African countries

Country	Corporate Income Tax Applicable to Mining	Dividend Tax	Interest	Value Added Tax	Capital Allowances	Tax Losses
South Africa	28%	15%	N/A	14%	Prospecting and exploration costs incurred is capitalised as “unredeemed capital expenditure” to be deducted against mining income once the mine is operational.	Tax losses can be carried over indefinitely
Zambia	35% copper and cobalt; 15% other minerals	15%	15%	16%	100% of pre-production expenses	Losses incurred while mining for any minerals is unlimited
Botswana	Variable rate between 22% - 55%	15%	10%	10%	100%	Losses incurred while mining for any minerals is unlimited
Ghana	35%	8%	8%	15%	The rate of amortisation for mining assets	Tax losses can be carried forward for five years following

					is 20% to be applied on a straight-line basis on the cost of those mining assets.	the year in which it was occurred.
Liberia	30%	5%	5%	7%		Tax losses can be carried over for a maximum of five years.
Sierra Leone	30%	10%	15%	15%	100% of start-up costs are deductible; 40% initial and 20% annual	Losses incurred can be carried forward

It is submitted that the tax model proposed in *The State Intervention in the Minerals Sector Report* (ANC: 2012) levied the highest amount of tax. The reason for the higher tax is due to the introduction of resource rent tax. This tax aims at taxing mining companies at 50% on the difference between the costs associated with extracting the mineral and the price it could get for the mineral, which is over and above the normal tax rate levied on companies of 28%.

It can be concluded that the resource rent tax could possibly discourage mining companies from seeking the best possible price for their minerals, or entice them to use less expensive (which could mean more risky) methods of extracting the minerals in an effort to narrow the gap between the costs associated with extracting the mineral and the price it can receive for the mineral in an arm's length transaction, to try to reduce the resource rent tax payable.

Botswana's tax model is very unique in the sense that it imposes a variable tax rate on mining companies operating within Botswana. As a result, the tax rate applicable varies from a minimum of 22% up to a maximum of 55%. The main driver in determining the rate of tax for a specific mining company is the relationship between

its taxable income and its gross income – or more simply put; the relationship between net profit and sales.

It is submitted that the model imposed on the minerals sector in Botswana, is more realistic, reasonable and fair than the tax model proposed in *The State Intervention in the Minerals Sector Report* (ANC:2012) and the current South African tax model. It would appear that the tax model used in Botswana ensures that the minerals sector is taxed on a scale more suitable to its trade, and that profitable mining companies pay taxes at a higher rate than smaller mining companies, making the taxes levied more rational. Furthermore, it is submitted that this system will provide the government with more funds to better the infrastructure, social development and economy, without the fear of losing foreign investments.

CHAPTER 8

CONCLUSION

The *State Intervention in the Minerals Sector Report* (ANC: 2012) emerged as a resolution during the 3rd National General Council Resolution on Economic Transformation held in 2012. The National General Council mandated the National Executive Committee to ensure that further work be done on ways in which the African National Congress can implement economic transformation in sectors such as the mining sector. It was suggested that methods including research, study tours and discussions be conducted to gather the required information. As a result of the research, the *State Intervention in the Minerals Sector Report* emerged. In this report (ANC: 2012), the mineral sectors of developed as well as developing countries are compared with each other.

The goal of the research according to *The State Intervention in the Minerals Sector Report* (ANC:2012) was to enable the African National Congress to present a scientifically researched overview of, particularly, the mining industry as well as international case studies, so that any political decision taken is based on an understanding of the real issues that other countries experience.

The terms of reference called for a critical analysis of:

- The existing mining sector, including potential and actual upstream and downstream sectors;
- Mineral-related logistics;
- Energy and environmental sustainability challenges and opportunities;
- Existing state assets in the sector;
- Present legislation and regulations including the licensing regulations; and
- The Mining Charter.

The project was also required to review a variety of international approaches to state intervention in the minerals sector, as well as the historical perspective on the evolution of current mineral regimes. This was achieved through evaluating the forms

of state interventions by “developmental states”, including through nationalisation, and evaluating other factors influencing such interventions in the context of maximising the growth, development and employment potential embedded in mineral assets.

The goal of the present research was to analyse the current tax model imposed on the mineral sector of South Africa, the proposed tax model as discussed in *The State Intervention in the Minerals Sector Report* (ANC:2012); and the tax models imposed on the mineral sectors of five other developing African countries, namely Zambia, Botswana, Ghana, Liberia and Sierra Leone. The purpose of the comparison was firstly to determine whether the countries were comparable with South Africa in terms of certain basic economic indicators. It is for this reason that the countries selected for the comparison were African countries only, as they share a relatively similar history and face the same challenges and volatility in the mineral sector. Secondly, the comparison was done to determine whether the South African proposed tax model is in line with trends in the countries used as comparatives to achieve the goals the model hopes to achieve.

Chapter 2 described the history of the mining sector in South Africa. This sector has played a significant role in the development of the economy, and is still a major role player in the country. South Africa’s mineral wealth is regarded as some of the world’s most valuable and its total resource value is estimated to be worth roughly R20.3 trillion, making South Africa the country with the fifth-largest mining sector in the world in terms of gross domestic product value. It is also the largest employer of semi-skilled labour, and a major attractor of foreign investment into the country.

Chapter 3 analysed the current tax model imposed on the mineral sector in South Africa. Currently, companies operating in this sector are taxed in accordance to the corporate tax rate of 28% on their taxable income. This is the same tax model imposed on all corporate entities in business in South Africa, excluding the Gold mining sector (which is not included in the present research). According to the current tax system, there are certain deductions and allowances specific to the mining sector, as well as provisions made for environmental management trusts focused on the rehabilitation of the environment surrounding mining activities. This could indicate that there is an opportunity, and possibly a need, to create a tax structure more specifically geared for the mineral mining sector in the economy, in order to maximise the fiscal impact it has

on the sector, to maximise the contribution made by the sector to the economy, and to reflect the responsibility that the sector has for the economy and the environment.

Chapter 4 provided an overview of the proposed tax model as suggested by *The State Intervention in the Minerals Sector Report* (ANC: 2012). According to this report (ANC:2012), State participation can be broadly defined as proposing various options ranging from 100% equity participation, through partial or carried equity arrangements, to equity participation without financial obligation. Mineral resources have long been viewed as having special strategic significance. It is a sector in which the state often believes it must have a high degree of control over strategic minerals (critical feedstock into the domestic economy, such as iron/steel) or minerals that dominate the national economy, for example, copper in Chile and Zambia and diamonds in Botswana. In a number of countries, this control has been exercised through direct state participation.

The Freedom Charter (Freedom Charter, 1955: 1) clearly states that “The national wealth of South Africa, the heritage of South Africans, shall be restored to the people. The mineral wealth beneath the soil ... shall be transferred to the ownership of the people as a whole.” As a result of this, and the National General Council’s mandate to the National Executive Committee to study the State participation models found in other developing and developed countries. Research was carried out by the National Executive Committee into State participation in South Africa’s minerals sector. *The State Intervention in the Minerals Sector Report* (ANC: 2012), the committee looked at various countries and models to try to understand which model has been most successful in creating wealth for its country.

The reasons for State participation, according to the report (ANC: 2012) can be divided into non-economic and economic objectives. With regard to the former, State participation was expected to regulate the behaviour of private sector investors in the national interest, to build national capacity in the resource sector through the transfer of information, managerial and technical skills from the private sector, and, whether explicitly stated or not, to address a wide range of development goals outside of the resource sectors. Specific objectives could include job creation, value addition, provision of social and physical infrastructure, and regional development.

Chapter 5 discussed the international trends and views regarding State participation in the mineral sector, by discussing the views and guidelines set out by The World

Bank. According to the report entitled "Overview of State Ownership in the Global Minerals Industry" (World Bank: 2011), most of the discussion regarding increased State ownership in the mining sector can be heard from African countries. This is understandable because not only is it the least thoroughly explored continent, but also because companies from China and other Asian countries have indicated their interest in African countries as potential investment targets. Although the experience from the previous wave of state-owned mining was less than positive, the desire to capture some of the opportunities in the present boom is strong and there is a conviction that many countries are now better prepared to govern the mining sector and manage mining companies than they were forty to fifty years ago. The World Bank report sets out the responsibilities of certain legislative bodies to be in place should a country decide to engage in the ownership of certain economic sectors in partnership with the private sector.

Chapter 6 compared South Africa's macroeconomic indicators with those of Zambia, Botswana, Ghana, Liberia and Sierra Leone, countries that were all identified and referred to in *The State Intervention in the Minerals Sector Report* (ANC: 2012), as examples of African countries where State participation was previously or currently being implemented. It was deemed necessary to make a comparison based on the history and macroeconomic indicators, to determine whether factors that influence South Africa's economy and would impact on its mining activities, are similar to those found in the five African countries. Also, macroeconomic indicators such as poverty, unemployment and economic growth have a direct impact on the country's ability to generate profits, while indicators such as the Gini coefficient indicates a country's ability to distribute the wealth created within its economy to the people of that country.

In its 2014 report, The World Bank (The World Bank: 2014) states that a country's economic growth has a greater impact on poverty reduction when income is more equally distributed. Furthermore, the report (The World Bank: 2014) paints a grim picture of the situation, looking at South Africa's macroeconomic indicators. Of the six African countries, including South Africa, it has the largest population, and the contribution made by the mining industry is the third highest after Ghana and Zambia, yet it has the highest unemployment rate, as well as the highest Gini coefficient, indicating that the income generated within the country is not equally distributed

between all its citizens. Also, the World Bank data indicated that South Africa's economic growth is the lowest compared to the other five countries analysed.

This indicates that South Africa still has a long way to go to ensure that "its house is in order" to ensure that it can create and sustain healthy economic growth. Its focus should be on decreasing the unemployment rate, addressing poverty and ensuring that income is more equally distributed among the citizens of South Africa.

The following is a summary of macroeconomic indicators -

Table 15: Summary of macroeconomic indicators

Country	Unemployment rate	Gini Coefficient	Poverty % of people living on under \$2 a day	Population in millions	Mining contribution to economy	Economic growth GDP 2013-2014 average annual % growth
South Africa	25%	70.0	31.3	52.3	20%	2.7
Zambia	13%	67.0	86.6	14.1	12%	6.5
Botswana	17.8%	60.0	49.4	2.0	34.7%	4.9
Ghana	12.9%	40.0	51.8	25.4	43%	7.4
Liberia	3.7%	52.6	94.9	4.2	1%	7.5
Sierra Leone	3.4%	62.9	79.6	6.0	12.1%	14.1

Source: The World Bank report

Chapter 7 analysed the current taxation models adopted in the five African countries. The rates imposed as well as what is taxed, varies between the different countries. In Zambia, where the mineral sector was previously nationalised but currently has a more privatised model, the focus is more on ensuring foreign participation in mining activities through financial incentives such as relief from income tax, in certain instances. In Botswana, Debswana is a partnership between the Government and De Beers that controls its diamond mining industry. For all other minerals exhumed, a variable

income tax rate is applicable, which is dependent on the gross income of the company. Ghana's tax rate is based on the operating profit made by the company. Zambia's mining contribution to the economy has increased significantly in the last year. This was due to the Government actively encouraging foreign investment especially in its iron ore mining industry. The tax rate imposed on mining activities differs from other industries, and is levied at 30%. In Sierra Leone, the legal mining sector is very small in comparison to the illegal mining activities in the country. The tax rate applicable to legal mining activities is 30%, and may be subject to additional tax on profits agreed to with the Ministry responsible for mineral resources.

The present research indicates that there is no "one size fits all" approach to the taxation of the mineral sector, and that countries must take into consideration all the factors pertaining to the industry before making any fiscal decision. Foreign investment and participation in developing countries are vital for their development and, as such, any fiscal policy should not discourage foreign investment, but try to involve and increase it to ensure increased benefits to the country.

In conclusion, the findings of this thesis indicate that there are many factors to consider and further research is necessary before South Africa will be in a position to propose the most suitable taxation model to be used in the mineral sector. Factors that need to be taken into account vary from political stability, the economic indicators as discussed in this study as well as promoting foreign investment in South Africa as a tool for economic growth. *The State Intervention in the Minerals Sector Report* (ANC:2012) addresses vital issues such as the effective linkages to be developed between the mineral sector and the rest of the economy through better investment in infrastructure, better education in maths and science and using profits made by the mineral sector to up-skill the labour force working in the mineral sector.

Certain aspects discussed in the report are of concern, such as the nationalisation of the minerals sector, as this will have adverse effects on South Africa's economy as well as the people of South Africa as foreign investment will decline, resulting in a weaker Rand and unemployment should international mining companies withdraw from the South African economy. Furthermore, the granting of mineral rights through public tender can pose problems, as South Africa has a history of tender fraud. To ensure that the tenders granted by the Government are given to the most suitable

candidates who will be able to best implement and exercise the responsibilities surrounding the mineral right, absolute transparency will need to be ensured. Lastly, the formulation of the Resource Rent Tax is unrealistic and problematic as it would discourage foreign investment and drive out foreign companies presently operating in South Africa.

Areas relating to the minerals sector that are not addressed in this thesis include the gold mining sector of South Africa as well as the diamond mining sector of Botswana.

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