Maximising fiscal benefits

by

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Maximising fiscal benefits

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Outline

1. The revenue objective
2. Key challenges
3. Implications for fiscal policy
4. Optimising government benefits
5. Concluding remarks
1. The revenue objective
The AMV (2009)

- Obtain an adequate share of mineral revenue
- Utilise revenues to eradicate poverty and finance growth and development
2. Key challenges
A. Characteristics of mineral resources (projects)

- High risk
- Capital intensive
- Quality & extent of resources unknown
- Long lead times
- Profitability uncertain
- Price volatility
- Depletable
- Environmental and social costs
- Minerals without reference price

Investor

Government
B. Conflicting interests

- **Governments**
  - Sufficient incentive to attract investment
  - Extensive exploration
  - Train and employ citizens
  - Procure local inputs
  - Retain forex
  - Right to impose taxes
  - Compensation for social costs
  - Intergenerational equity

- **Investors**
  - Sufficient incentives to cover risks
  - Focused exploration
  - Faster payback
  - Employ skilled competitive labour
  - Procure competitive inputs
  - Repatriate profits
  - Stable political and tax regime

Obtain as much value as possible

Compensate for risks and maximise profits
C. Conflicting objectives

Attract investment

- Promote exploration & exploitation

Maximise value

- Compensation for depletion and environmental and social costs & Accelerate development

Incentives

- Taxes
- Other arrangements

Government
3. Implications for fiscal policies
A. Resolving the ‘conflicts’

• Promote realisation of rent

• Facilitate equitable distribution of rent

• Promote achievement of other development goals
B. Examples of fiscal instruments

- Resource rent tax

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Merits</th>
<th>Demerits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts for threshold rate of return on capital</td>
<td>Equitable</td>
<td>Complex administration</td>
</tr>
<tr>
<td>Rate of tax</td>
<td>Does not impact cut-off grade</td>
<td>Susceptible to leakages</td>
</tr>
<tr>
<td>Allowable deductions</td>
<td></td>
<td></td>
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<tr>
<td>Ring fencing</td>
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</table>
### B. Examples of fiscal instruments

#### Economic rents (Royalties)

<table>
<thead>
<tr>
<th>Type of instrument</th>
<th>Merits</th>
<th>Demerits</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue-Based</strong> (Per Unit / Ad valorem)</td>
<td>Simple, Easy to administer</td>
<td>Regressive, May fail to capture windfall rent</td>
</tr>
<tr>
<td></td>
<td>Suitable for regimes with low tax administration capacity</td>
<td>May increase mine cut-off grade (Reducing resource size &amp; mine life)</td>
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<td></td>
<td><strong>Stable &amp; predictable government revenue stream</strong> (Especially unit-based variant)</td>
<td>May collapse marginal mines (which still create socio-economic benefits)</td>
</tr>
<tr>
<td><strong>Profit-Based</strong></td>
<td>Midway between revenue-based and profitability</td>
<td></td>
</tr>
<tr>
<td><strong>Profitability-Based</strong></td>
<td>Progressive</td>
<td>Complex for weak tax administration regimes</td>
</tr>
<tr>
<td></td>
<td>May capture windfall rent</td>
<td>Unstable, Unpredictable revenue streams</td>
</tr>
</tbody>
</table>
B. Examples of fiscal instruments

• Customs duties

• Government equity

• Stabilisation
4. Optimising Government benefits
A. Achieving the right balance

- A minimum take

- Avoid high front end taxes

- Profitability-based taxes to capture windfall

- Incentives for contributing to development goals
  - Training, infrastructure development, linkages, etc.
B. Addressing leakages

• Tax justice
  • Allowable deductions
  • Transfer pricing
  • Mispricing
  • Tax avoidance
  • Tax havens
  • Etc.
C. Price discovery

• Auctions

• Minerals without reference prices
D. Managing the benefits

• Prudent investments
  • Poverty reduction
  • Development capital
  • Intergenerational equity
  • Local community benefits

• Revenue transparency
5. Concluding remarks
• The capacity factor

• Account for negative externalities (Environmental and social costs)
Thank you for your attention
References/Acknowledgements

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