Spotlight Session 2: Rethinking Tax Incentives in the Mining Sector in Africa

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ECA

Agenda

1. Introduction to mining tax incentives
2. Key findings from the report
3. Recommendations

What Are Tax Incentives in Mining?

A tax incentive is any **special tax provision**, granted to **mining investors**, that provide **favourable deviation from the general tax treatment** that applies to all corporate entities.

Where are they found?

In Legislation

- General income tax code
- Mining law
- National investment laws

In Contracts

- Mining contracts
- International tax treaties

What are Tax Incentives in Mining?

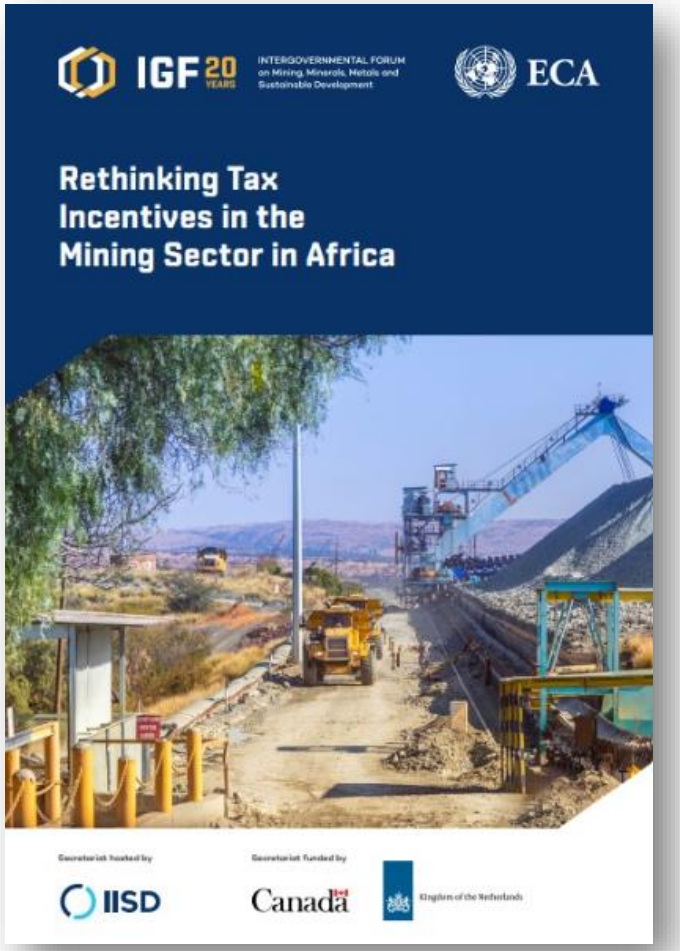
Cost-based vs profit-based incentives

Cost-Based Incentives	Profit-Based Incentives
• Investment allowance/credit, customs duty exemptions, VAT exemptions on import, accelerated depreciation, loss carry forward • Allow taxpayers to recoup their investment faster and to defer tax to later stages in a project's life, therefore not reducing cash flows during the initial critical years • Better suited to mining due to capital-intensive nature	• Income tax holiday, WHT on income, Export Processing Zone (EPZ), royalty- based incentives • Marginal mines benefit less than profitable mines from profit-based incentives • Associated with high redundancy rates and are ineffective at attracting investment

Key Findings from the Report

Tax incentives in the mining sector in Africa…

1. **…**have led to the loss of substantial mining revenues
2. …are less relevant to attracting mining investment
3. …have been a source of illicit financial flows from Africa
4. …have negatively impacted communities



1. …Have Led to Substantial Mining Revenue Losses

Cost-benefit analysis of tax incentives

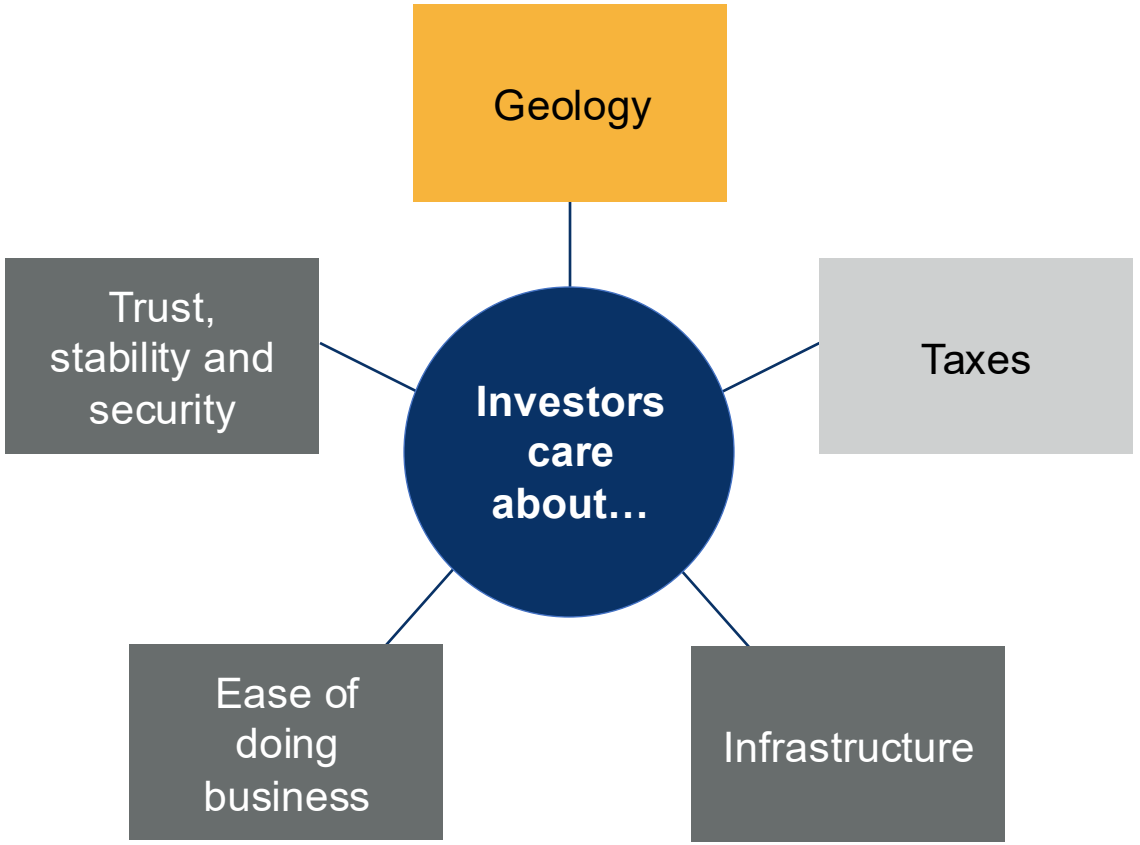
Costs	Benefits
• Revenue foregone • Administrative costs • Environmental, economic and social costs • Indirect costs: Economic distortions • Potential for corruption or abuse	• Amount of economic value the extractive operation brings to the economy (including multiplier effect) • Employment • Skills development • Government revenues

Takeaways

✓ Benefits should outweigh the costs for an incentive to be useful
✓ While it is easy to measure the direct cost and benefits of an incentive to a mining project, it is more cumbersome to measure the indirect costs and benefits as well as the resulting externalities

2. …Are Less Relevant to Attract Mining Investments

Factors investors consider in the decision to invest



3. …Have Been a Source of Illicit Financial Flows

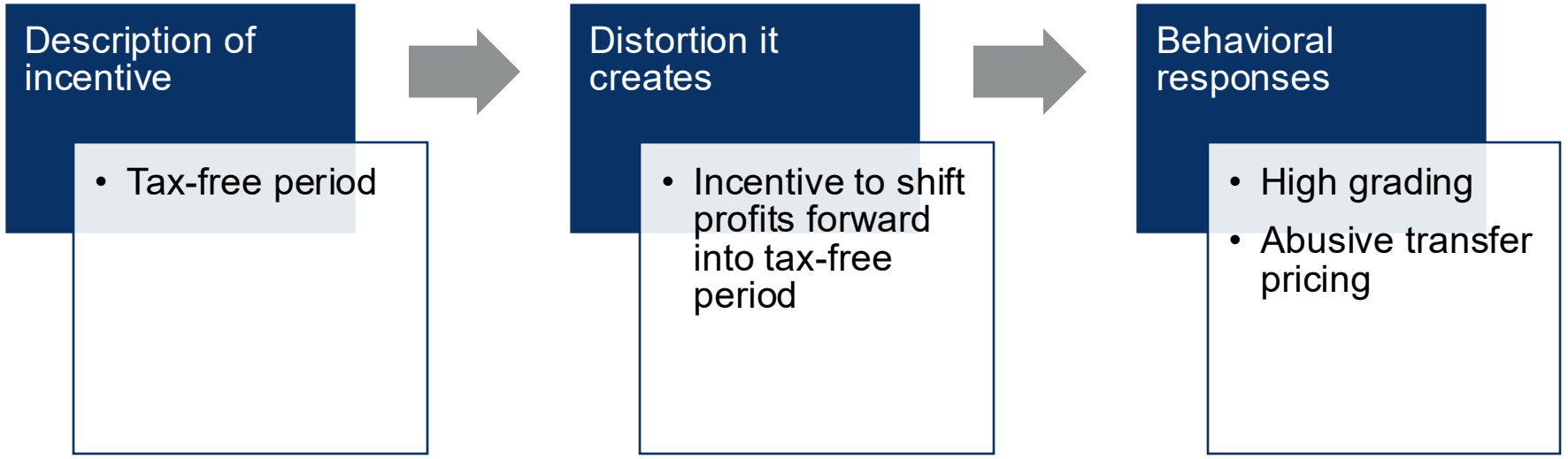
Risk of abuse

Income tax holiday	HIGH
Economic Processing Zone	
Royalty-based incentives	
Fiscal stabilisation assurances	
Withholding tax relief on interest, services	MEDIUM-HIGH
Cost-based incentives	MEDIUM
Import duty relief*	

*Import duty relief can also be low risk – most of the equipment imported will not crowd out domestic alternatives.

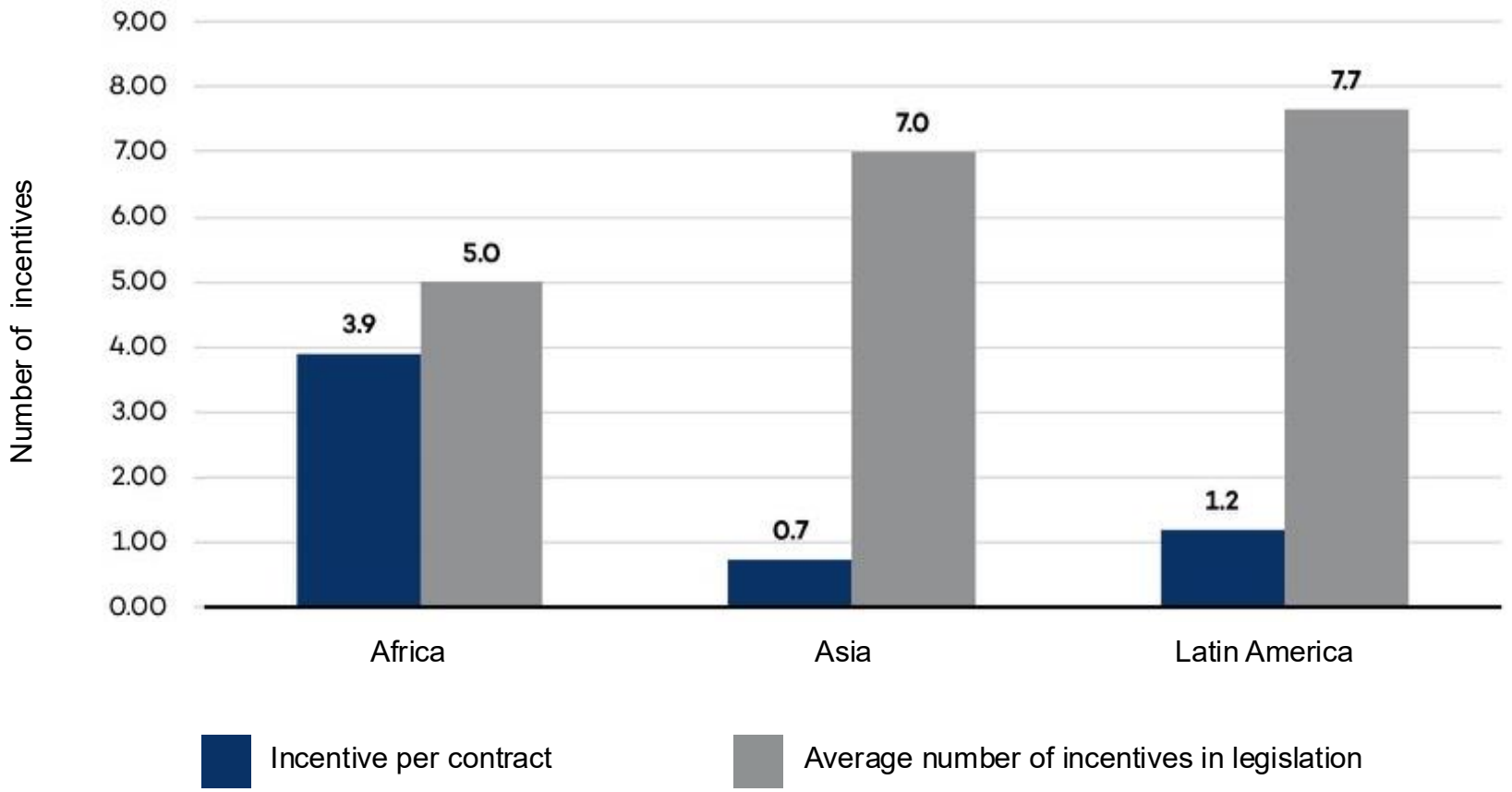
3. …Have Been a Source of Illicit Financial Flows

Example: Investor behavioural response to an income tax holiday



3. …Have Been a Source of Illicit Financial Flows

Lack of transparency in incentives given through contracts



4. …Have Negatively Impacted Communities

- Revenue forgone from tax incentives directly affects the communities (especially sub-national taxes)
- Domestic companies may be fully taxed, while foreign firms may receive tax benefits, creating a barrier to domestic investment, including artisanal and small-scale mining, which has the potential to benefit local communities directly
- Tax incentives can positively impact communities if they are targeted and linked to specific outcomes
    - They can be designed to encourage local hiring, training and technology sharing
    - They can be used to make investors adopt gender responsive programs

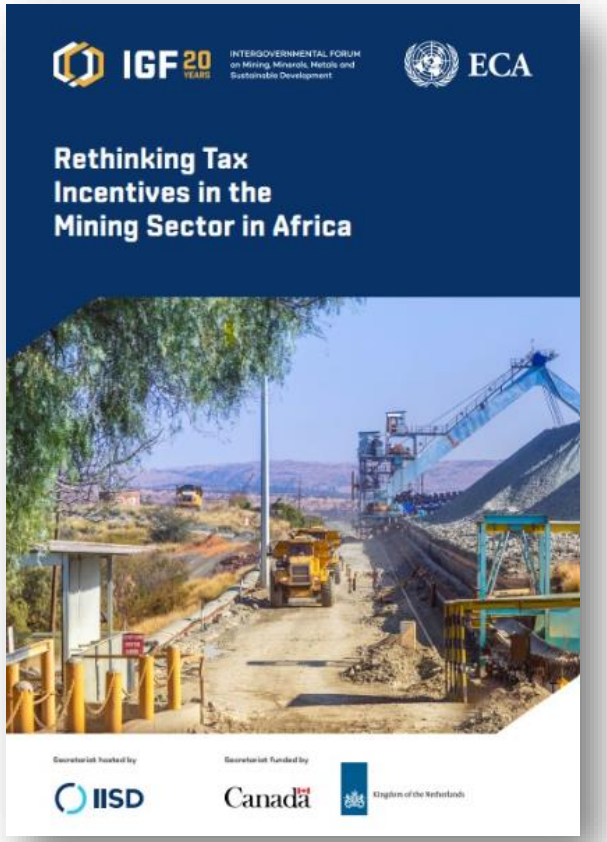
Reforming Mining Tax Incentives

Takeaways

- ✓ Countries should rethink their tax incentives and eliminate harmful ones
  - If offered, incentives should be time-bound, targeted, transparent and grounded in a demonstrable development need
- ✓ Governments should conduct regular cost-benefit analyses to evaluate effectiveness and strengthen accountability
- ✓ Regional coordination should be enhanced to curb harmful tax competition across the continent
- ✓ Countries should undertake a strategic review of tax policies (incentives) to align with the African Mining Vision, supporting value addition, local industrial development and sustainable growth

Download the Report

Rethinking Tax Incentives in the Mining Sector in Africa



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