TAXATION AND THE AFRICA MINING VISION:

Overcoming Challenges of Revenue Maximisation in the Extractive Sector

A case study of Uganda

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Introduction

Today, mining makes up a substantial part of many African economies with a potential to deliver significant development benefits when managed in a holistic and sustainable manner. Africa is a source of over 50% of mineral exports such as cobalt, manganese, chromium, diamonds and titanium to key commodity markets including the US, China, the Middle East and Europe. It also hosts 30% of the world's mineral and hydrocarbons reserves and supplies 12% of the world's total oil production.

In Uganda, the mineral sector plays a central role in the socio-economic development of our country. Uganda accounts for 4 percent of the world's production of pumice. The country also produces cobalt, gold, iron ore, kaolin, stone aggregates, lead, limestone, niobium (columbium), salt, steel, tantalum, tin, tungsten and vermiculite.

The sector provides employment, raw materials for local industries, export earnings and opportunities for new investments. Uganda's mineral potential is very high given the existence of a variety of geological formations, many of which have yielded exploitable mineral deposits. The geological maps produced established that there has been a significant increase in the mineral resource base known in the country including gold, iron ore, copper among others in the various regions of the country. A wide range of development minerals have also been discovered including asbestos, clay, diatomite, limestone, marble among others. Uganda also confirmed the existence of commercial Oil and Gas resources was in 2006. To date the country has (6.5) billion barrels of oil out of which 1.4bbl are recoverable and 500 billion cubic feet of gas in the Albertine Graben (UNCTAD, 2015).

However, the ratio of mineral rents to GDP averages across Africa has remained as low as 2.7%. For Uganda mining accounts for about 0.3 percent of the GDP. This has mainly been attributed to poor rent capture and Low value addition.

In a bid to improve the governance of minerals in Africa, the African Union (AU) Assembly of Heads of State and Government in February 2009 adopted a continental framework to promote mineral resource based development and structural transformation known as the Africa Mining Vision (AMV).

This paper discusses the provisions stated in the AMV for addressing the challenge of revenue management in the extractives sector. Drawing on examples from Uganda's taxation regime, the paper examines the existing taxation regime of the extractive sector in Africa. The paper explores the recommendations provided by the AMV on what needs to be done to improve the taxation regime in order to ensure that Uganda and other African Countries receive an equitable share of revenue from their mineral assets over the long term.

Africa Mining Vision

The Africa Mining Vision (AMV) is a policy framework which was created by the African Union in 2009 to ensure that Africa utilizes its mineral resources strategically for broad-based and inclusive development. The AMV's ultimate goal is "to enhance transparency, equity and optimal exploitation of mineral resources to underpin broad-based sustainable growth and socio-economic development".

An Action Plan to be implemented at national and regional levels was approved by Ministers in December 2011 and an implementation coordination centre, the Africa Mineral Development Centre (AMDC) was also established at the United Nations Economic Commission for Africa (UNECA).

The AMV's goal resonates with Agenda 2063, a "strategy to optimise use of Africa's resources for the benefits of all Africans." Agenda 2063 identifies the minerals sector as one of the fundamental sectors that could propel the achievement of the aspirations of Africa's growing population. This will necessitate Africa maximizing its revenues from the mining sector which hitherto has been a challenge.

Taxation of the extractive sector from a historical perspective

The mining sector has for long been an enclave with limited inter-sectoral linkage. Therefore, the sector has had a limited role in the structural transformation of African countries. During the colonial period, the benefits accruing from the extractive sector were appropriated and expropriated for the benefit of the empire. During the post- colonial period the mining companies through concessions controlled and externalized the mining resources.

Prior to the AMV, the role of taxation in the extractive sector was about attracting Foreign Direct Investment (FDI) with each country trying to offer more generous tax regimes. This has led to the race to the bottom and very low tax rates in many countries. In general most African countries have maintained the following tax regimes: No Value Added Tax (VAT), No import or export taxes (except SL), CIT rates reduced from 40% during 1970s/1980s to 30% or lower, extremely low withholding tax rates (between 10 and 15%) on dividends, loan interest and consultant fees compared to 20%-30% other mining economies, no windfall or additional profit taxes, very low royalties averaging around 3% and the inclusion of stability agreements/clauses. Governments also provided tax holidays.

In addition through tax avoidance and evasion

practices and other malpractices of the Multinational Corporations (MNCs), governments have lost tax enormous tax revenues. Thus most of the revenue has been captured and externalized by the Multi-National Companies.

Taxation and the Africa Mining Vision

The AMV provides for solutions to the existing challenges that inhibit the ability of countries to design and implement fiscal regimes that fairly balance the expectations of host governments and investors. The AMV focuses on how much is generated and how much of it stays in the economy. In addition to helping African Countries link mining to development and also minimise social and environmental damage, the AMV provides for the maximization of mining revenue. This is a departure from the narrow generation of revenue in a way that is consistent with attracting FDI.

According to the AMV Action Plan 2013; Outcome 1: "Optimize the share of mineral revenue accruing to resource rich economies"; provides for guiding questions to be taken into consideration while designing a fiscal regime that ensures optimal revenue capture, management and sharing. These include, inter alia:

- Does the fiscal regime deliver value for the country over the long term?
- Does the fiscal regime ensure that government receives a rising share of the revenues with rising profitability of mining activities? (progressivity)
- Does the fiscal regime guarantee appropriate minimum government revenue in all production periods and price cycles? (stability)
- Does the fiscal regime ensure robustness to changing circumstances (stability and flexibility)?
- Is the fiscal regime designed to encourage long-term investments?
- Does the fiscal regime limit opportunity or create loopholes for tax avoidance and evasion?
- Does government offer stability clauses? Are they the appropriate instruments to achieve the desired outcomes and are they limited in duration?
- Does the fiscal regime contain provisions for capital gains tax?
- Are the instruments of the fiscal regime easy to implement?
- Does the fiscal regime inspire confidence that the country is collecting what is due or owed and what is fair?
- Does the country have adequate administrative capacity and institutions with clear roles / mandates to collect all revenues?
- Does the country have oversight audit institution(s) and mechanisms?
- Does the fiscal regime facilitate and encourage mineral economic linkages?
- Does the country have a robust anti-corruption regime, including legally binding anti-corruption clauses?

The AMV also provides for a range of mineral fiscal instruments commonly used in the design of fiscal regime. These are divided into 2 parts i.e. direct and indirect tax instruments. The direct instruments include: Corporate income tax (plus withholding tax), Progressive profit taxes, Resource rent taxes; and Windfall profits tax, additional profit tax, super-profit tax. The indirect tax instruments include: Royalties ad valorem, specific/production volume, Import duties, Export taxes, Value Added Tax/Goods and Services Tax, Labour levies (skills, unemployment), Energy levies, Competitive bonus bidding, auctions

(e.g., hydrocarbons), Surface fees, License fees, Production sharing contracts , and State equity participation.

Overview of Uganda's Mining Fiscal Regime

While designing the fiscal regime, there is need for countries to ensure that they receive an equitable share of revenue from their mineral assets over the long term which varies with the entire mineral value chain: from licensing and contracting, to auditing of production, revenue assessment and collection, accountability and transparency of the use and management of revenues, from environmental protection to mine closure and related issue.

Uganda's fiscal regime has evolved over time. This has often been aimed at closing loopholes which have often been exploited by potential tax payers to avoid and evade taxes all in an effort to maximise revenue generation. The table below shows a brief highlight of Uganda's tax regime within the extractives sector in Uganda.

Fiscal Element	Current rates
Value Added Tax	• No VAT is charged on purchase of shares at the entry stage • Investors in the mining and petroleum exploration sector can register for VAT before starting to make taxable supplies. This facilitates claiming of input VAT paid on imported plant, equipment, machinery and supplies incurred during the development phase.
Stamp duty	• Stamp duty is chargeable at 1% on a purchase of shares. • 0.5% stamp duty on company formation, capital-raising activities.
Income Tax Act deductibles	• All expenditure of a capital nature incurred in searching for, discovering, testing and winning access to mineral deposits is tax deductible. • Losses can be carried forward indefinitely based on the licence area
Withholding Tax	• 15% withholding tax payable on interest. • Interest restrictions apply where debt equity ratio exceeds 1.5:1. • There is guidance on what constitutes foreign debt and foreign equity within the law.
Withholding tax on payments to non-residents in the mining sector	• Withholding tax of 15% or reduced rate depending on the Double Taxation Agreement (DTA) applies on payments by resident persons to a person outside Uganda. • Under the UK treaty the rate remains at 15%.
Withholding tax on payments to residents	• Withholding tax of 15% on interest and dividends.
Capital Gains tax (for indirect and direct disposal of assets)1	• Sale consideration taxed where the underlying asset/immovable property (includes mining rights) is in Uganda; • The capital gains tax rate is 30%.

Corporation tax	• Mining companies are subject to a Variable Rate Income Tax. • A specified formula applied for purposes of computing the variable rate income tax. • Derived rate is usually 30%. The tax rate is applied to the chargeable income to compute the corporation tax payable by the mining entity.
Royalties	• Royalties are payable on the gross value of the minerals based on the prevailing market price of the minerals. Examples of royalty rates are 3% for precious metals, 5% for precious stones and 3% for base metals and ores. • The Minister has, with the approval of the Cabinet, powers to waive any royalty payable on any mineral from a particular deposit.
Transfer pricing	• Taxpayers are required to maintain proper transfer pricing documentation containing the company details and transaction details, agreements and the pricing methodology used in determining the arm's-length price. • These provisions are often applied by the Uganda Revenue Authority where they are of the view that a non-resident person may be transferring profits from Uganda.
Tax filing and payments	• Self-assessment returns are due by the end of the sixth month after the end of the accounting year. Electronic filing is done for all tax returns. • Tax is payable in instalments based on estimated profits. • 50% is due by the end of the sixth month of the accounting period and the remainder payment is due by the end of the 12th month. Balance paid with the tax return
Tax assessments	• It is not uncommon for the tax authorities to issue speculative initial tax assessments. Assessments following a tax audit are generally more reasonable. Taxpayers can appeal to assessments issued by the tax authorities as provided for in the Tax Procedures Code Act 2014.

Source: PWC, 2015

1. *A mining right, petroleum right or petroleum information is considered to be immovable property for purposes of disposal.*

An Assessment of Gaps in the Fiscal Regime Governing Extractives in Uganda

The government of Uganda has over the years established measures in order to improve the management of revenue within the extractives sector by amending the tax laws and putting in place the Public Finance Management Act (2015) which also provides for revenue management in the petroleum sector. Despite these efforts, the government has not maximised the potential of revenue collected within the extractives sector.

Currently the fiscal regime ensures that government receives a rising share of the revenues with rising profitability of mining activities. However companies have often taken advantage of the provision in Section 38 of the Income Tax Act cap 340. This section provides that where, for any year of income, the total amount of income included in the gross income of a taxpayer is exceeded by the total amount of deductions allowed to the taxpayer, the amount of the excess, in this Act referred to as an "assessed loss", shall be carried forward and allowed as deduction in determining the taxpayers' chargeable income in the following year of income. This provision has been exploited by mining companies which declare losses every year which in the process are exempted from paying tax on their income.

Section 89B(2) Uganda's Income Tax Act cap 340 provides that where there is inconsistency in the taxation of contractors and subcontractor's income from petroleum operations, the provisions of part IXA of the Act and petroleum agreement shall take precedence over other parts of the Act. This is a stability clause which ensures that the terms in the Production Sharing Agreement (PSA) take precedence over those in the Income Tax Act. This ensures the incentives and fiscal terms in relation to income tax provided under the PSA are stabilised. Such clauses compromise the country's ability to adjust the fiscal regime to align with new economic realities or national development strategies.

Despite the fact that the tax regime provides for payment of capital gains tax at a rate of 30%, companies have often taken advantage of the loopholes in double taxation agreements signed by Uganda with other countries to avoid payment of this tax. A recent example is the case in which Heritage re-domiciled in Mauritius to take advantage of the DTA with Uganda to avoid crafting the sale as a sale of immovable property situated in Uganda which would be taxable in Uganda to employing a share sale which is taxable in the Mauritius which was the residence state and not Uganda.

While the Government of Uganda has made some efforts in streamlining the Corporate Income Tax (CIT) regime, CIT is susceptible to tax planning, especially among Multi-National Companies (MNCs) that have the resources to hire experienced tax managers. MNCs have attained some power to indirectly influence tax policy to favour their operations against the mutual benefit and revenue generation objectives of the government.

Uganda's investment regime is characterised by excessively generous tax holidays and exemptions within the investment code, tax laws, tax treaties as well as investment agreements. These have greatly undermined

revenue collections from the extractives sector in Uganda and the rest of the African countries and have greatly contributed to the "race to the bottom" between states as countries strive to offer the lowest tax rates.

Transparency in the extractives sector has also proved a challenge in Uganda. Despite the fact that the government has over the years committed to the Extractive Industries Transparency Initiative (EITI), its efforts to do so have declined over the years.

It is also worth noting that the tax administration unit; Uganda Revenue Authority has limited capacity to enforce the laws in place to maximise revenue collections from the extractives sector. This is in terms of staffing levels as well as the skilling. As a result, the government has failed to realise the full revenue potential from the extractives sector in Uganda.

Recommendations

To Government

The Government of Uganda should expedite national implementation of the Africa Mining Vision by aligning mineral sector laws, policies and institutions with its provisions and derivative policy instruments.

Governments should develop harmonized policies governing tax incentives within countries and across the African continent. These should lay out clear criteria under which investors in the extractives sector may benefit from tax incentives. Additionally, governments should be able to undertake periodic review of exemptions to ensure value for money. This will minimize the award of unnecessary incentives hence a reduction in revenue losses from the mining industry.

Tax authorities within the African Countries should implement the capital gains tax (CGT) on beneficial transfers of mineral rights, including offshore changes in control of the mother Company or ultimate controlling company. The reporting of such changes must be mandatory.

Uganda and other African countries should take a step to initiate negotiation of previously signed treaties that have loopholes which have been taken advantage of by investors in the mining sector to avoid or evade taxes. Additionally, countries should be able to get rid of or review the stabilization clauses within the laws, treaties and production agreements signed with investors.

Governments should also consider participation or gaining some equity control in strategic mineral companies especially those which are strategically important for the domestic economy i.e. iron/steel, cement and oil. In addition to ensuring increased revenue, government also ensures adequate supply and pricing of the minerals.

There is need for the government of Uganda to immediately establish a multi stakeholder group that involves the Government, companies and the full, independent, active and effective participation of civil society. The group should develop a work plan to oversee the extractives sector and validate the data and reports which are disclosed. This will help track revenue within the extractives sector and greatly contribute to improvements within the fiscal regime.

The Ugandan government needs to take a step to enhance transparency within the

mining sector in Uganda. One of the initiatives required of the African Union countries for implementation of the AMV is to join the EITI. To date, the government of Uganda is still making promises on joining the initiative but no action has been taken.

To Civil society

Active citizenship is critical to make leaders accountable to implement the Africa Mining Vision framework. Civil Society has a key role to play in organising and building consciousness of citizens on EITI and popularising the Africa Mining Vision. This will greatly contribute to the expedition of the AMV implementation in Uganda.

Civil society needs to engage the broader political governance on the importance of the African Mining Vision. The appreciation of the good mineral governance within the political circle will greatly contribute to improved policies that are in line with the Africa Mining Vision.

Conclusion

The Africa Mining Vision provides an invaluable blue print for governments to review their fiscal regimes to ensure maximum capture of their mineral revenues for mineral-based structural transformation. The recovery of the mining sector in Africa will require a shift in government objectives towards enhancing transparency, equity and optimal exploitation of mineral resources to underpin broad-based sustainable growth and socio-economic development, rather than a primary objective of maximizing tax revenues.

The recommendations if put to action can contribute greatly to an improvement in the governance of the mineral sector, specifically the fiscal regime hence promoting sustainable development for all.

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