**Funding Public Services - not Foreign Profits: Rethinking Tanzania's Mining Tax Incentives**

Since the publication of the Mbeki Panel report on Illicit Financial Flows from Africa, Public Services International (PSI) has been at the forefront in mobilizing trade Unions and Civil Society Organizations (CSOs) in the Africa and Arab Region to campaign to end illicit financial flows - and corporate tax avoidance.

This Research Report is a continuation of this work, with the goal of showing government leaders and our communities that there is an alternative to giving in to the whims and wills of foreign corporations.

This is the key to enabling governments to raise revenue domestically to invest in quality public services. The insufficient quality of public services and push for privatisation, often in the interests of big corporations, is in-large-part a result of inadequate public revenues.

Our campaign in Ghana, Nigeria, South Africa, Tanzania, Tunisia and Kenya has created a new generation of tax justice campaigners, enhanced our relationships with CSOs, produced useful research: all with the aim of shifting tax policies for the benefit of working people.

This report was commissioned to analyze the links between tax incentives in the Tanzania Mining Sector, inadequate public revenues and the wider issue of corporate tax avoidance and evasion.

The report finds that tax incentives provided to multinational companies are susceptible to abuse, and can lead to significant domestic revenue losses. The government must reform tax incentive policies to ensure the benefits of mineral resources in Tanzania produce create decent jobs and contribute to quality public services.

We need the entire Trade Union movement in Tanzania, in collaboration with CSOs, students and citizens, to lobby the Tanzania government for reforms of tax incentives in the mining sector.We have been able to do this with support from our partner, Friedrich Ebert Foundation (FES).

Sani Baba Mohammed, Regional Secretary, PSI Africa and Arab Countries

**Importance of Mineral Resources in Tanzania**

Tanzania is one the countries blessed with huge reserves of mineral resources. Economic minerals produced in the country include gold, diamond, coal, copper, silver, dimension stones, tanzanite and other varieties of gemstones. The major investors in the sector are foreign-owned multinational corporations (MNCs).

These include:

- Anglogold Ashanti (once named the world's most irresponsible company) which owns and operates the Geita Gold Mine in Geita;
- Barrick Gold from Canada-which (through Acacia Mining Limited) owns and operates the Bulyanhulu, Buzwagi, and North Mara mines in the country;
- Petra Diamonds which owns Mwadui Diamonds Ltd;

Tanzaniate One Mining Limited.The mining sector has huge potential to contribute immensely towards domestic resource mobilization, job creation, and sustainable economic development for resource-rich countries. Extraction of minerals should benefit the citizens of the country. But the experiences of different countries show this is often not the case. in Tanzania the sector has failed to contribute to GDP growth and revenue generationin the way many hoped for(URT, 2011). This paper examines this issue with a focus on tax incentives for, and job creation by, the mining industry.

**Why this study is important**

The fiscal policy objectives discernible from the Tanzania's Mineral Policy can be described as "maximizing government revenue while remaining attractive as a destination for foreign capital".

Equally important in the same Policy is "integration of the mining sector to the rest of the economy and maximizing local content (including employment of citizens in mining and related operations)". As is the case with many other developing countries, the sector is dominated by the activities of subsidiary companies of foreign-owned multinational corporations (MNCs). This is, in part,explained bythe unique characteristics of the industry, which include the need for heavy upfront capital investments; the long production period and risks involved, most of which would simply be beyond the reach of local companies. The context envisioned by this study therefore is that any strategic extraction of the Tanzinian mineral resources should involve: attracting substantive and meaningful foreign direct investment by the MNCs; adopting initiatives to ensure the MNCs' operations are well integrated into the rest of the economy with maximum local content; effectively taxing all relevant activities; and prudent use of the mineral revenues.

The proposition being implied by this study is that government revenue and decent jobs for citizens should represent the immediate benefits to Tanzanians; and that tax incentives, if any, should ultimately support, among other things, generation of decent jobs in the industry.

The key questions of the study are about the nature and impact of tax incentives offered to MNCs in the mining sector; and on the level and nature of employment offered to Tanzanians by the MNCs. The paper is informed by the use of secondary data (including from policy, legislation and related documents; as well as industry and revenue performance reports) complemented by interviews with key informants including personnel from organizations involved in the management of the mining sector, academia, trade unions, as well as independent professionals with insights into the workings of the industry and its taxation.

**Nature of the industry and applicable taxes**

The nature of the mining industry can be summed up in the words of the Natural Resource Charter as "the transformation from wealth in the ground to wider societal benefits…". The benefits to society from this industry are secured through, among other things, effective taxation of the relevant activities.. Boadway and Keen(2010), identify a number of features which make taxation of mining important yet challenging for many countries. These include: exhaustibility of the mineral deposits; high costs of investment and operations; long production periods; prospects for high profits and substantial government revenue; uncertainty regarding quantity of available deposits, quality of the deposits, accessibility of the deposits, remote locations, restoration and reclamation, reliance on sub-contractors and fluctuating prices. The important role of MNCs, which tend to possess superior information compared to host governments, is another challenge.

A variety of fiscal/tax instruments have evolved to attempt to address these challenges. These include: bonuses, royalties, resource rent tax, and government equity, export taxes and requirements to provide infrastructure (which emphasize the government's resource ownership); and corporate income tax (CIT), import duties, and value added tax (VAT) which emphasize the government's taxing power.

**Tax Incentives: Nature, Rationale and Challenges**

A tax incentive is a deduction, exclusion or exemption from a tax liability offered as an enticement to engage in a specified activity such as investment in capital goods for a certain period (Policy Forum et al., 2012). In the context of mining, a tax incentive can be defined as any special tax provision granted to mining investors that provides favourable deviation from the general tax treatment that applies to other corporate entities (Redhead, 2018). The incentives are offered in a number of ways and forms:

**Tax holidays**

A tax holiday is a tax-free period. The duration may vary from a single year to the entirety of the project. It may take the form of a complete exemption from tax-on-profits, or a reduced rate, or a combination of the two.Tax holidays are widely regarded as a poor form of investment incentive because: the precise nature and boundaries of the tax holiday are poorly defined; they create significant opportunity for abuse through transfer pricing and other profit shifting arrangements; and that the transition to regular taxation at the end of the tax holiday can be administratively complex.

**Stability Clauses in Mining Development Agreements**

Stability clauses sometimes freeze tax laws applying in particular cases. The law in effect on the date of an agreement must therefore remain available, along with any explanatory documents, in addition to current legislation. According to Calder (2014), stability clauses can cause many

problems for administrations. Their scope, including conditions for review, is sometimes unclear, and they may present an obstacle to much needed legislative reform to simplify and consolidate tax rules applying to different companies or to strengthen weak legislative provisions.

**Cost-based Incentives**

Cost-based incentives include investment allowances, investment tax credits, accelerated depreciation, and loss carry forwards, all of which decrease the cost of capital. The depreciation allowances may include an aspect of 'Capital Allowance Uplift'-which is an uplift allowed on unredeemed qualifying capital expenditure. These types of incentives are better suited to mining investments than tax holidays: they allow taxpayers to recoup their investments through appropriate deductions from their taxable income, or directly from their tax bill; they defer tax to later stages in a project's life and therefore do not eat into cash flows in the initial critical years when capital is most needed; and it is easier to anticipate the revenue cost of the incentive because it is based on the amount of investment. The risk associated with cost-based incentives is that investors may artificially inflate the cost of investment to increase the tax benefit. The recommendation is to clearly define the assets, and asset categories to which the cost-based incentive applies; and to monitor import duty concessions for mining imports.

**Import Duty Relief**

This type of incentives involves exemption of import duty on inputs and capital goods. Their drawback is that companies will tend to increase the cost of imported equipment and machinery procured from related parties so as to artificially maximize the cost-based incentives and deductions.

**Role of the Mining Sector in Job Creation**

For local communities, decent mining company employment should be safe, stable and fairly compensated, allowing employees and their families to plan ahead to improve livelihoods and financial security (Intergovernmental Forum on Mining [IGF], 2018). Unfortunately, what often happens is that, while wages might be high for highly-skilled workers such as engineers and managers, they can be very low for miners who are trained on the job and have limited formal education.[1] Issue areas include hours of work; job security; gender and women issues, occupational health and safety (Koyi, 2019). Stated policies in the mining industry proclaim commitment to principles of equality of opportunity in the workforce, although this is often not the case. (Macintyre, 2010, as cited in Koyi, 2019).

[1] https://www.ilo.org/global/about-the-ilo/newsroom/news/WCMS_187783/lang--en/index.htm, viewed on 30th April 2019

**Policy Implementation Strategies**

Strong policy frameworks and implementation strategy are necessary to promote quality employment and working conditions in the mining sector. IGF (2018) makes a distinction between: regulatory approaches, which result in 'stick' –based policies that rely on strong compliance mechanisms with the prospect of financial sanctions or loss of licenses; and facilitative approaches, which result in incentive-based, "carrot" policies that offer support and incentives for the development and employment of local workers. Examples of regulatory approaches include: mandated minimum percentages of local people employed in specific job roles; mandated requirements to conduct training of local workers or support the development of training facilities; visa restrictions on foreign workers; mandated succession/localization plans; and mandated reporting standards on how local content requirements have been achieved. For facilitative approaches, examples include: provision of financial resources or support for the creation of training facilities and/or streamlined training-to-employment/skills development programs; preference in bidding process on the basis of direct employment strategy; provisions that local people will be used "to the extent possible"; and fiscal incentives such as tax incentives, levies, and subsidized financing (See IGF, 2018). According to the same source, the country-specific examples for regulatory approaches include:

- Angola-which requires oil companies to hire at least 70% Angolan nationals;
- Ghana- prescribes minimum level of employment of Ghanaians (which increase over life cycle of the project), reserves unskilled labour for Ghanaians nationals, and prescribes percentages for maximum number of expatriate staff to total number of senior staff permitted;
- Nigeria-which requires companies to hire only Nigerians in junior and intermediate positions and prescribes a maximum number of 5% of management positions;
- South Africa-which requires companies to hire at least 40% local labour at all levels (at least 10% women in mining activities) and achieve minimum percentage of historically disadvantaged representation at management levels.

**Findings of the Study**

1. The reforms the Tanzanian government has taken in the last two decades have resulted in an improved mining regime.
    a. Formulation of Mineral Policy of 1997 and enactment of the Mining Act, 1998. This resulted in an increase in Foreign Direct Investment (FDI) in the mineral sector from US$ 1.3 billion to US$ 2.5 billion; commissioning of six large scale gold mines which produced an average of 50 tonnes of gold compared to less than 1 tonne, which was produced by small scale miners. In addition, a medium scale tanzanite mine producing an average of 1.4 million carats per annum was commissioned in 2002; increase in the value of mineral exports from US$26.66 million to US$1,003.21 million; growth of the mineral sector from 7.7% to 10.7% (at 2001 prices); increase in employment in large scale mines from 1,700 to 13,000

workers; increase in Government revenue from large scale mining from US$ 2 million to US$ 78 million; increase in the contribution of the mineral sector to the GDP from 1.4% to 2.7%. The most recent reforms, 2016 to 2017, resulted in increased royalty rates in some of the mineral sub-sectors; mandated local value addition to minerals; enactment of the Natural Wealth and Resources Contracts (Review and Renegotiation of Unconscionable Terms) Act, 2017, with enhanced parliamentary scrutiny of mining contracts

   b. The government is now entitled to a 16% share of mining companies' capital as free carried interest. The government is empowered to purchase a further 34% to bring its ownership to 50%. Prior to these reforms' government participation was provided for as a negotiable element.

2. According to the research underlying this report Tax Incentives provided to multinational companies are susceptible to abuse and consistently lead to revenue losses to Government.
   a. It identifies that from Corporate Income Tax, Value Added Tax, Import Duties to Stability clauses, Multinational companies may find avenues to avoid paying their fair share of taxes.
   b. For example, recent news stories indicate that the government of Tanzania is in conflict with Acacia Mining because the company is alleged to have engaged in tax evasion, money laundry and other acts of corruption. The stories include the company being charged with a tax bill of about US$190 billion.
   c. a study by the Chr Michelsesn Institute (CMI) in 2016 found that The Golden Pride Mine which was in operation for 12 years (1991-2013) only paid corporate tax for its last three years of operation.
3. The Natural Wealth and Resources Contracts of Act, 2017 provides for enhanced parliamentary scrutiny of mining contracts in Tanzania
4. The current negotiations led by the Trade Union Congress of Tanzania (TUCTA), to raise the minimum wage from Tsh.400,000 to Tsh750,00 face setbacks due to structural differences in terms of salary scales, between private-sector based and public sector-based employees of the mining sector.
5. The Occupational Safety and Health Authority (OSHA) is not adequately equipped to deal with cases and to enforce compliance. There is also the issue of insufficient prevention efforts for accidents and deaths; and inadequate (often mishandling) of treatment cases when accidents/diseases occur.
6. Access to information on the obligations of multinational companies in terms of employment creation and local content, vis a vis government incentivse, is not readily available. The website of the Mining Commission contains a standard format for detailed reporting on local content performance by the companies, but the reports are not available.
7. Most of the workers in the mining sector are not organized into Trade Unions, do not have access to permanent contracts of employment, and the sector generally does not have CBAs.

**Recommendations**

- The need to generate revenue domestically for the development of public services should be paramount. The government needs to position itself to optimize on the opportunity offered by the recent reforms to re-negotiate the fiscal terms of contracts to enhance revenue contribution of the sector.
- Increase transparency through public participation. Enhanced parliamentary scrutiny of contract terms and possibility for publication of specified terms of contract promotes transparency in management of the industry. To optimize on this, there is need for continuous training and awareness programmes for the relevant parliamentary committee(s) and the participation of Trade Unions and Civil Society Organizations (CSOs) in the scrutiny, monitoring and evaluation process.
- Review all existing statutory tax incentives through a cost-benefit analysis and remove those that are not beneficial. For example, government should re-assess the relevance of exemptions from import duties as one of the tax incentives, considering the risk of transfer pricing that such exemptions tend to fuel.
- The number of Tanzanian employees in mining companies must be established and made readily available to the public. The government needs to conduct a study to establish the required numbers of Tanzanian employees in mining companies.
- Local content regulations should be enforced. The requirement for companies to report their performance in local content is a good starting point. The government needs to adopt measures to ensure compliance by the companies with the requirements for employment of Tanzanians, with clear and published penalties for non-compliance. Compliance should include labour brokering companies who sub-contract for mining companies.
- Demand an increase in minimum wage and address structural challenges in pay. Continue with negotiations to address differences in the pay structure, between public sector-based and private sector-based staff of the mining sector to unlock implementation of the increased minimum wage agreed in the Trade Union Confederation of Tanzania (TUCTA)-led efforts.
- Workers in the mining sector must be organized into trade unions to ensure that workers have permanent working contracts and have access to collective bargaining agreements.
- Expand training and education institutions to integrate mineral, mining and natural resource management studies into higher education programs.
- Following in the steps of the Integrated Mine Technical Training Programme (IMTT), the government may adopt policy initiative to local government authorities to develop strategies to build local capacities for a broader context of local content that will facilitate indirect employment by the mining sector as well.
- Strengthen the capacity of Occupational Safety and Health Authority (OSHA) to provide adequate oversight on safety and health matters in the industry

- Overall, the link between incentives received by companies, public service provision, jobs for Tanzanians and general economic development need to be emphasized and enforced as one of the prerequisites for the incentives.
- Participate actively in the Regional/Sub-regional initiatives towards harmonization of tax laws and policies to curb unhealthy tax incentives and competitions.

**Conclusions**

The mining sector offers significant development potential for Tanzania, with huge reserves and a variety of mineral resources. There has been a long history of efforts and reforms towards ensuring sufficient contribution of the mining sector to the Country's social-economic development. The most significant attempts to improve the situation in recent years have come through the 2016 and 2017 reforms which have resulted into a visibly better tax regime for the mining sector, enhanced government control and parliamentary scrutiny. Evaluation of the revenue performance of the industry is indicative of adverse effects of the of tax incentives to attract foreign direct investment into the mining sector. Even though there are strong theoretical arguments in favour of tax incentives as a tool to attract FDI, their practical relevance needs to be reconsidered in light of the challenges they present to developing countries.

In the area of creation of decent jobs, the study shows, albeit with limited data, that there is policy and legal regime that is significantly consistent with leading practices in terms of prescriptions for local content and employment generation and, among other things, a minimum set of standards. However, reality appears to point to the existence of gaps in compliance with and enforcement of the policy and legal requirements regarding employment in the sector, wages, and work conditions.

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