CONCEPT NOTE

IMPLICATIONS OF THE EXTRACTIVE FISCAL REGIME TO THE TANZANIA ECONOMY: A CASE OF THE MINING SECTOR.

Introduction:

In Sub-Saharan Africa, tax revenues account for less than a fifth of GDP compared to a third of GDP in the Organisation for Economic Co-operation and Development (OECD) countries and the extractive sector represents a unique opportunity to enhance domestic resource mobilization. Globally, taxation is now seen as the most sustainable source of revenue for governments, with the potential to contribute to investments in basic services and to enhance the social contract between citizens and their government. The United Nations handbook (2017)[1] on Extractives Industries Taxation emphasizes that resource rich countries need to balance key issues like attracting foreign or domestic direct investment in the extractives industries, while ensuring the government receives an appropriate share of revenues in order to enhance the contribution of taxes to sustainable and equitable development. According to Bloomberg, 2018, the IMF recently noted that Sub-Saharan African (SSA) countries could increase tax revenue by an average of 5% of GDP if they reform their tax policies[2]. These could include removing harmful tax incentives and exemptions, renegotiating tax treaties that undermine the tax base related to the extractives industry, strengthening tax systems and regional cooperation to curb tax leakages and illicit financial flows that occur as a result of tax avoidance and evasion.

Tanzania is endowed with vast natural resources, predominantly with a lot of minerals (largely characterized with both small and large-scale operations)[3] which contribute about 5% of the country GDP. Several efforts have been made by the government to streamline the domestic laws in order to generate more revenue from the extractive sector. These include: the Mining Act 2010 and its amendments, license holders and contractors in the extractive sector are liable to pay taxes including corporate tax (30%), capital gain tax (30%), withholding tax especially on dividends (10%) and other taxes. Profits resulting from transfer or disposal of rights are also subject to taxes, which are collected by the Tanzania Revenue Authority[4].

Therefore, in order to understand the Mineral fiscal regimes and its implication in the Tanzania economy, background description of the mining fiscal regime is inevitable. Since early 1980's, Tanzania has been undergoing structural economic reforms (from international, regional and National initiatives) all aiming at promoting the country socio-economic development. Thus, triggering for legal and policy reforms in Tanzania such as the development of the National

[1] https://www.un.org/esa/ffd/wp-content/uploads/2018/05/Extractives-Handbook_2017.pdf
[2] https://www.bloomberg.com/news/articles/2018-05-08/tax-reform-could-boost-sub-sahara-revenue-by-5-of-gdp-imf-says
[3] https://www.tanzaniainvest.com/mining/page/4
[4] https://eiti.org/tanzania#tax-and-legal-framework

Mineral Policy of 1997, enactment of the Mining Act of 1998 and adjustments in the financial laws that regulate the Mining sector. Further, more reforms were also realized in early 2000s resulting to the enactment of the Mining Act of 2010 and thereafter the enactment of the 2017 Natural Resources Laws[5]. The main objective of the reforms was centered on creating a better conducive environment to encourage private investment in the sector including the foreign direct investments (FDIs). Furthermore, the role of the government has also been shifted from being sole owner/direct operator to regulator of private investment to having more state control in the natural resource management. With this, the mining sector has been targeted to grow to 10 percent of GDP from 1.5%. A strong, vibrant, well-organized private sector is thus intended to enable this process. In addition, the role of the CSOs will be critical in ensuring oversight and optimal utilization of these revenues generated from the extraction of oil, gas and minerals.

Despite the increase of the Foreign Direct Investment (FDI) in between 1998 to 2008,in 2009 the average annual growth rate of the mineral sector was 13.74% and value of mineral exports increased from US$ 26.66 million in 1997 (less than 1% of total exports) to US$ 1,003.21 million in 2007 (52% of total exports). The situation led to public outcry on the imperative need to increase its contribution through enhancing integration of the mineral sector with other sectors of the economy and having a fiscal regime which maximizes benefits to the national economy.

As a result, the objective of this research is to examine the effectiveness of the mining fiscal regime and its implication for the development of the Tanzania Economy as the country move towards middle income status.

a) Fiscal regimes governing the mining sector in Tanzania

Mining companies usually work to maximize profit generation whereas countries like Tanzania struggle to create a stable environment for settling taxes that can maximize revenue generation from the mining sector (NRGI, 2019)[6].

There are a number of fiscal instruments / terms that govern the compliance of tax and revenue management in the Tanzanian Mining sector. Among others including Royalties[7], Corporate tax[8], Expenditure on another licence[9], Value Added Tax[10], Depreciation allowance for capital expenditure[11], loss carry-forwards[12], withholding tax on dividends, Withholding tax on interest[13],

[5] The Written Laws (Miscellaneous Amendments) Act 2017[5]; the Natural Wealth and Resources (Permanent Sovereignty) Act 2017[5]and the Natural Wealth and Resources (Review and Re-Negotiation of Unconscionable Terms)[5] Act 2017. Mineral processing and its associated issues b. Mineral concentrates and the possible minerals to be found after mineral processing c. Introducing local content requirement which was not covered under the Mining Act before d. Introducing the integrity pledge to be taken by mineral right holders, that they will refrain from corrupt practices as well as pledge to support the country's campaign against corruption e. Introducing the Executive Secretary to the Commission instead of the Secretary to the Board which has been turned into a commission

[6] NRGI, 2019: Magufuli seeks the right balance for Tanzanian Fiscal Mining Regime

[7] Royalties are chargeable on the gross value of minerals produced under license at the rate of 5 per cent for uranium, gemstones and diamonds, and 4 per cent and 3 per cent respectively for metallic minerals including gold, and other minerals.

[8] Corporate tax is payable under the Income Tax Act, 2006 (Income Tax Act Revised Edition) at a rate not exceeding 30%.

[9] Expenditure on prospecting and mining operations in respect of another license area may, for the purpose of ascertaining taxable income, be treated as though it was expenditure
Incurred in respect of the mining licenses

[10] special relief is limited to cover only exploration and prospecting activities, while excise duty exemptions abolished

[11] is deducted at the rate of 100 per cent on capital expenditure for exploration and development.

Withholding tax on payment for technical services and on management fees, Customs duty on imports of mining equipment and supplies, Tax stability guarantee[14] and capital gains tax etc.

Despite the above efforts, the fiscal regime between 1998 up to 2015 appeared to hinder government efforts to collect more revenue thus the development of the 2017 fiscal regime (NRGI, 2019). With the new regime, the government is questioned for its ambitious agenda whereby if taxes will be set too low, it means that the government will miss out on much-needed funds for its ambitious development agenda while foreign-owned companies make excessive profits. Whereas putting them too high, puts the government under risk reducing investment thus impacting on low revenue anticipations for the country[15].

b) Transparency and Revenue Management in the mining sector in Tanzania

The government of Tanzania is committed to ensure that tax system is transparent, fair and that the capacity of TEITI[16] is enhanced to provide oversight within the extractive sector. Mining resources are also finite, and therefore, it is important that revenues generated are managed prudently and invested wisely into sustainable and long-term economic activities to improve the quality of people's lives. This has never been the case with mining revenues in Tanzania, though current reports from the government show that revenue collection in the sector has been enhanced. For instance, March 2019, the Ministry of Minerals had already collected over TZS 240 billion which represented 78.6% of the target. This increase (particularly from the sale of Tanzanite under Artisanal and Small-Scale Mining (ASM)) is due to changes in mining law, the introduction of mining markets and the building of the Mererani wall (famously known as UKUTA) leading to an increase of production from 147.7 to 781.2kg (An increase to more than 400 %) .Those records provide for the cover of three consecutive years – 2016 to 2018 and the first five months of 2019.

Whereas, during the 2015-18 period, persistent declines have been observed in revenue collection in the mining sector. On average, the government through TRA collected tax revenues to the tune of TZS 1,176 billion from the extractive sector according to TRA (2019), contrary to TZS 434.6 reported by TEITI in 2015/16 fiscal year (*2.7 times*). The TRA data is also lower than the total contribution of government revenue from the extractive sector in 2016 of TZS 13,914 billion (*3.12% of total government revenue and 11.8 times the one reported by TRA*) as reported by IMF in 2016. The differences between IMF and TRA data is based on the fact that TRA focuses on tax-related revenues while IMF considers all economic rents from the extractive sector (tax and

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[12] the losses may be carried forward indefinitely until recovered against income. For mining companies without MDA, losses can be carried forward for three years. After this period, those companies are subjected to 3% of the turnover

[13] tax on the interest on foreign loans is at the rate of 10 per cent and accrued interest is deemed a payment; therefore, withholding tax thereon is payable

[14] Special Mining License holder may enter into an MDA with the government and receive a tax stabilization assurance for a large investment project of over US$100 million for the full life of the project with review milestones every 10 years

[15] Ibid

[16] Tanzania Extractive Industry Transparency Initiative (TEITI) that is bound to increase transparency and accountability in the mining, oil and gas sectors in Tanzania

Non-tax sources). Further, mineral rents (*difference between value of production at world prices and total cost of production*) as a percentage of GDP was 2.95% in 2016.

c) Managing expectations

Extractive resources are finite. Therefore, it is important that revenues generated are managed prudently and invested wisely into sustainable and long-term economic activities to improve the quality of people's lives. Predominantly, Tanzania has been mining for more than 30 years and the revenues corrected have insignificantly contributed to the development vision, a lesson that should be taken as the country is rethinking to revamp its mining sector. Tanzanians continue to live in conditions of material poverty. Recent estimates put the number of those living below the poverty line at 12 million or a quarter of the population. Poverty has persisted, despite reports of relatively stable growth of the economy averaging 7%, for the last years[17].

Also, taking into account on the ongoing Tanzania- Barrick framework agreement, it proposes not only a 50/50 sharing of economic benefits that will be derived from jointly developed Mining Company[18] but also a settlement payment of USD 300 million. This agreement is made a center for scrutiny amongst sector stakeholders as it goes against the spirit of the current fiscal regime and the government ambitions to maximize revenues especially from the Mining sector in Tanzania.

The following shall be Lines of inquiry to be used to guide all data collection and analysis for the project and action research approaches.

Main lines of inquiry	Sub lines of inquiry
1. Fiscal rule and fiscal regimes in the mining sector	i. What is the status of the mining fiscal regime- how are the projections, reporting and policy choices? ii. What is the implication of the current mining fiscal regime for development of the country's economy? iii. What is the status of the on-going contract negotiations vs revenue projection? iv. What is the future for the Tanzania Mining sector?
2. Fiscal Transparency and Accountability	i. Since Tanzania has been mining for more than 30 years, how are revenues accrued from the mining sector collected and managed? ii. What are the challenges facing Tanzania in ensuring transparency and

[17] https://helda.helsinki.fi/bitstream/handle/10138/154641/Contemprorary%20concerns%20in%20development%20studies.pdf

[18] The Launch of Twiga Minerals Heralds Partnership Between Tanzanian Government and Barrick: https://www.barrick.com/English/news/news-details/2019/The-Launch-of-Twiga-Minerals-Heralds-Partnership-Between-Tanzanian-Government-and-Barrick-/default.aspx

	the impact to effective management of revenues from the mining sector? iii. Is there a clearly legal defined framework for the purpose of managing Revenues from the Mining sector? iv. What are the implications for the Non-compliance of the TEITA Act of 2015 regarding public disclosure of extractive contract specifically the Mineral Development Agreements?
3. Sustaining Competitiveness	i. The government is questioned for eroding value and diminishing competitiveness through the political economy while investors are faulted for not integrating projects into the economies of areas hosting extractive-FDIs, negotiating unfair deals, being merely opportunistic and evading tax Conflicting laws and uncoordinated institutions within the sector. How can this be managed for maximum impact?
4. For the purpose of investing for the future	i. For instance section 251 (a) (b) of the Petroleum Act, 2015 provides for the Government to cause for an establishment of a fund into which shall be deposited revenues derived from oil and gas. Nonetheless, there are no specific legislation that provide for the establishment of the fund to tap revenues generated from the mining sector in the country. How does the government plan to enforce this? ii. What is the risk associated with lack of such laws in the mining sector?

	balance between under and over-regulation in order to maintain legitimacy in the eyes of the public as well as secure future investments?