



# TRANSFER MISPRICING VIA MINERAL PRODUCTS

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IGF-OECD Collaboration  
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## Now to the outputs.

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- Transfer mis-pricing can also occur on mine outputs – particularly mineral products.
- Aim is to give a mix of theoretical TP foundations, and also practical examples in an industry sector that's important to many countries



## Our areas of focus

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- G20 asked us to look at how we could help developing countries address a big concern
- We responded that one part of the answer is to better understand the mineral product prices used by multinationals
  - Formulation, forces affecting prices
  - Economic context to transactions
- The work is on medium/large scale mines where MNEs are operating (not artisanal)
- Build a stock of knowledge and a **methodology**



## What's wrong?

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- Concern that mineral product producing countries not receiving an appropriate return from extraction and sale of mine products because of base erosion
  - Under-price mine products in related party transactions
  - (or over-charge for related functions – as noted)
    - So this is a subset of all the many and varied TP issues that might arise



# An example

Copper Concentrate Shipment	Arm's Length Price	10% Under-priced Copper	Copper under-priced, no gold declared
	\$m	\$m	\$m
Gross Value of Cargo FOB [A]	39.5	35.1	32.7
Production Costs [B]	22.5	22.5	22.5
Royalty [C]	1.7	1.5	1.4
CIT Base [A-B-C]		11.1	8.8
Company Tax Payable [D]		3.3	2.6
Total Revenue per shipment [C]		4.8	4.0
<b>Potential Revenue Loss Per Ship</b>		<b>-1.4</b>	<b>-2.2</b>
<b>Potential Annual Revenue Loss</b>		<b>-71.4</b>	<b>-112.3</b>





## Why is this happening?

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- Revenue authorities may still be building their sector knowledge and administrative capabilities
- Legal settings may be under-developed
  - (eg reporting, international information networks)
- The information needed to verify whether the transaction arm's length simply may not exist
- Authorities may not know what information they require or where to look for it
- The information may be difficult or expensive to obtain



# Essential building blocks in effective TP

## Transfer Pricing Analysis of Commodity Transactions

### TP rules, procedures and documentation

Revenue authorities need internationally consistent, comprehensive rules, internal processes to apply them effectively and documentation that enables effective analysis.

### Industry knowledge

Revenue authorities need to understand the industry value chain, commodity market functioning, the role of key price indices, common price adjustments and awareness of the role of financing.

### Information networks

Revenue authorities need effective domestic information sharing with other agencies, as well as an effective international network for information exchange.

# A SYSTEMATIC APPROACH





# Context

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- **Building an understanding of the mining sector is essential** to understanding potential base erosion risks and to applying transfer pricing analysis.
  - The key is to build that knowledge in a systematic way.
- **Here's one way: A 6-step methodology.**
  - Steps aim to sequentially understand the profile and structure of the domestic mining industry, the mines in operation and what they are producing.
  - Once the mining sector has been mapped, this allows administrators to identify key mineral products to be examined, as well as data that may be needed to assist in understanding the economic context of the industry.
- **As knowledge increases, info asymmetries narrow and revenue authorities should be able to use market pricing information more effectively.**
  - Naturally, you are at different stages of expertise with mining practices and mineral product markets, which will affect the amount of time needed for each step.
  - And it should help to narrow areas of dispute with taxpayers based on misunderstandings.



# Pricing work – build a foundation first

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## **6 steps.**

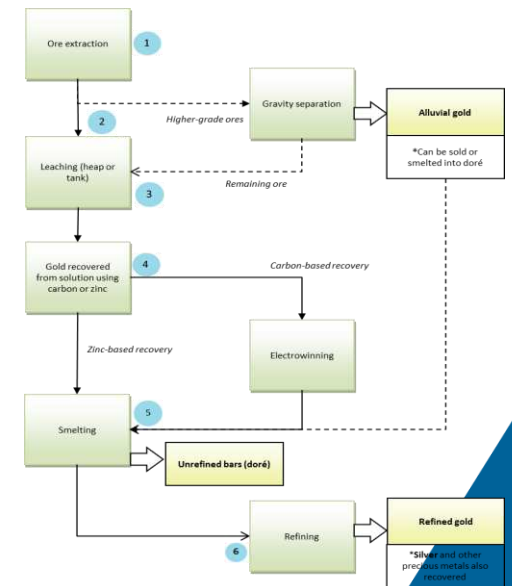
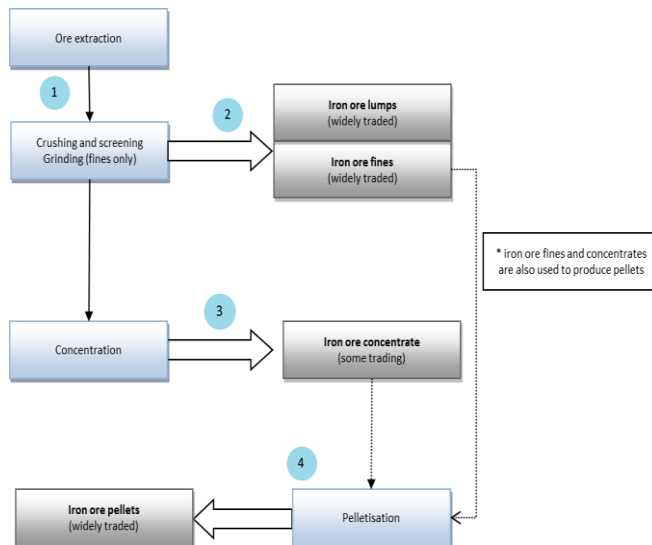
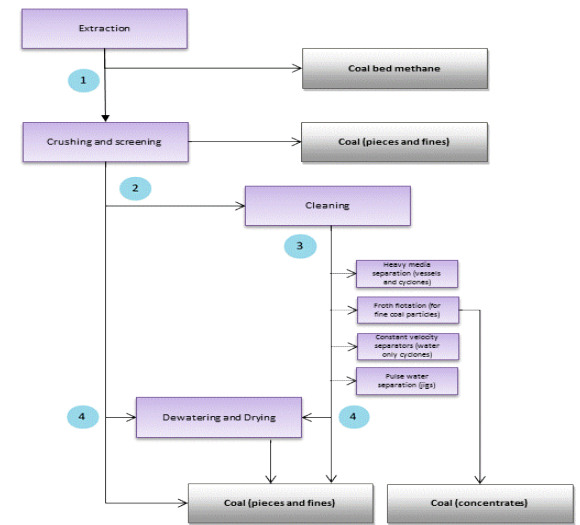
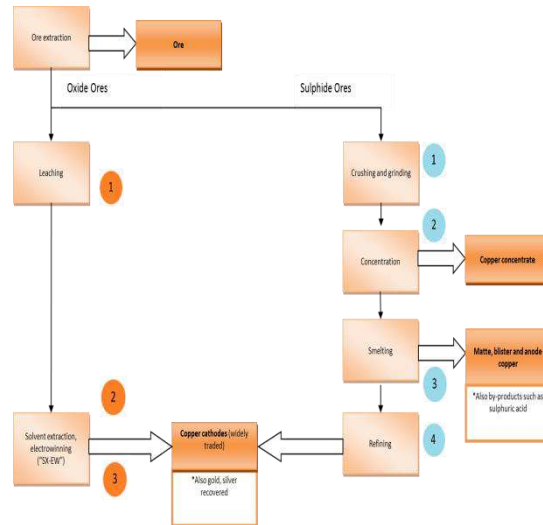
- 1. review each mine for how minerals are extracted and transformed to saleable products
- 2. identify in detail the actual products each mine produces and sells, and whether the processing facilities are also used by third parties under tolling arrangements
- 3. understand what those products are used for, what drives their prices and how they are traded internationally



## A foundation

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- 4. identify related party sales and understand the economic context to those transactions (including the functions, assets and risks of the related parties)
- 5. identify available information, analysis and data to review product sales transactions between related parties
- 6. devise approaches or methodologies that can address as many of those information gaps as possible





# Delivery

- This information is all contained in a toolkit
  - released by the Platform for Collaboration on Tax

<http://www.oecd.org/tax/toolkit-on-comparability-and-mineral-pricing.pdf>

## The Platform for Collaboration on Tax

### **A Toolkit for Addressing Difficulties in Accessing Comparables Data for Transfer Pricing Analyses**

Including a supplementary report on  
**Addressing the Information Gaps on Prices of  
Minerals Sold in an Intermediate Form**

International Monetary Fund (IMF)  
Organisation for Economic Co-operation and Development (OECD)  
United Nations (UN)  
World Bank Group (WBG)



# Some Issues Raised

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- Needless to say, understanding the mining industry is essential.
- Each mineral has unique characteristics and market structure.
- Pricing data is not available for every transaction, and some components of a price are more difficult to verify.
  - Eg products with opaque markets
- Other transactions may be embedded in prices (eg project financing, service fees), making TP analysis more difficult.
- This work has limits – elements of price that will be unique to the facts and circumstances of the transaction.
- Verifying prices best if it's done in a timely way.

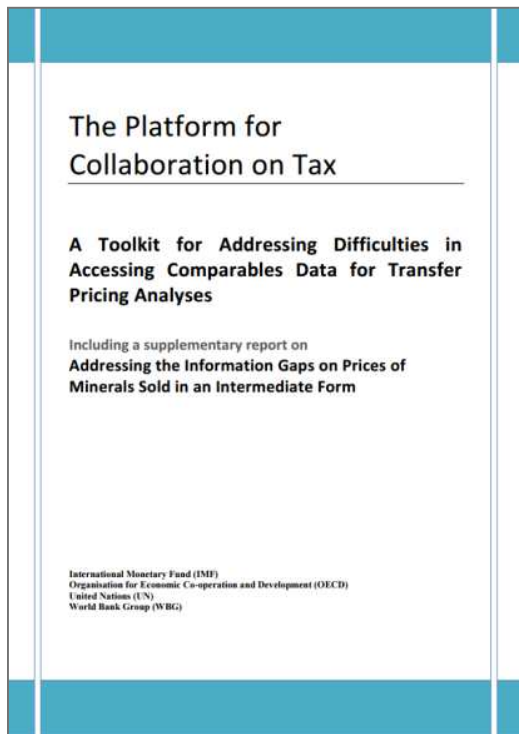
## *Broader issues*

- Product testing is fundamental
- Wider efforts to obtain information can greatly assist in revenue protection
- Broader revenue policies (eg incentives) may be undermining goals



# Where it's going

- Under the IGF-OECD project, we plan to extend the work



Bauxite Study and the challenges of opaque reference markets

Strengthening Govt Oversight of Mineral Value

Led by:





## Focus questions

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- What issues are you seeing?
- What approaches are working?
- How can we support your work?





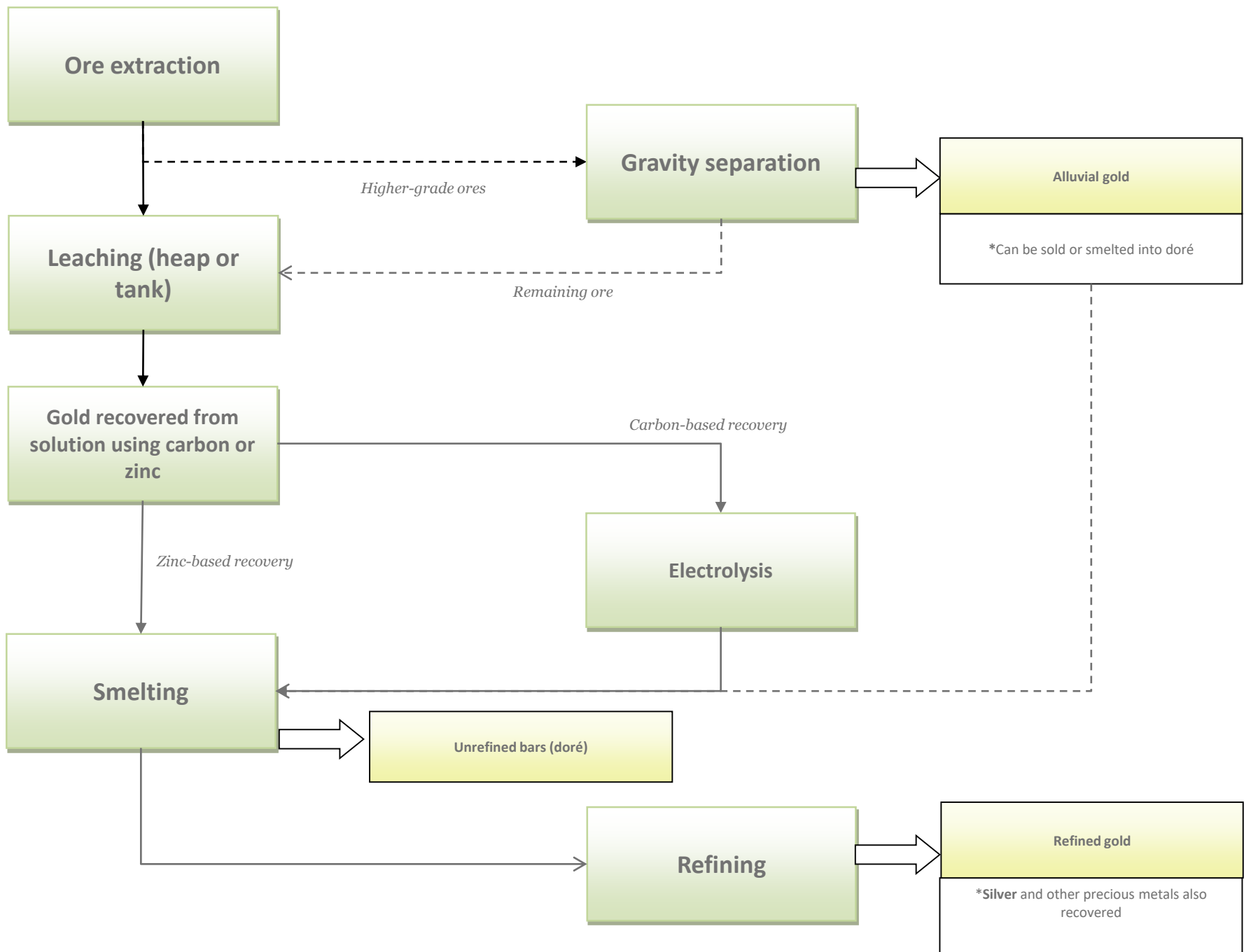
# THANK YOU!

Web: <http://www.oecd.org/ctp/tax-global/taxanddevelopment.htm>

email: [dan.devlin@oecd.org](mailto:dan.devlin@oecd.org)

# EXAMPLE CASE STUDY

## GOLD DORÉ





Source: Australian Mining Monthly

Alluvial gold



Doré – eg 85% gold, 10% silver, impurities

Source: bay area business centre

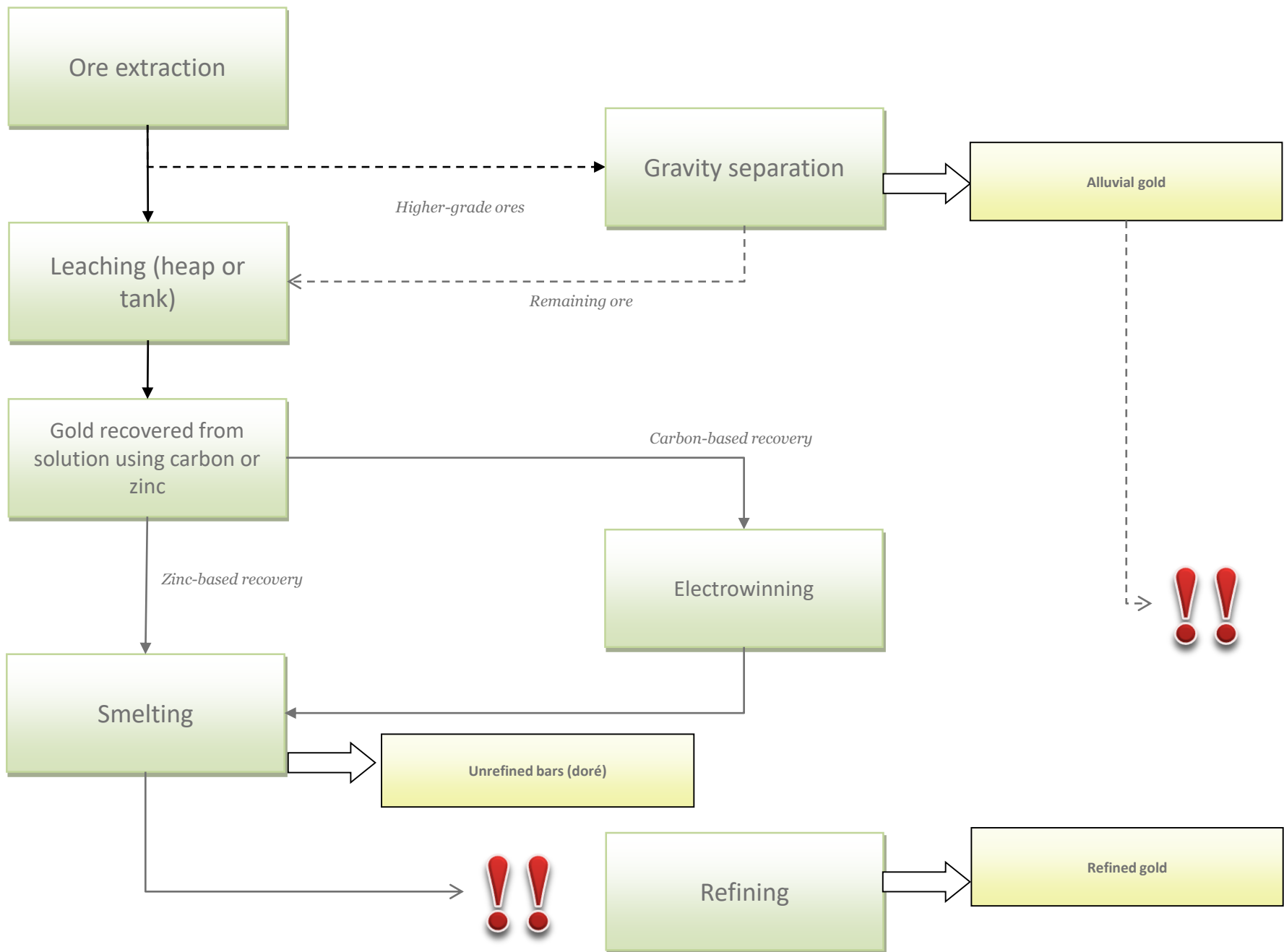
Refined gold



# Risks

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- High value metal..
- Gold can go missing during recovery processes
  - Early on: Gravity separated gold fragments
  - Later: Controls on doré bars – discrepancies between mine weight and refined weight
- Doré is mis-priced (sold cheaply to related entity abroad) or there are “handling/marketing fees”





# Gold Pricing

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- Doré an important export for many
  - requires refining to transform to pure gold, separate precious metals
- refinery will process the doré and sell the refined gold into global bullion markets
  - Might return to customer (eg breaking down a large gold bar)



# Gold Refining

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- An important third party against price manipulation. Most miners don't have their own refinery.
- Why? It's a competitive, low margin business.
  - Over-capacity globally
  - Quick turnaround to minimise price risks
  - Means they are very careful with weights/measurement
- Earnings are from:
  - Refining fee
  - Margin on price (paid to doré seller vs LBMA)
  - Bonus metals (grams not paid to doré seller)
    - Can be recovered at specialised facilities (especially Japan)
  - Special products e.g. retail coins
  - They will usually fully hedge price risks



# MEMORANDUM OF OUTTURN

Our Ref:  
 Date of Lodgement: /11/2011  
 Date of Outturn: /11/2011 10:32  
 Gold Price: \$ 0.00  
 Silver Price: \$ 0.00  
 Shipment No.:

Deposit Number	Receipt Wt(oz)	Official Weight	Assay Report Gold(%)	Silver(%)	Fine Gold Allowed(oz)	Fine Silver Allowed(oz)
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	Description: SR 4393-					
25790	624.85	620.20	77.150	20.490	478.006	125.808
	Description: SR 4395-					
25791	968.77	963.99	87.020	10.870	838.025	103.738
	Description: SR 4397-					
25792	906.04	902.94	83.200	14.870	750.495	132.924
-----						
	Total Fine Allowed				2066.526	362.470
-----						
To Metals Account:					2066.526	362.470
-----						
Buyer:						
	L/No:					
-----						
Less Charges: Refining					1,499.79	
	Assay				265.50	
	Environmental				81.91	
	Freight Dep No:25792				2,299.69	
	GST				0.00	-4,146.89
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					Amount Due To Refinery	
					USD	4,146.89
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## Brief comment on gold markets

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- Not a formal currency, but almost
- There's a global reference price
  - London Bullion Market Association (LBMA)
- But not all doré sellers get exactly the same price (commissions, fees etc)
- Implications:
  - Small regional differences may arise, but quickly eroded by arbitrage
  - pricing should not deviate too far from LBMA
  - No need for marketing