



IGF

INTERGOVERNMENTAL FORUM
on Mining, Minerals, Metals and
Sustainable Development

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OECD
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Ottawa, November 15, 2019

To Mr Pascal Saint-Amans,

The Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF) is grateful for the opportunity to provide comments on the OECD Inclusive Framework, Pillar One.

The IGF is the centre of excellence on mining and sustainable development and serves as a unique global venue for dialogue between its 70 member-country governments.

Since 2017, the IGF has had a program to address tax base erosion and profit shifting challenges in the mining sector, which is a collaboration with the OECD, African Tax Administration Forum (ATAF), and the Inter-American Centre for Tax Administrations (CIAT). The program aims to provide sector-specific solutions to some of the most pressing BEPS challenges faced by resource-owning developing countries.

Please find our comments on Pillar One attached herein.

Yours sincerely,

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Background

The Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF) is the centre of excellence on mining and sustainable development and serves as a unique global venue for dialogue between its 70 member-country governments.

Since 2017, the IGF has had a program to address tax base erosion and profit shifting challenges in the mining sector, which is a collaboration with the OECD, African Tax Administration Forum (ATAF), and the Inter-American Centre for Tax Administrations (CIAT). The program aims to provide sector-specific solutions to some of the most pressing BEPS challenges faced by resource-owning developing countries.

This submission is structured as follows: part one explains why source-based taxation remains the most appropriate model of taxation for natural resources; and part two examines the scope of the “Unified Approach” with reference to the mining sector.

Maintaining Source-Based Taxation for Natural Resources

1. The defining feature of natural resources is that they are finite and non-renewable. This creates significant scope for the existence of rents. However, these rents are location specific. That means that unlike the profits generated for Facebook, by Facebook users globally, the profits from mining are tied to a mine, which is a physical operation that is fixed to a specific location.
2. Moreover, natural resources, and the rents they generate, are owned by the people. It is a concept that is enshrined in international law, and in many constitutions. In this regard, taxes paid by extractive companies to the host state should be considered a *quid pro quo* for the right to extract a publicly owned resource, similar to wages charged by a worker for her labour.
3. Any attempt to reallocate taxing rights away from the resource-owning country – now, or in the future – would be unacceptable to host governments and their citizens. Source-based taxation remains the most appropriate form of taxation for natural resources – although not without its challenges.

Amount A

4. The mining industry should be excluded from Amount A for the following three reasons:
 - a. Mineral resources are location specific and publicly owned, making it inappropriate to shift taxing rights away from the source country;



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- b. With respect to the specific criteria for the new taxing right, mining is neither highly digitalised, nor consumer facing. While the use of digital technology in mining is increasing, it remains primarily a 'bricks and mortar' business; and, even if mines were operated entirely remotely, the business would still be underpinned by a location specific, immovable resource.
 - c. There is limited value generated from marketing intangibles. Mineral and metal prices are generally underpinned by market-based prices that reflect the physical characteristics of the mineral commodity, rather than any marketing intangibles.
5. The carve out should apply to the "mining industry" as defined as the full production supply chain – exploration, development, extraction, processing, transportation, and sales to end customer.¹ This would include construction of infrastructure related to mining activities (e.g. processing plants). All these elements should be subject to a carve out to ensure that taxing rights remain in the resource-owning country. However, ideally, this would be achieved through a well-drawn scope rather than a carve out, which may be interpreted in a narrow way, potentially leading to more confusion and disputes.
6. Possible minimal linkages to consumers should not alter the above results. There are some limited cases where mineral and metal commodities are sold directly to consumers. De Beers, for example, is involved in both mining rough diamonds in Southern Africa, and selling polished and cut diamonds directly to consumers largely in the US and China.² While this segment of the value chain is consumer facing, the other criteria for a carve out remain intact: location specific resource, and limited use of digital technology and marketing intangibles relative to other sectors of the economy. Moreover, the value of the consumer-facing sales are likely to be a relatively small proportion of total sales, making it a less significant part of the value chain.³ For these reasons, plus the need to prioritise ease of administration, a carve out should apply to the whole mining value chain.
7. In determining the scope of a carve out for mining, the question arises whether commodity trading should be included. IGF's view is that commodity trading is distinct from mining, and should be excluded from a carve out for the following reasons:
 - a) Unlike mining, where profits are tied to an immovable resource, commodity trading has no direct linkage to the underlying physical asset. Of the four major commodity traders – Glencore, Trafigura, Gunvor, Vitol – only Glencore has mining operations.⁴

¹ Note that customer is different to consumer

² De Beers does not undertake the cutting and polishing of its diamonds. Instead it sells all its rough diamonds and buys back polished and cut diamonds (not the same ones) for retail sale.

³ De Beers generated revenue of only \$0.2bn in 2018 from Other Diamond Sales (which is how it classifies its sales of polished diamonds) compared to De Beers total revenue of \$6.2bn (mostly from the sale of rough diamonds). See <https://www.debeersgroup.com/reports/insights/the-diamond-insight-report-2019>

⁴ Anton Lof and Magnus Ericsson, (2019) *Commodity Trading: understanding the tax-related challenges for home and host countries*, International Institute for Sustainable Development (IISD), pg.27-28.



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- The other traders are limited to buying the product from the mine in the source country, and on-selling it to customers.
- b) Traders are primarily logistics companies that use financial markets to fund their operations and limit price risks acquired through their operations. In this sense, they achieve scale without mass largely through intangibles such as trading algorithms and software.
8. Although trading is distinct from mining and should be excluded from a carve out, it is also not consumer facing, and the relevant intangibles relate to trading not marketing. On that basis, trading may be out of scope of Amount A irrespective of how the carve out for mining is defined. The same is true for any trading activities done by mining companies.⁵
9. The issues highlighted in paragraphs 7 and 8 further underscore the potential pitfalls of excluding sectors through carve outs. Careful drafting of what is included, is preferable to exclusions or carve outs, which in international law disputes are always read down in a minimalist way.

Amount B and Amount C

10. Amount B is described as being a fixed return in respect of an assumed “baseline” level of marketing and distribution activity in the market jurisdiction (the jurisdiction of the consumer). However, in cases where the local revenue authority is of the view that the level of local activity is higher than the baseline, it would have the ability to claim a higher amount (based on transfer pricing principles) under Amount C. Hence, Amounts B and C are considered together.
11. The carve out for mining under Amount A should also apply to Amount B. This is for two reasons. The first is a threshold issue: assuming that Amount B is premised upon Amount A, it has already been established that there should be no new taxing right in the market country in the case of mining, hence a minimum return cannot be assigned.
12. Secondly, even if Amount B is found to be distinct from Amount A, and hence scope remains an open question, it would be inappropriate to reward the marketing function using a fixed return on sales because of the limited use of marketing intangibles in the mining sector. This view finds support in the dispute between the Australian Tax Office (ATO) and BHP, where the ATO successfully challenged BHP’s use of a commission on sales as a basis for allocating profits from the sale of Australian iron ore to its marketing hub in Singapore.⁶ The ATO has since determined that a return on operating costs is an

⁵ Some large mining houses also have a trading arm. However, as distinct from traders, these companies derive the majority of their revenue from the sale of their own production.

⁶ IGF appreciates that offshore marketing hubs are generally located in an intermediary country and not the market country, which Amount B is focussed on. However, the example is relevant insofar as it illustrates



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appropriate basis for remunerating offshore marketing hubs, and that anything above 100 percent mark-up on the hub's costs is a transfer pricing risk and liable to audit.

13. There are two issues with respect to mandatory and binding arbitration. First, the OECD should clarify that its intention is not to invite taxpayer initiated binding dispute settlement.⁷ This would be akin to bilateral investment treaties, where the experience of extending investment treaty rights and obligations between states to direct private enforcement has been that governments are left with much less control over the interpretation and application of treaty provisions. Second, from IGF's perspective, there is a lack of consensus amongst its member countries on whether mandatory and binding arbitration is a good approach. Some members are strongly opposed on the basis that it infringes unduly on their sovereignty.

that remunerating marketing functions based on return on sales is problematic irrespective of whether the function is located in an intermediary country, or market country.

⁷ Para 30 states "Any dispute between the market jurisdiction and the taxpayer over any element of the proposal should be subject to legally binding and effective dispute prevention and resolution mechanisms."