



## BEPS in Mining Case Study: Boosting Zambia's revenues from the sale of manganese and copper

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Zambia, located in southern Africa, is well-known for its abundant natural resources, primarily copper, coal, cobalt, emeralds, hydropower, lead, gold, silver, uranium, and zinc. The country is especially famous for its copper, which has largely been credited as the source of Zambia's improving economic growth figures in recent years. It is an essential export good for the country, with raw and refined copper making up approximately three quarters of its exports by value in 2017 (Observatory for Economic Complexity, 2020).

Despite this track record of improved economic growth and Zambia's reclassification as a lower-middle-income country nine years ago, the country has a difficult history of severe income inequality (World Bank, 2019b). Moreover, the limitations it has faced in raising mining sector revenues

are compounded by high levels of government expenditure and an accumulation of debt that, as of 2018, was equal to 78% of the country's GDP, further constraining public budgets (World Bank, 2019a).

Collecting the right amount of revenue from the sale of copper and other minerals is a crucial step for Zambia to alleviate its fiscal pressures and make more public resources available to achieve its national development priorities. This case study outlines some steps that Zambia has taken to improve revenue collection from the mining sector, with support from the African Tax Administration Forum (ATAF), the Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF), and the Organisation for Economic Co-operation and Development (OECD).

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The training on transfer pricing risk assessment in the mining sector was very useful and practical, reflecting actual issues encountered by auditors.

**Ignatius Mvula, Head of the Mining Audit Unit, Zambia Revenue Authority.**

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## Key Outcomes

- We (ATAF, IGF, and OECD) helped Zambia improve its methodology for valuing manganese ore.
- We worked with Zambia to revise their transfer pricing rules to prevent the profits from the sale of base or precious metals from being shifted overseas to low-tax jurisdictions.
- We provided assistance in transfer pricing risk assessment and on Zambia Revenue Authority (ZRA) audit cases.

This support comes from our BEPS in Mining Program, which takes a whole-of-government approach to address critical mining revenue issues. We are working with Zambia's Ministry of Mines, Ministry of Finance, and the ZRA in all program activities, including trainings for government officials.

## Addressing Abusive Transfer Pricing

In mining, government revenue is normally generated by levying royalties, income taxes, and some indirect taxes. The amount of royalties and taxes depends on the price received for the minerals produced—normally, the sale price or a relevant quoted price—and the volume of minerals sold. It is therefore critical that governments know how minerals are priced and measured.



Lee Corrick (ATAF/OECD) and Alexandra Readhead (IGF) deliver training on transfer pricing in the mining sector in Lusaka in 2020.

In the case of Zambia, some large-scale mining companies often sell their copper directly to affiliated smelters in Zambia, refineries, or an associated marketing or trading hub, often located in a low- or no-tax country. These hubs are often created for the sole or primary purpose of avoiding tax, meaning that companies may deliberately under-price the related party export sales. This allows them to pay less tax in the country where they have extracted these minerals and artificially shift their profits to foreign related parties, usually in a low- or no-tax jurisdiction. This is often referred to as abusive transfer pricing.

While the challenges of addressing such profit shifting are significant, some key improvements have already been seen in Zambia. The use of reference pricing under a type of sixth method provided in Section 97A of the Zambia Income Tax Act and the use by the ZRA of third-party sales agreements between the foreign related party and end customers can help Zambia attack hub structures and ensure accurate compensation for their copper. Accessing such agreements in the past had proved difficult, given the lack of a legal basis for requesting them from the local mine and their affiliates unless there was a double tax treaty with the marketing hub jurisdiction that allowed Zambia to request information.

We worked with Zambia to help them enhance the provisions of Section 97A of

their transfer pricing rules relating to the extractive industries on the application of the reference price. This resulted in empowering the ZRA to substitute the third-party sales price for the publicly quoted price where it is higher. This will further discourage taxpayers from using hollow hub structures to avoid paying tax in Zambia. Additionally, the new rules have given the ZRA powers to request third-party sales agreements from foreign related parties and, thus, detect potential under-pricing of mineral exports.

## Valuation of Manganese Ore

Another challenge is the valuation of manganese ore for export purposes and, to some extent, for mineral royalty purposes. We worked with the ZRA and made improvements in the valuation of manganese ore, leading to fewer disputes and increased revenue.

We have also assessed transfer pricing risks for a few flagship mining projects, which will help guide the ZRA in selecting which cases to audit. This ensures that limited audit resources are prioritized according to

the highest risk areas and most material financial flows. An inter-agency Mineral Pricing Working Group has been created to leverage the specialized expertise of different branches of government and bring them together in one platform. This group will build on the mineral valuation training we provided and continue working alongside IGF experts to develop an internal risk assessment framework for pricing specific minerals.

## References

- Observatory for Economic Complexity. (2020). *Zambia*. <https://oec.world/en/profile/country/zmb/>
- World Bank. (2019a). *The World Bank in Zambia*. <https://www.worldbank.org/en/country/zambia/overview>
- World Bank. (2019b). *Zambia Economic Brief: Leveraging renewable natural resources for a sustainable future*. <https://www.worldbank.org/en/country/zambia/publication/zambia-economic-brief-leveraging-renewable-natural-resources-for-a-sustainable-future>

These insights came from desk research and trainings by the IGF, OECD, and ATAF for the [BEPS in Mining Program](#), which addresses tax base erosion and profit-shifting in the mining sector.

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