

There is no such thing as a safe haven: super taxes are a risk for the mining community across Latin America

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The commodities 'super cycle' and the global financial crisis have collided to make special mining taxes and royalties more attractive to government policy makers than at any time for a generation.

While it is true that the former Australian Prime Minister was forced from office for attempting to introduce a special mining tax, his successor is on the verge of pushing through a version of the same bill which would tax mining companies on 'super profits' (defined as ROI >7% above the yield on long-term government bonds) at a rate of 30%. Australia is not alone. In the past year South Africa, Tanzania and Indonesia have all introduced some form of special taxes or royalties on the mining industry. Perhaps most surprisingly, Chile has introduced a bill which will increase its royalties on copper to 14%.

The Chilean case is particularly interesting. According to the 2010/11 annual survey of mining company executives carried out by the Frazer Institute, Chile is the only jurisdiction outside North America that consistently ranks in the top 10 of friendly jurisdictions from mining companies. The Latin American country was placed at no.8 by the Frazer Institute, reflecting positive sentiment that dates back to the introduction of a favourable FDI framework in the late 1970s. Its closest regional neighbours were Mexico (no.35) and Colombia (no.40).

The new royalties regime introduced by the Chilean Government is less favourable than the 'Nazar' version of the Mining Act which looks set to be introduced by the Honduran Congress in the next six months : Honduras being ranked by mining executives as 79 of the 79 jurisdictions surveyed by the Frazer Institute. What explains this disconnect?

Firstly, tax is not everything. The Frazer survey ranks jurisdictions according to a range of factors, including the certainty and predictability of the regulatory/legislative framework, the nature of environmental regulations, labour issues indigenous land claims, and other social-economic factors that help to determine whether there is a 'social licence' for mining. But even taking this broad range of factors into account does not explain the fact that Chile is ranked no.8 and Honduras is ranked no.79. The fact is that things changed - the fiscal environment in Chile worsened and its 30 year track-record of friendly policies did not provide a reliable guide to the future.

The lesson for the mining industry is that there are no safe havens. For each new generation of stakeholders, for each new political or economic cycle, the arguments must be made afresh: the mining industry plays a huge role in economic and social development, particularly for remote and rural regions of the country where it often represents the only truly sustainable means of growth. Yes the industry should pay its 'fair share' of tax but a balance must be struck between short-term and long-term tax yields and there is a tipping point at which higher rates of taxation will result in lower yields.

The mining industry must play an active role in the public policy debate about what paying its 'fair share' of tax really means. It must help to educate stakeholders about how the industry operates, and the point at which marginal tax rates will create disincentives for new investment and job creation. It must carve-out a constructive role working with the government to attract new foreign investment, jobs and tax revenue. Fundamentally it must realise that there is no such thing as a safe haven when it comes to political risk, regardless of a jurisdictions track-record or a governments positive noises.