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DMR BRIEFING: MINERAL BENEFICIATION

Portfolio Committee on Trade and Industry

Parliament, Cape Town
17 October 2014



mineral resources

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Mineral Resources
REPUBLIC OF SOUTH AFRICA

Presentation outline

- ❑ Introduction
- ❑ State of and the impediments to the implementation of the mining charter
- ❑ Transfer pricing and its impact on the economy
- ❑ The Implementation of the MPRDA, especially wrt Sections 26 and 100
- ❑ The status of implementation of the minerals beneficiation strategy
- ❑ Mechanisms in place to address impediments to the minerals beneficiation strategy
- ❑ Concluding remarks

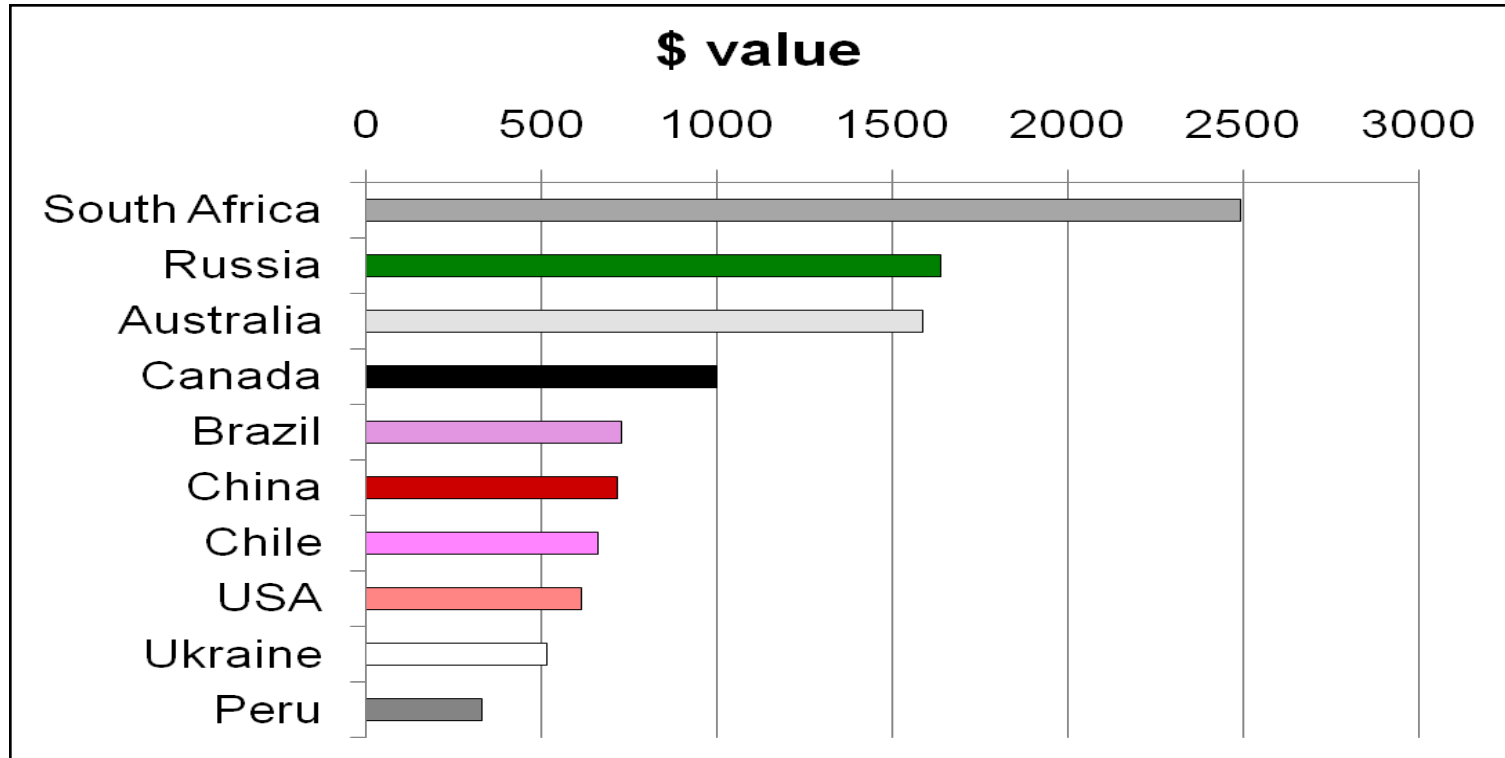
Introduction



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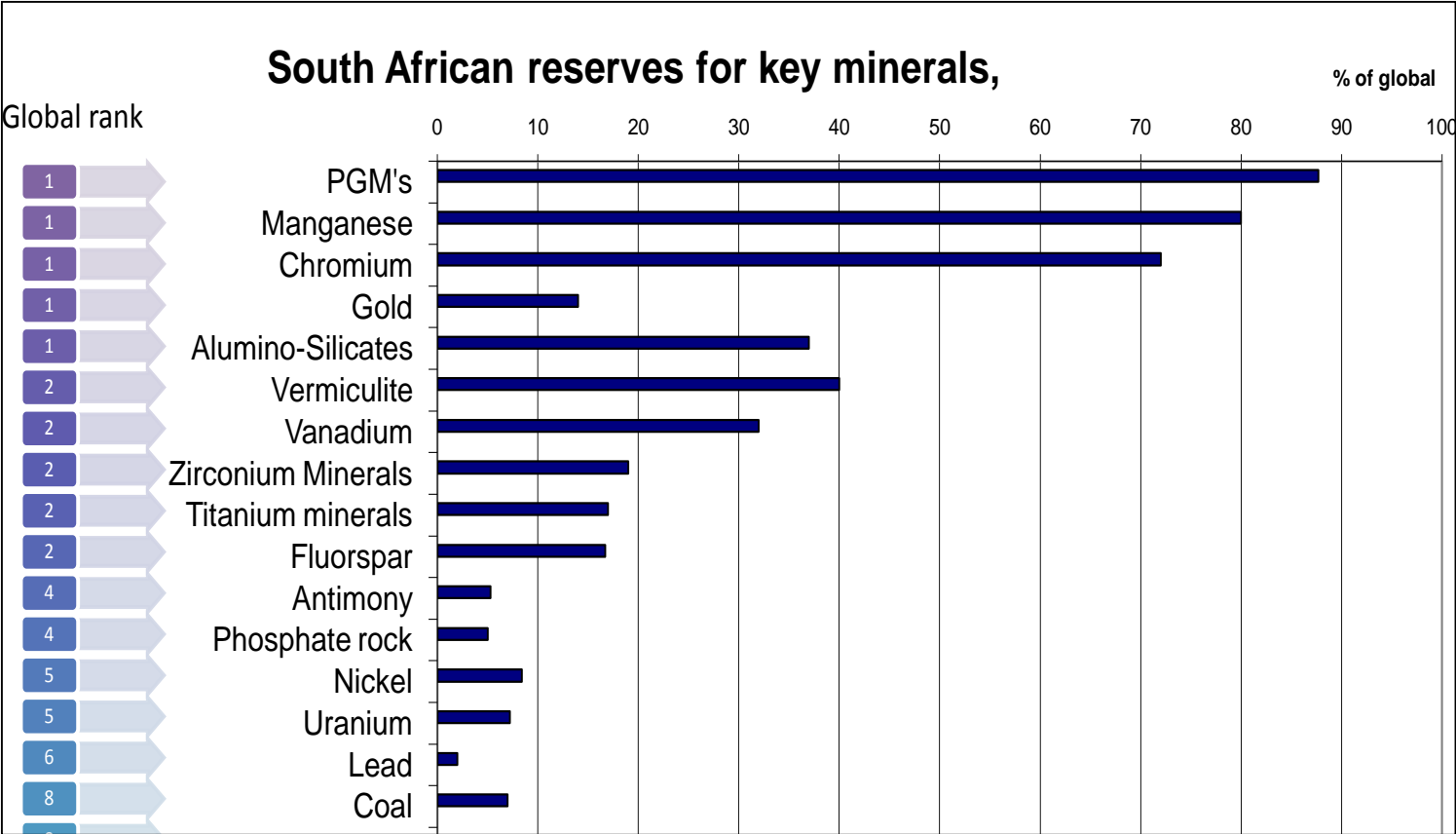
Comparative non-energy in-situ mineral reserves valuation



In-situ value estimation excludes energy commodities (coal, uranium, thorium)

Source: Citibank Report, 2010

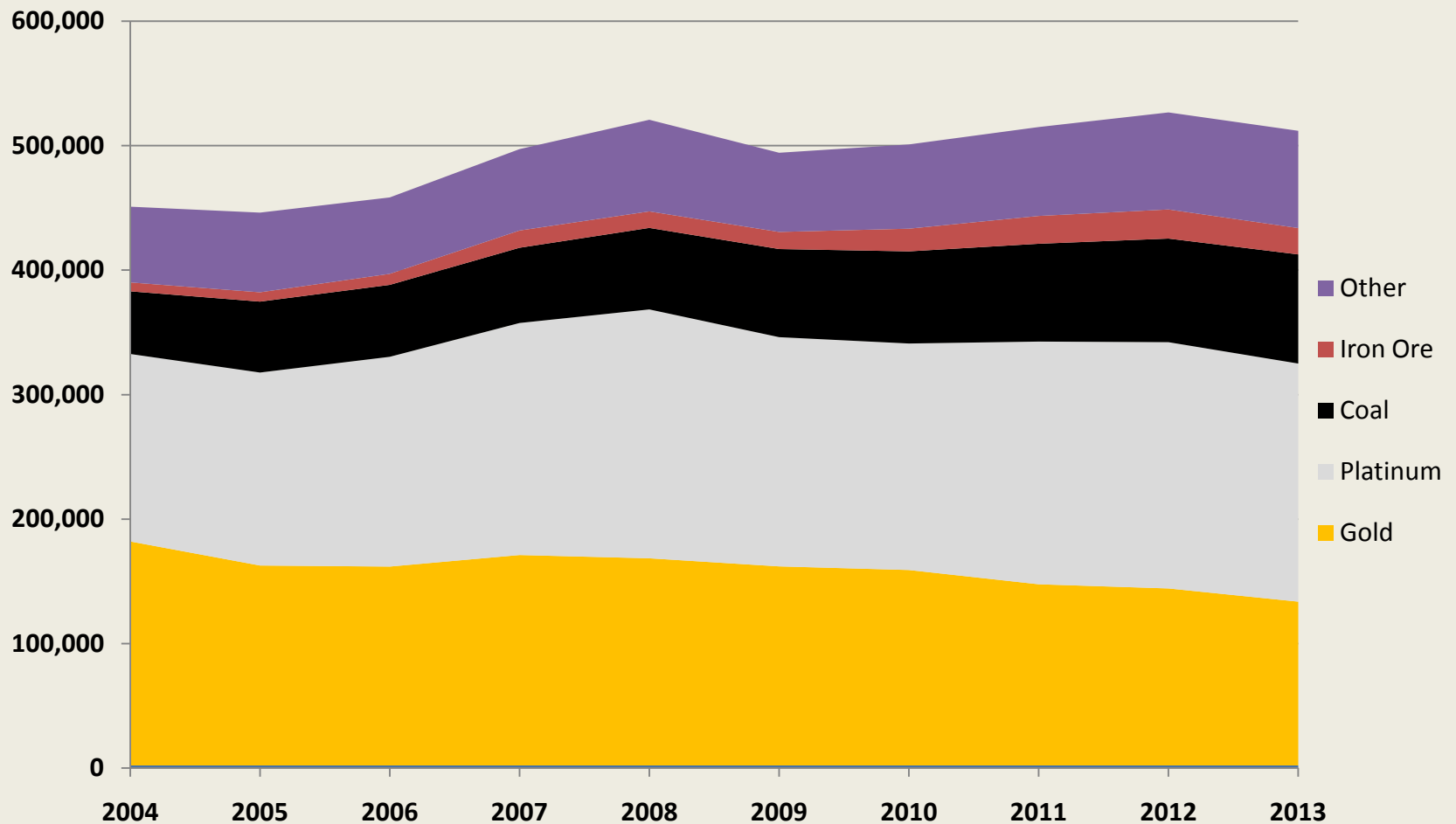
SA reserves of key minerals



Source: Global insight and USGS



Net employment trend in the mining industry

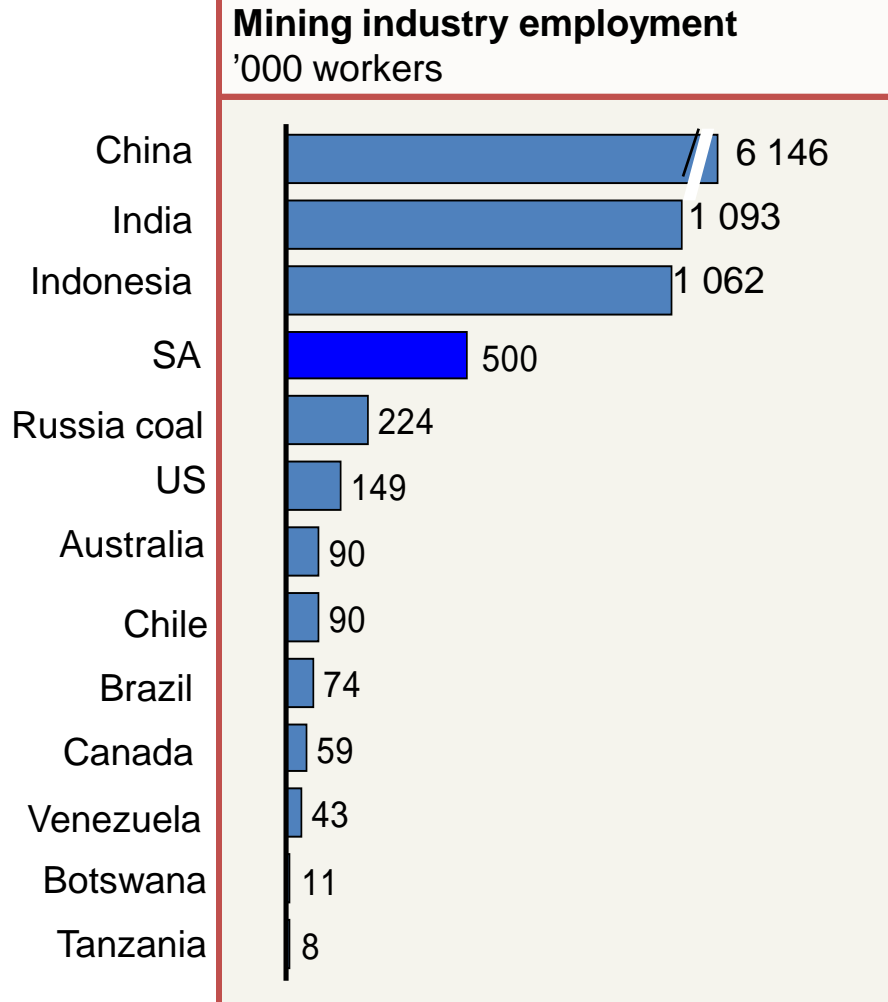


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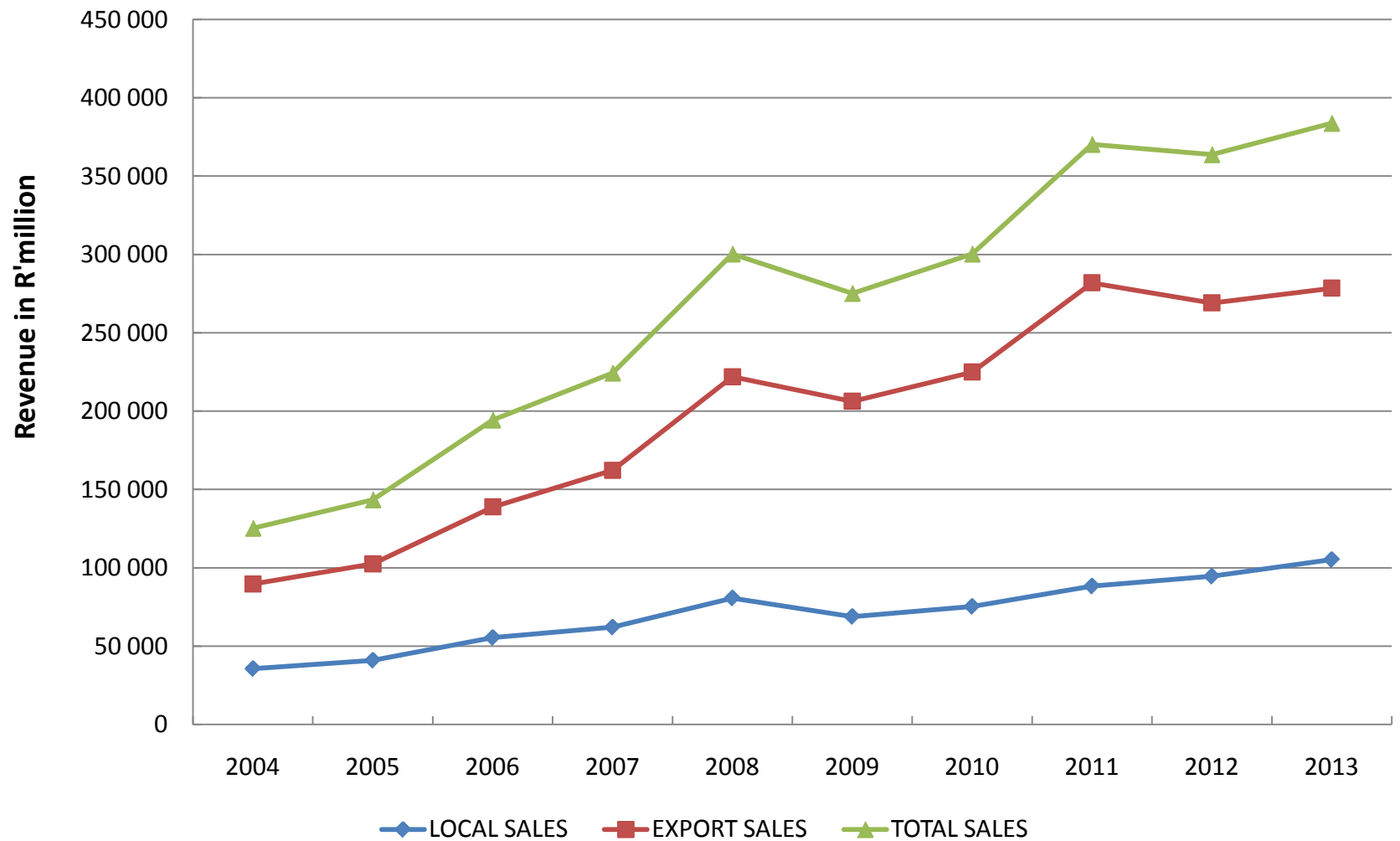
Source: DMR statistics

Comparative mining employment



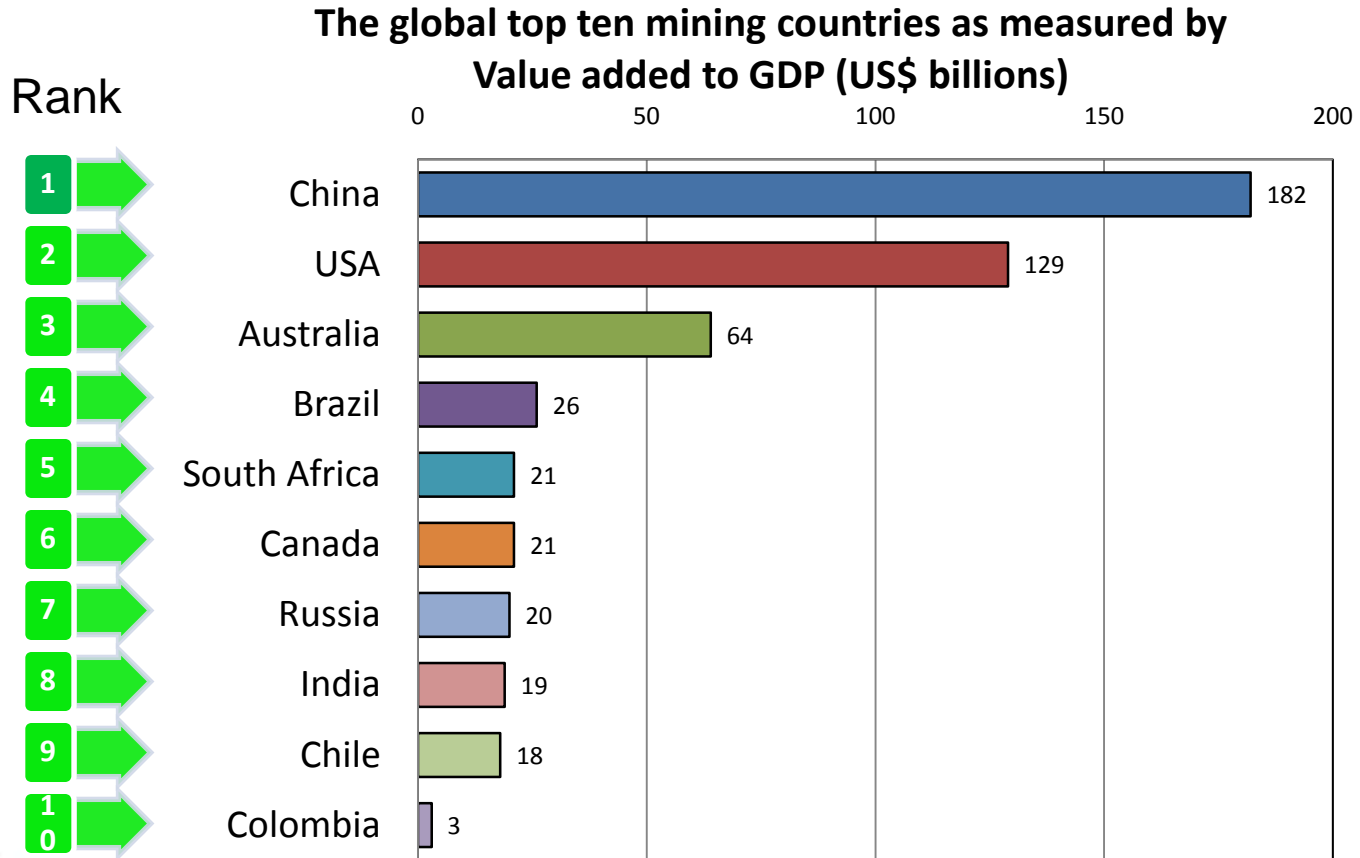
SOURCE: DMR, Minerals Council of Australia; Australian Bureau of Statistics; Bank of Botswana; Brazilian Labour Ministry; Natural Resources Canada; Statistics Institute of Chile, US MSHA; Indian Economic Survey 2007/08; Indonesian Ministry of Labour; Venezuelan Labour Ministry

Mining revenue



Source: DMR statistics

South African mining industry is world's 5th largest by GDP value.....



Source: Global insight

South Africa ranks 6th in productivity

Country	Value Added to GDP (US\$ Billion)	Direct Employment ('000)	Productivity (Value added generation in US\$ million per 1 000 employees)
USA	129	149	866
Australia	64	90	711
Canada	21	59	356
Brazil	26	74	351
Chile	18	90	200
RSA	21	519	40
China	182	6,146	30
India	19	1,093	17



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Mining contribution to the economy (cont...)

Table 1: Breakdown of contributions by sector to Company Income Tax

CIT - Provisional: % Share by sector	2001/02	2002/03	2003/04	2004/05	2011/12	2012/13
FINANCE, INSURANCE, REAL ESTATE AND RELATED SERVICES – including Long Term Insurers	28%	31%	33%	35%	34%	36%
MANUFACTURING	30%	31%	31%	32%	24%	22%
RETAIL AND WHOLESALE TRADE	8%	7%	10%	11%	11%	11%
TRANSPORT, STORAGE AND COMMUNICATION	8%	6%	6%	9%	8%	8%
MINING AND QUARRYING	18%	17%	11%	4%	11%	8%
SPECIALISED SERVICES	4%	3%	4%	4%	5%	4%
OTHER	1%	0%	0%	0%	2%	4%
AGENCIES AND OTHER SERVICES	1%	1%	2%	2%	2%	2%
CONSTRUCTION	1%	1%	1%	1%	2%	2%
AGRICULTURE, FORESTRY AND FISHING	1%	2%	2%	2%	1%	2%
ELECTRICITY, GAS AND WATER	1%	1%	1%	1%	1%	1%

Source : National Treasury



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A summary of mining industry's significance to the South African economy

- ❖ Creates 1 million jobs (500 000 direct & 500 000 indirect)
- ❖ Accounts for about 18% of GDP (including multipliers)
- ❖ Contributes approx. 50% to foreign exchange earnings
- ❖ Accounts for 18% of total fixed investment (including multipliers)
- ❖ Accounts for more than 30% of JSE value (in excess of R2 Trillion)
- ❖ 18.5% of corporate tax receipts (2007R22 billion, 2008 R33 billion)
- ❖ Creates demand for 50% of volume of Transnet's rail and ports
- ❖ Contributes to 93% of electricity generation via coal power plants
- ❖ Consumes an avg. of 32 000 gigawatt hours of electricity, representing approx. 15% of national electricity demand
- ❖ Responsible for 37% of country's liquid fuels through coal (>R30 billion worth)



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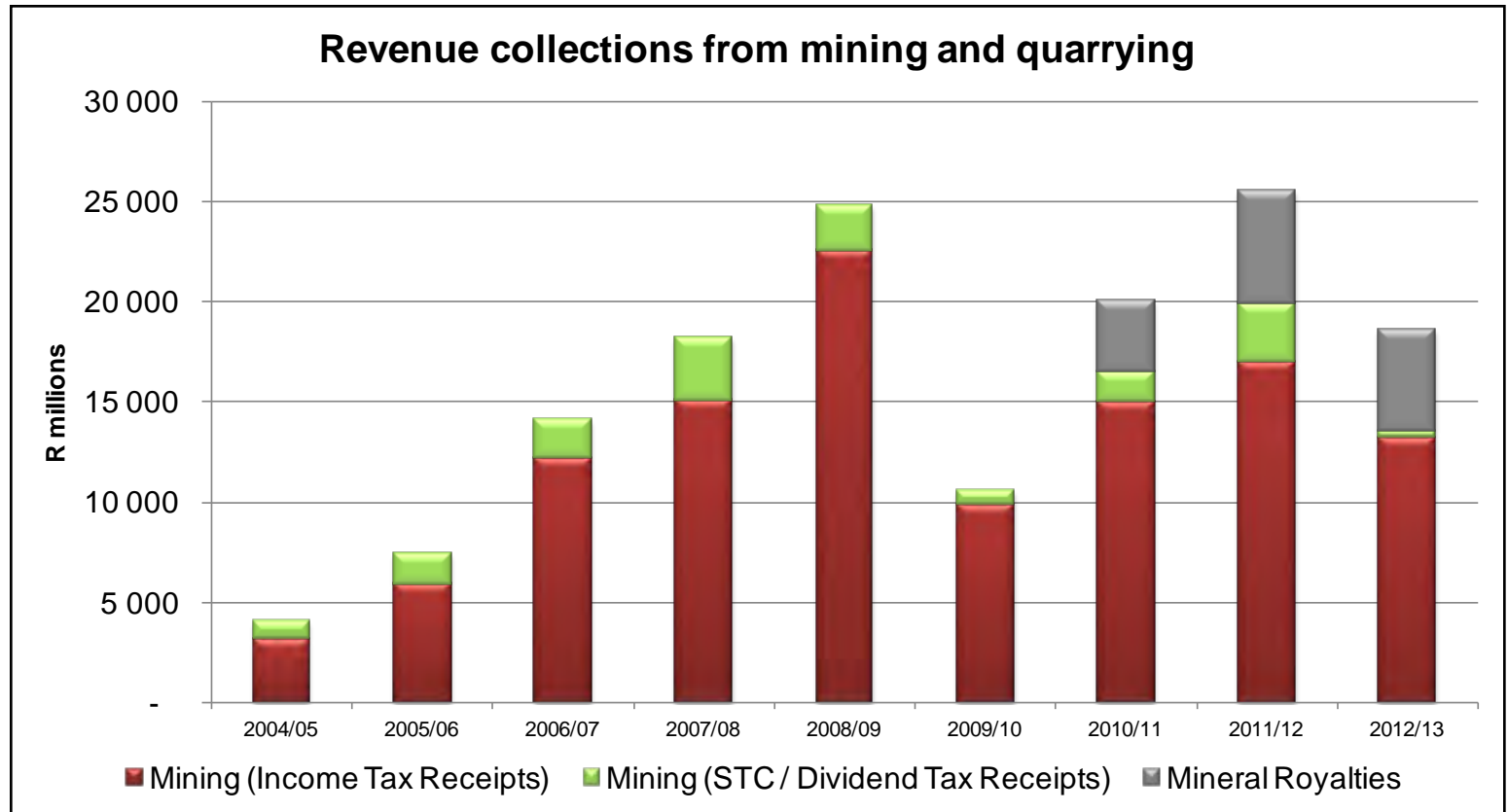
Transfer pricing and its impact on the economy



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State's revenue collection from mining



Source : National Treasury

Comparative national benefit derived from mining

Commodity-related revenues in selected commodity-exporting countries, 2007

Country	% Total revenue	% GDP
Chile	31.3	8.6
Mexico	35.4	7.9
Norway	24.3	14.3
RSA	< 5	< 5
Russia	26.2	10.5

Note: Commodity-related revenues include, where applicable, **corporate income tax** from the natural resource sector, **royalties**, **licenses**, **export taxes**, and **income from state-owned mining companies**.

Source: SAMI 2008/9 and OECD mining report. 2010

❑ Arbitrage:

“The simultaneous purchase and sale of the same securities, commodities, or foreign exchange in different markets to profit from unequal prices”

❑ Transfer Pricing:

“The setting of a price (artificially low) for the transfer of raw materials, products or services between the trading units of a large organisation”

- ✓ *The trading units are wholly owned by the large organisation and may be domiciled in different countries, typically considered to be tax havens.*

Case study: complex structuring to effect BEPS?

BEPS = BASE EROSION AND PROFIT SHIFTING

Company X Ltd and its subsidiary structures

Company	Activity	% Interest
Company X (Pty) Ltd (SA)	Mining	74% (BEE compliant)
SPV Y (Pty) Ltd (SA)	Investment Holdings	100%
SPV Investment Holdings (Pty) Ltd (SA)	Investment Holdings	100%
SPV Ltd (Asia based)	Commodity marketing and sales	100%
SPV Shipping Ltd (Asia based)	Shipping	100%
International BV (EU based)	Commodity marketing and sales	100%
International Trading sa (EU based)	Commodity marketing and sales	100%
SPV Holdings SARL (EU based)	Investment Holdings	100%
SPV Pte Ltd (Asian based)	Commodity marketing and sales	100%
SPV Resources Development (Pty) Ltd	Exploration	50% (High risk)



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17

Previous work on transfer pricing

WORK PROGRAMME OF THE KATZ COMMISSION:

- ❑ Having been appointed on 22 June 1994, the Commission completed its first *Interim Report* ("the first Report") on 18 November 1994, as presented to Minister of Finance on the same day of completion.
- ❑ At the request of the Minister of Finance the 1994 Report was submitted to the Parliamentary Joint Standing Committee on Finance for consideration and, more particularly, for evaluation of the public response to the recommendations contained in the Report.
- ❑ The evolution which is occurring in the approach to and administration of South Africa's exchange control regulations necessitated the preparation by the Commission of a second report. This *Second Interim Report* was issued by the Commission on 28 June 1995
 - ✓ It dealt with thin capitalisation and transfer pricing rules
 - ✓ These issues had already been identified in Chapter 14 of the first Report in which the Commission recommended the introduction of transfer pricing rules to protect the tax system against abuse as well as to prepare the system for any further relaxation of exchange controls.

LEGISLATIVE BASIS TO REGULATE TRANSFER PRICING:

- ❑ In its First Interim Report, the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa (“The Katz Commission”) articulated the fact that there was a lack of protection against the abuse of transfer prices
- ❑ The Katz Commission noted that the South African tax system needed legislative teeth with which to protect itself against excessive price manipulation between related parties
- ❑ The Second Interim Report listed various approaches, as developed by the worlds’ tax systems, from which the South African Legislative had a choice to implement in order to counteract transfer pricing
- ❑ Prior to 1995, transfer pricing in South Africa was regulated by the compliance with article 9 of the OECD Model Tax Convention Treaty or its equivalent.
- ❑ Section 31 of the Income Tax Act 58 of 1962 (“the Act”), as amended, took effect from 19 July 1995 to regulate transfer pricing in South Africa.



Action plan to date

- ❑ DMR has undertaken preliminary evaluation of the prospects of transfer pricing in the mining industry of SA and extensive literature review is seemingly corroborative
- ❑ The SADPMR has jointly undertaken preliminary assessment of diamonds and precious metals with the SARB
- ❑ Exploratory meetings of technical teams of the DMR and SARS have been held
- ❑ **Securing and protecting national economic sovereignty**
 - ✓ Since the purported transfer pricing activity is a function of under-stating the value of minerals at the point of export and declaration of revenue to SARS (customs), SA has capable institutions that can be geared to harmonise coordination to validate, quantify and value mineral exports to protect the national economic sovereignty. These include, the South African Bureau of Standards (SABS) and the interplay amongst DMR, SARS and Customs, which cannot be overstated.
 - ✓ To this effect, the DMR has initiated a strategic cooperation with SABS to utilise technical prowess in partnership with other key institutions of government – this requires resources to effect meaningfully.
- ❑ The meeting between the Ministers of Mineral Resources and Finance is imminent.



State of and the impediments to the implementation of the mining charter



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Mining Charter

- ❖ 1995-1997, the new democratic dispensation embarked on a process of reviewing the mining legislative framework
- ❖ In 1998 the White paper on Minerals and Mining Policy for South Africa was adopted with the primary objective of transforming the mining sector
- ❖ The year 2002 presented a major shift for the mining industry, with the promulgation of the Mineral and Petroleum Resources Development Act, 2002 (Act 28 of 2002)(MPRDA);
- ❖ The MPRDA gave effect to the transformation principle embedded in the white paper;
- ❖ **Section 100 of the MPRDA** empowered the Minister to develop a Mining Charter, a policy instrument to effect transformation with specific targets;
- ❖ In 2004 the mining industry, organised labour and Government negotiated and developed the Mining Charter.



- ❖ The Charter introduced several transformation elements:
 - **Ownership**- to encourage HDSA ownership
 - **Procurement**- HDSAs as preferred supplier for capital goods, services and consumables
 - **Housing and living conditions**- establishing measures to improve the standard of housing including upgrading of hostels and conversion of hostels into family units
 - **Employment Equity**- encourage participation of HDSAs in management
 - **Human Resources Development**- to address the skills gap in the industry by promoting mining related educational advancement, providing skills training opportunities to miners and implement career paths;
 - **Mine Community and Rural development**- to improve the lives of communities where mining takes place and labour sending areas; and
 - **Beneficiation** : to Promote beneficiation of RSA mineral commodities
 - **Procurement** – to advance empowerment of HSDSA;
 - **Migrant Labour System** – It aimed at addressing the discrimination of foreign migrant workers
 - Reporting – Submission on annual basis



The 2004 Mining Charter, had weaknesses. Its scorecard did not provide clear targets in most elements and as a result was not able to address the objects of sustainable development and transformation effectively.

2004 Mining Charter - scorecard

		Yes		No		100%	
Human Resource Development							
•	Has the company offered every employee the opportunity to be functionally literate and numerate by the year 2005 and are employees being trained?	Yes		No			
•	Has the company implemented career paths for HDSA employees including skills development plans?	Yes		No			
•	Has the company developed systems through which empowerment groups can be mentored?	Yes		No			
Employment Equity							
•	Has the company published its employment equity plan and reported on its annual progress in meeting that plan?	Yes		No			
•	Has the company established a plan to achieve a target for HDSA participation in management of 40% within five years and is implementing the plan?						
•	Has the company identified a talent pool and is it fast tracking it?	Yes		No			
•	Has the company established a plan to achieve the target for women participation in mining of 10% within the five years and is implementing the plan?						
Migrant Labour							
•	Has the company subscribed to government and industry agreements to ensure non-discrimination against foreign migrant labour?	Yes		No			
Mine community and rural development.							
•	Has the company co-operated in the formulation of integrated development plans and is the company co-operating with government in the implementation of these plans for communities where mining takes place and for major labour sending areas? Has there been effort on the side of the company to engage the local mine community and major labour sending area communities? (Companies will be required to cite a pattern of consultation, indicate money expenditures and show a plan).	Yes		No			
Housing and Living Conditions							
•	For company provided housing has the mine, in consultation with stakeholders established measures for improving the standard of housing, including the upgrading of the hostels, conversion of hostels to family units and promoted home ownership options for mine employees? Companies will be required to indicate what they have done to improve housing and show a plan to progress the issue over time and is implementing the plan?	Yes		No			
•	For company provided nutrition has the mine established measures for improving the nutrition of mine employees? Companies will be required to indicate what they have done to improve nutrition and show a plan to progress the issue over time and is implementing the plan?	Yes		No			
Procurement							
•	Has the mining company given HDSA's preferred supplier status?	Yes		No			
•	Has the mining company identified current level of procurement from HDSA companies in terms of capital goods, consumables and services?	Yes		No			
•	Has the mining company indicated a commitment to a progression of procurement from HDSA companies over a 3 – 5 year time frame in terms of capital goods, consumables and services and to what extent has the commitment been implemented?	Yes		No			
Ownership & Joint Ventures							
•	Has the mining company achieved HDSA participation in terms of ownership for equity or attributable units of production of 15 percent in HDSA hands within 5-years and 26 percent in 10-years?					15%	26%
Beneficiation							
•	Has the mining company identified its current level of beneficiation?	Yes		No			
•	Has the mining company established its base line level of beneficiation and indicated the extent that this will have to be grown in order to qualify for an offset?	Yes		No			
Reporting							
•	Has the company reported on an annual basis its progress towards achieving its commitments in its annual report?	Yes		No			



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Mining Charter review

- ❖ In 2009 the DMR conducted a baseline assessment on compliance with the Charter requirements by industry
- ❖ The findings of the assessment identified a number of **shortcomings in the** manner in which the mining industry was implementing various elements of the Charter – the weakness of the Charter was further highlighted
- ❖ This led to the review of the Mining Charter to clarify requirements by improving on the reporting process, with an improved scorecard
- ❖ In 2010 an amended Mining Charter was published by the Department

Revised Mining Charter elements

❖ **Ownership:**

- ❖ Meaningful economic participation of HDSA by 2014 -26%
- ❖ Full shareholder rights 26%

❖ **Housing and living conditions:**

- Conversion of hostels to obtain objective of one person per room
- Conversion of hostels into family units and facilitate home ownership by 2014

❖ **Procurement and enterprise development:**

- Procure a minimum of:
 - ✓ 40% of capital goods;
 - ✓ 70% services and
 - ✓ 50% Consumables from BEE entities by 2014
- Multinational suppliers must contribute 0.5% of procurement to social fund



Revised Mining Charter elements

- ❖ **Employment equity:** Mining companies must achieve a minimum of 40% HDSA across all levels by 2014
- ❖ **Human Resource Development:** Spend a percentage of annual payroll in essential skills development which must amount to 5% by 2014
- ❖ **Mine community development:**
 - Implement approved community projects
 - By 2014 – Up-to-date project implementation
- ❖ **Sustainable development and Growth:**
 - Implementation of approved EMPs – 100%
 - Implementation of tripartite action plan on health and safety – 100%
 - Percentages of samples analysed in South Africa facilities – 100%
- ❖ **Beneficiation:**
 - There has to be additional beneficiation beyond the base line –Section 26 of MPRDA will be implemented



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Revised Mining Charter elements

- ❖ **Reporting (monitoring and evaluation):**
 - Companies to report annually on their levels of compliance with the Mining Charter
- ❖ **Second Assessment**
 - The second assessment for the 2014 milestone is currently being conducted to ensure that the DMR quantifies the compliance levels of the ten year window period
 - The report produced will provide compliance levels iro of the agreed milestones, and will be used as the basis on which the Mining Charter targets may be reviewed
- ❖ **Reporting (monitoring and evaluation):**
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The status of implementation of the minerals beneficiation strategy



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BENEFICIATION



- ❑ Beneficiation is part of a broader policy and legislative framework that leverages more value from the mining sector beyond taxes and royalties.
- ❑ This framework will enhance the beneficiation element of the framework and leverage on others

BENEFICIATION

- ❑ The beneficiation strategy was adopted by Cabinet in 2011 as policy
- ❑ The strategy seeks to, inter alia:
 - Increase a ratio of beneficiation extent to mineral production and increase export revenue
 - Enhance the nation's productive capacity
 - Facilitate economic diversification
 - Expedite progress towards a knowledge based economy
 - Create opportunities for new enterprise development
 - Contribute to creation of decent jobs and poverty alleviation

BENEFICIATION

- ❑ These actions have been used to develop an implementation plan which is subject to finalisation
- ❑ One of the recommended actions has been implemented which is strengthening the MPRDA to ensure security of supply
- ❑ The DTI, supported by the DMR and other relevant departments, has committed to collaborate on finalisation of the value chain specific interventions in the current MTSF

PILOT COMMODITY VALUE CHAINS (ENERGY)

- Energy vital to any industrialisation process security of energy supply is of the utmost importance
- Main energy commodities are Coal, Uranium and Thorium
- Value chain interventions:
 - The coal reserves and resources technical study has been concluded
 - Quantification of the country's uranium and thorium reserves
 - Support for R&D into alternative and future energy sources (e.g. Fuel cells)

PILOT COMMODITY VALUE CHAINS (IRON AND STEEL)

- Steel products are vital inputs into labour intensive manufacturing processes but anti-competitive pricing is a major constraint to growth
- The inter-departmental steel value chain has been established amongst the Ministries of Trade and Industry, Economic Development and Mineral Resources to consider appropriate interventions sought
- Value chain interventions:
 - Invoke regulatory provisions to ensure sustainable and developmentally priced input commodities
 - Encourage investment into the South African steel industry to break prevailing anti-competitive behaviour by competitors


PILOT COMMODITY VALUE CHAINS (PIGMENT AND TITANIUM METAL)

- This value chain is a potential key growth area for the country as increasing levels of urbanisation are expected to underpin demand for Ti-mineral concentrates for pigment and aerospace component manufacture
- Value chain interventions:
 - Investigation into the viability of establishing a chlorine plant in conjunction with a pigment plant
 - The development of a more cost effective primary titanium metal production

PILOT COMMODITY VALUE CHAINS (AUTOCATALYTIC CONVERTERS)

- South Africa accounts for 1 in 10 autocats. produced globally and tightening emissions legislation will underpin future growth in this sector
- South Africa has set a target of capturing 25% of the global catalysis market by 2025
- Value chain interventions:
 - Invoke provisions of the law to ensure security of PGM supply
 - Development of metal access mechanism
 - Unlock the intrinsic value within the PGM sector





Mechanisms in place to address impediments to the minerals beneficiation strategy



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BENEFICIATION

- ❑ To achieve the mineral beneficiation objectives, the strategy identifies constraints to local beneficiation which are:
 - ❖ Limited access to raw materials for local beneficiation
 - ❖ Shortages of critical infrastructure
 - ❖ Limited exposure to R&D
 - ❖ Inadequate skills
 - ❖ Access to markets
- ❑ The strategy further recommends a set of actions that will unlock these constraints

PROGRESS ON IMPLEMENTING BENEFICIATION STRATEGY (LEGISLATION)

Mineral beneficiation

26. (1) The Minister may initiate or prescribe incentives to promote the beneficiation of minerals in the Republic.

(2) If the Minister, acting on advice of the Board and after consultation with the Minister of Trade and Industry, finds that a particular mineral can be beneficiated economically in the Republic, the Minister may promote such beneficiation subject to such terms and conditions as the Minister may determine.

(3) Any person who intends to beneficiate any mineral mined in the Republic outside the Republic may only do so after written notice and in consultation with the Minister.

- ❑ The strategy identified the need for the current provision of the MPRDA for beneficiation to be strengthened as it was largely silent on how Minister would promote beneficiation



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PROGRESS ON IMPLEMENTING BENEFICIATION STRATEGY (LEGISLATION)

Amendment of section 26 of Act 28 of 2002, as amended by section 22 of Act 49 of 2008

21. Section 26 of the principal Act is hereby amended—

(a) by the substitution for subsection (1) of the following subsection:

“(1) The Minister [may] must in order to regulate the mining industry to meet national development imperatives and to bring optimal benefit for the Republic initiate or promote the beneficiation of [minerals] mineral resources in the Republic—

(a) to ensure transformation of the mining and other sectors involved in the beneficiation of minerals or mineral products;

(b) to ensure sustainability for the supply of minerals in the national interest; and

(c) to develop local capacity.”;

(b) by the substitution for subsection (2) of the following subsection:

“(2) The Minister must—

(a) in consultation with a Minister of the relevant national departments designate any mineral or mineral product for local beneficiation;

(b) after taking into consideration the national developmental imperatives such as macro-economic stability, energy security, industrialisation, food security and infrastructure development; and

(c) after considering the advice of the Council as contemplated in section 56B;

publish such conditions required to ensure security of supply for local beneficiation in the prescribed manner.”

(c) by the insertion after subsection (2A) of the following subsection:

“(2B) Every producer of designated minerals must offer to local beneficiaries a prescribed percentage of its production of minerals or mineral products in prescribed quantities, qualities and timelines at the mine gate price or agreed price.”; and

(d) by the substitution for subsection (3) of the following subsection:

“(3) No person, other than a producer (or an associated company of such producer) in respect of its own production and who has complied with subsection (2B), may export designated minerals or mineral products without the Minister’s prior written approval.”

20 Minister is empowered to designate certain minerals for beneficiation purposes.

25
30 The Bill requires mining operations to set aside a certain percentage of their production for local



CONCLUDING REMARKS

- ❑ Beneficiation represents a “game changing” opportunity for the country and a win-win scenario for all stakeholders in domestic mineral value chains.
- ❑ Realisation of this “game changing” opportunity will be premised on close cooperation amongst all stakeholders (Government, Business, Labour and organised civil society)
- ❑ The development of commodity specific requirements, in the regulations under section 26, will be primarily guided by the country’s developmental imperatives, including energy security, industrialisation, food security, energy infrastructure and macro-economic stability, representative of a source of certainty for all stakeholders.





Inspiring new ways.....



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