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# No watertight agreements

Fiscal risk is on the rise, not just for miners, as tax policy becomes the battleground for a broadening array of political objectives.

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Low national productivity due to historically weak public investment spending needs fixing. Slowly growing but aging populations and, elsewhere, fast growing younger populations demanding higher quality urban public facilities are intensifying pressures on governments to bolster revenue collections. Rising debt-servicing obligations from imminently higher US interest rates, after a decade of cheap money, will add force to the search for more taxes.

Recently lowered US tax rates are not a reward for deserving corporates but an attempt to divert economic activity. For similar reasons, the Australian government is proposing reduced taxes for companies.

Australia's opposition parties have promised to reverse any benefits for larger companies once elected. In the US, too, higher rates are on the cards if targeted revenue gains fail to materialise or those politicians who believe the tax changes are fundamentally unfair gain power.

As widening disparities in income distribution have become a focus of political action and a growing worry among mainstream policy economists, tax policy is more than ever an ideological battleground.

Meanwhile, taxes on imports designed to raise the US share of global trade have begun to disrupt supply chains. Retaliatory measures by Chinese and European governments now threaten hitherto well established business logistic chains.

Companies structured to operate under the terms of the North American Free Trade Agreement are hopeful that their business models remain intact after new arrangements, including the threat of taxes to divert trade benefits, are hammered out.

Britain's exit from the European Union opens the way for a rethink of corporate fiscal incentives on both sides of the English Channel.

**Companies have no choice but to recognise the prerogative of governments to set priorities**

The increasingly aggressive use of targeted fiscal measures against foreign individuals or countries, designed for geopolitical ends, are also impacting the capacity of companies to operate in affected jurisdictions even where they might hold locally conferred rights to operate.

Within this swirling mix of politics and economics, miners are just one set of easily overridden interests.

Companies outside the mining industry are better able to respond to tax changes by relocating production to escape unfavourable policies. Locational decisions are not taken lightly but are modified more easily. Hence Harley Davidson can allocate production of its iconic motorcycles across plants the US, Brazil and India to more easily access markets. Brazil's iron ore production, on the other hand, cannot be shifted to more convenient locations.

Legislators have become increasingly hostile to corporate locational decisions with potentially adverse effects on tax collections. Rapid growth among the likes of Apple, Facebook, Amazon and Google, whose activities easily blur national boundaries and whose sometimes indistinct 'products' raise complex questions about the geographic origins of their profits, have heightened political sensitivities about the sharing of tax burdens.

BHP and Rio Tinto have suffered similar reputational damage among sceptical lawmakers as they tried to justify large profits from iron ore sales out of relatively lowly-taxed companies in mineral-poor Singapore.

Added to these general pressures are an array of additional fiscal risks for the mining industry that arise from the role of government as the vendor of rights to sub-surface mineral resources.

Fiscal regimes can impact the timing of mineral development, the duration of mining activity and possibly the efficiency and safety with which mining is conducted.

The terms and conditions on which transfers of rights to non-renewable resources occur affect the amount and distribution of national wealth.

Some governments allow relatively free access to mineral properties counting on the benefits flowing from speedy and unencumbered development. In other jurisdictions, states will seek to exercise more control including through direct ownership and participation in project decision making.

Pressures for the adoption of universally applied fiscal models have resulted in less emphasis on more easily policed royalty schemes and more widespread use of income as the determinant of tax payments.

For governments, abandonment of royalties brings risks. Income taxes allow self-assessment, at least in the first instance. A drop in commodity prices has a proportionately greater adverse impact under a profit-based tax than under a royalty structure.

Since every mineral development is different, bespoke fiscal terms are sometimes thought advantageous. Seemingly favourable mine-by-mine contracts of work bring their own risks. Pressures for

amendments emerge as subsequent contracts are negotiated on differing terms leading to demands for consistency.

Parties to contracts in any line of business will seek to amend previous agreements if circumstances change or unanticipated events intervene. Governments are no less likely to do the same.

Even among the most competently governed nations, responses to macroeconomic changes may require periodic reordering of tax arrangements. Fiscal risks rise as macro volatility goes up.

Companies have no choice but to recognise the prerogative of governments to set priorities, the potential for domestic political change to affect policy agendas and the risk attaching to unanticipated circumstances.

There is no such thing as a watertight fiscal agreement. Continual wariness - by companies and their investors - about the likelihood of fiscal stability is needed.

Examination of historical track records within individual jurisdictions and a rigorous appraisal of tell-tale signs of risk based on the experiences of others is a necessary minimum in a risk-mitigation strategy.

This opinion piece will lead off the 2018 Mining Journal World Risk Report (feat. MineHutte ratings), which is set to be published in late September

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