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**RE: DRAFT TAX ADMINISTRATION LAWS AMENDMENT BILL, 2018: COMMENTS PERTAINING TO KEY MINING TAX ISSUES**

We have attached the comments from the SAIT Mining Tax Work Group on the draft Tax Administration Laws Amendment Bill pertaining to key mining tax issues. We appreciate the opportunity to participate in the process and would welcome further dialogue.

Please do not hesitate to contact us should you need further information.

Yours sincerely

**Andre de Klerk**  
**Chair of the Mining Tax Work Group**

## MINING TAX SUBMISSION

### Proposed amendment to Section 6(3)(b) of the Mineral and Petroleum Resources Royalty Act

a. Treasury proposal

It is proposed to clarify the original policy intent that the tax base for royalty purposes was generally defined both in the legislation and the explanatory memorandum as gross sales excluding the costs of transportation, insurance and handling (“TIH”) of the final product or mineral between the seller and the buyer as this would unintentionally increase gross sales leading to a higher royalty tax payable. In 2009, additional clarification was made in section 6(3)(b) of the Mineral and Petroleum Resources Royalty Act dealing with gross sales. The 2009 changes resulted in the policy intent regarding the definition of gross sales not to be clearly expressed in the text of the legislative provision even though the policy intent was clear in the explanatory memorandum.

b. Comment – High Court judgment confirms policy intent

The determination of Gross Sales without having regard to the transport, insurance and handling (“TIH”) cost has been a contentious issue to date and is the subject of numerous tax disputes with SARS. The High Court was recently asked to interpret the provisions of Section 6(3)(b) to clarify the interpretation of the relevant statute, which it did in the matter between UMK and the Commissioner for SARS (case no. 741582016).

The High Court judgment clarified the uncertainty in respect of the interpretation of section 6(3)(b). Accordingly, there is no uncertainty with regards to the determination of Gross Sales, the tax base. However, this section is now proposed to be amended.

The Explanatory Memorandum (“EM”) to the TLAB 2018 indicates that the amendment in 2009 resulted in the policy intent not being clearly expressed in the text of the legislative provision. The EM does not indicate the clarity required.

The order made by the High Court states that Gross Sales is to be determined by excluding/deducting any expenditure incurred in respect of TIH cost, which is in line with the policy intent set out in the

EM to the Mineral and Petroleum Resources Royalty Bill 2008, which according to the Explanatory Memorandum to the TLAB 2018 has not changed:

*“The determination of both gross sales and EBIT excludes transportation, insurance and handling charges. This exclusion is necessary so as not to penalize minerals that are located far from markets or an export port.*

*Transport, insurance and handling charges for the transportation of minerals, in the conditions as per Schedules 1 and 2, between buyer and seller are excluded.” (own underlining)*

It follows that the order made by the High Court confirms the policy intent in that it ordered that the TIH cost incurred after the mineral reached the condition specified be deducted/excluded from Gross Sales.

It is therefore unclear what clarity is required as the UMK judgment brought the certainty that has been required. We are concerned that the certainty regarding the policy intent provided by the court may again be called into question should the wording be amended as proposed, resulting in further unnecessary disputes between SARS and taxpayers.

c. Comment – Commercial terms

It should be considered that the nature of the global market is such that in respect of most of the minerals exported prices are determined with reference to an index price.

Index prices are quoted with reference to Incoterms that sets out the commercial terms in respect of which the prices are quoted. The Incoterms represent universal terms that defines a transaction between sellers and buyers, so that both parties understand the tasks, costs, risks and responsibilities, as well as the logistics and transportation management from the exit of the product to the reception by the importing country.

In most cases commodity Index prices are quoted based on FOB, CIF or CFR terms all of which require that the seller is responsible to deliver the goods on to the ship at its risk and cost, and in terms of CIF and CFR deliver the mineral to the port of discharge. Risk and reward pass from the seller to the buyer when the goods have passed over the ship's rail at the named port of shipment. The seller must bear all cost and risk to deliver the goods onto the ship and at the destination based on the Incoterms to which the Index price reference to, via the mechanics of the Incoterms TIH costs are indirectly recovered. (Refer to Annexure A for a more detailed discussion on the mechanics of Incoterms).

The proposed wording may create uncertainty and room for disputes in respect of Indexed based trading as to what is required by the taxpayer to discharge the burden of proof of what amount was received or accrued in respect of TIH cost. SARS may argue that if the recovery of TIH costs is not separately disclosed on the sales invoice, it has not been received or accrued. If such amounts were disclosed on invoices it will contribute to disclose the seller's margins etc and disclose the pricing of its logistics agreements, which will disadvantage the taxpayer in a competitive trading environment. In a globally competitive world, this is simply not commercially viable.

If the compliance requirements are unclear, the ambiguity created by the proposed changes will result in further disputes with SARS, whereas the judgement in the UMK matter has provided the certainty required for both SARS and the Taxpayer.

At the end of the day, the seller of mineral products should be able to reduce the royalty for proven transport, insurance and handling costs paid via proof of invoice / actual payment made in respect of these costs. No reason exists to require these fees to be separately listed on the sale invoice for the mineral itself. The royalty was always intended to fall on the value of the mineral – not unrelated charges that are factor of distance to market.

## **ANNEXURE A**

Incoterms or International Commercial Terms are a series of pre-defined commercial terms published by the International Chamber of Commerce.

It represents universal terms that defines a transaction between importer and exporter, so that both parties understand the tasks, costs, risks and responsibilities, as well as the logistics and transportation management from the exit of the product to the reception by the importing country.

Most international transactions are conducted based on the Incoterms and it represents the standard for international trading activities.

Index prices are generally quoted with reference to an Incoterm such as FOB or CIF or CFR etc. and it indicates to the seller and buyer that the quoted Index takes into account costs, risks and obligations in relation to the commercial terms depicted by the relevant Incoterm.

To illustrate:

The Iron Ore price for example quoted at CFR includes the FOB cost plus freight cost to the named port of delivery, which is different to a CIF price, which includes the FOB cost plus the freight and insurance cost to the port of delivery. Accordingly, the CIF and CFR price at the same point in time would be different even if delivery is to the same port of delivery as a result of the additional insurance cost that CIF terms carry.

In respect of the FOB Incoterm the seller is responsible to deliver at its cost and risk the goods onto the ship, where risk and reward passes from the seller to the buyer.

There is also a difference in price between the EXW (Ex Works) or FCA rail siding price for example, to an FOB price as the FOB price takes the logistics cost to the port and loading cost into account. Table 1 below list the most commonly used Incoterms and segregate the costs, responsibilities and risks between the seller and the buyer.

