THE FREE MARKET FOUNDATION
of Southern Africa
progress through freedom

Comment on the

Minerals and Petroleum Royalty Bill
30 April 2003

This submission is confined to three core aspects of the Bill: its impact on small, new and black economic empowerment companies; international competitiveness; and the negative investor implications of the fiscal stabilisation provision.

1. Empowerment, small and new businesses

A turnover royalty has three fatal consequences. Firstly, it is imposed on new businesses when they are struggling to recover initial capital, and places marginal businesses below the threshold for survival. To tax companies regardless of their profitability has the net effect of reducing potential revenue from profitable companies and failing to recover revenue from marginal or loss-making companies because it renders them insolvent or prevents them from investing at all.

Secondly, a turnover royalty is a disproportionately high cost for new or small businesses. It discriminates in favour of established and profitable businesses thereby undermining national goals of black economic empowerment, and small and medium business development.

Thirdly, a turnover royalty brings about direct and absolute reduction in the quantity of viable mineral deposits and shortens the life expectancy of all mines. Some marginal deposits, which could be mined profitably for many decades – there are many examples in South Africa – would not be viable with a turnover royalty. Had there been a turnover royalty historically, many successful South African mines would never have come into existence, would have closed at an early stage, or would have been much smaller. Not only would the country have incurred a needless loss of wealth and jobs, but government would have collected reduced or zero revenue in such cases.

2. International Competitiveness

The royalty envisaged is in excess of the norm for countries characterised by successful mining industries.

Not only does the royalty start at the high level found in uncompetitive countries, but the message to international and local investment communities is that this is a start; that the level is certain to be raised. (see below).

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This Bill is another "nail in the coffin" of South Africa's famous mining industry and international perceptions about South Africa. It is one in a succession of measures, including mineral right nationalisation, which is at variance with international trends, and suggests that the government is not serious about GEAR and NEPAD.

While the rest of the world moves towards the position South Africa occupied when it was the world's leading non-oil producer of minerals, we are moving towards the position in countries with rich mineral deposits, but poor mining industries, low economic growth and third world poverty. The global trend is towards mineral rights enhancement, reduction of taxes (in all forms) and deregulation.

3. Royalty / Fiscal Stabilisation

The "fiscal stabilisation" provision re-enforces negative perceptions and "messages" to the effect that investing in South Africa is risky because of increasing constraints and imposts, and policy instability. It implies that, not only is there a new tax, along with a range of additional costly regulations from policies within other departments such as Mineral and Energy Affairs and Labour, but that there is more to come. At a premium of at least 2% or up to 50% of the royalty rate, investors can purchase insurance against one element of increased risk and instability, indicating a clear intention to impose higher rates in future at worst, and to subject the industry to uncertainty at best.

The increased policy instability and uncertainty created by a plethora of additional taxes and regulations is having a detrimental effect on South Africa's potential as an investment destination. Investors will be inclined to go elsewhere or take a short-term view of investing in South Africa – quickly get as much out of the country as they can before policy changes rob them of profitability.

There is an investor perception of inadequate co-ordination between government departments, and of policies based on dubious assumptions, such as the aggregate amount of tax paid by South African mines. What matters is the aggregate amount of revenue in all forms collected from the mines, and the impact on profitability and capital accumulation of all forms of constraints on resource ownership and economic freedom imposed by all government departments.

One of the problems plaguing South Africa is the inordinate amount of management time involved in dealing with and responding to the volatile regulatory climate. Investors prefer countries where laws are stable and predictable. South Africa is a very small player in the world economy accounting for less than 0.05% of global GDP. If it wants to attract long term investment on a significant scale from local and foreign investors it must stop (a) constant and complex changes to laws affecting business and (b) provisions in laws that promote uncertainty and create costs that far exceed benefits.

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