THE REVISED LONDON MINING AGREEMENT:

BETTER, BUT STILL A MAJOR PROBLEM

SUMMARY INTRODUCTION

The government of Sierra Leone has revised the mining agreement with London Mining signed in December 2009 and produced a new, draft agreement that is soon to be scrutinised by Parliament. NACE finds that the new agreement is better overall than the current one but contains 11 provisions inconsistent with Sierra Leone’s legislation while some of its terms are actually worse than in the current agreement.

The new agreement should not be ratified in its present form, since the country will unnecessarily lose badly-needed revenues. Increasing revenues from mining must be a top priority for the government, along with ensuring transparency in such revenues as under the Extractive Industries Transparency Initiative.

THE CURRENT AGREEMENT

The UK-based company, London Mining is embarking on a large project to develop an iron ore mine at Marampa, east of Freetown. The agreement signed by the government and London Mining on 31 December 2009 was widely criticised, including by NACE, for giving too many concessions to the company. Most importantly, it gave London Mining:

- a 6 per cent income tax rate for 10 years, compared to the standard 30 per cent
• a formula for paying royalties that would have reduced such payments from the standard 30 per cent
• the ability to prevent future governments from raising taxes on the company (a stabilisation clause).


NACE has obtained a copy of the new, draft agreement dated 14 August 2011 and analysed its fiscal terms. A full analysis is in the Annex.

The good
There are several important improvements over the current agreement. For example, the new agreement would increase the corporate income tax rate, require the company to pay its full royalties consistent with the Mines and Mineral Act, and increase the lease rent payable for its mining concession.

However, these positives are outweighed by other aspects of the agreement.

The bad
The new agreement includes 11 terms that are inconsistent with Sierra Leone’s legislation, notably with the Mines and Minerals Act, 2009 and the Income Tax Act, 2000. The most important include:

• London Mining would retain a 6 per cent income tax rate for three years and then pay 25 per cent. This is still a significant concession compared to the 30 per cent standard rate.
• The company would pay only 1 per cent import duty on the value of imports of mining equipment for the first eight years, compared to legislation stating 3 per cent.
• The company has been given reductions in three categories of withholding tax – on dividends, on interest on loans and on contracts awarded to non-residents – that are more generous than in the legislation.
• The ability to offset various expenditure items against tax (notably community development spending and lease and surface rent payments) is not provided for in legislation.

The ugly
Some terms of the new agreement are worse than the current one:

• The company has been given an exemption from paying social security (NASSIT) contributions for its expatriate staff (for which there is no provision in legislation).
The company’s ability to offset lease rent and surface rent is a new concession not in the current agreement.

- The company would be exempt from paying Roads Users Fuel Levy; the current agreement allows the company to pay 20 per cent of the prevailing rate.

The mixed

The new agreement would require the company to spend at least 1 per cent of its gross sales revenue on community development - the same as the current agreement. This compares to a requirement in the Mines and Minerals Act to allocate only 0.1 per cent – a ten-fold increase. However, the new agreement commits the company to spend such a sum only for five years, and also allows it to offset such spending against tax, as noted above.

WHY THE PRESENT AGREEMENT SHOULD NOT BE RATIFIED

NACE is not opposed to London Mining operating the mine at Marampa, but the terms under which this takes place are critical. The key issue is to increase revenues from mining to enable the government to spend more on eradicating poverty. Sierra Leone earned only around $10.2 million from mining in 2007 and $7.2 million in 2006. As a proportion of total government revenues, mining earnings amount to only around 5 per cent. This is very little for a country rich in mineral resources.

The tax concessions given to London Mining reduce the potential revenues to the government. At the same time, the new agreement – like the current agreement - is inconsistent with the country’s legislation. The Mines and Minerals Act of 2009 took several years to pass and is an improvement in the country’s mining laws: most importantly, it raises royalty rates payable by companies and requires all large-scale mining companies to enter into Community Development Agreements with the local community. Overall, the Act provides a more transparent and level playing field for companies to operate in Sierra Leone, and marks a break with the past when individual companies received special tax concessions from ministers without public scrutiny – from which ordinary Sierra Leoneans benefitted little or not at all.

The new agreement with London Mining, although improved, is a continuation of the murky past. It opens the door for every mining company to negotiate special terms and tax concessions. Indeed, this is happening: the government has signed an agreement with African Minerals in August 2010 that also contradicts Sierra Leone’s legislation in numerous ways – and which also needs to be urgently revised, NACE believes.
The London Mining agreement directly contradicts the government’s promise to the IMF, made in May 2010, to the effect that ‘This new fiscal regime [ie, the Mines and Minerals Act] will apply to all new mining contracts’. 4

The government’s willingness to override the terms of its own legislation sends a signal internationally that Sierra Leone does not abide by enacted laws. This is likely to discourage reputable foreign investment. Numerous studies suggest that when foreign investors consider making investments, tax incentives are not the most significant factor – more important are the predictability of government regulations and transparent decision-making processes, alongside other factors such as the quality of infrastructure.5 The signal sent by the London Mining agreement is these factors are not yet in place in Sierra Leone.

Financial benefits?

London Mining has stated that the government will receive more than $200 million in revenues from the Marampa mine over a 10-year period, and that the company needs such fiscal incentives to operate profitably.6 Yet even if the projected benefits from the mine do materialise, they may well be offset by concessions the government will have to offer other companies in special agreements. London Mining’s argument that it could not operate competitively without these special fiscal and other terms is difficult to accept. The provisions in the MMA are hardly onerous on companies; they are broadly in line with international and West African practice. But even if they were too onerous for companies to bring needed foreign investment to Sierra Leone, the solution would not be to offer companies special deals but to revise the legislation.

RECOMMENDATIONS

- NACE calls on Parliamentarians to reject the ratification of the new London Mining agreement. The agreement should be revised to be consistent with the country’s legislation, and to ensure that the country maximises its revenues.

FOR FURTHER INFORMATION, CONTACT NACE COORDINATOR CECILIA MATTIA IN SIERRA LEONE ON 076602470 or at 82 Soldier Street, Freetown.
ANNEX

COMPARISON OF THE CURRENT AND NEW LONDON MINING AGREEMENTS AND SIERRA LEONEAN LEGISLATION


<table>
<thead>
<tr>
<th>THE FIRST LONDON MINING AGREEMENT, 2009</th>
<th>THE REVISED AGREEMENT, 2011</th>
<th>VERDICT AND COMMENTS</th>
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<tbody>
<tr>
<td><strong>LEASE RENT</strong></td>
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<tr>
<td>US$ 5,000 per square mile and a minimum of US$ 50,000 a year (Section 5 (a)) a year</td>
<td>US$ 500,000 a year (Section 5.1)</td>
<td>Much better, and consistent the MMA</td>
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<td></td>
<td></td>
<td>The MMA sets no general rate: the terms are to be agreed between the company and landholder or Minister (Section 34)</td>
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<tr>
<td><strong>LEASE RENT II</strong></td>
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<tr>
<td>Not mentioned</td>
<td>Lease rent and surface rent payments will be treated as allowable expenses to be offset against income tax payments (Section 5.1)</td>
<td>Worse, and inconsistent with SL legislation</td>
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<tr>
<td></td>
<td></td>
<td>Neither the MMA nor ITA provide for offsetting lease rent payments against tax</td>
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<tr>
<td><strong>ROYALTY CALCULATION</strong></td>
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<td>3% royalty ‘after deducting any Sales Tax, Value Added Tax, Goods and Services Tax, export duty, levy or excise payable to GOSL’ (Section 5(b))</td>
<td>3% of the market value of the minerals calculated on sales value in an arms-length transaction. The government and LM will conclude an Advance Pricing Agreement to ensure sales are based on arms-length transaction values.</td>
<td>Better, and consistent with the MMA</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Section 148 (2) of the MMA states that the royalty is payable on the ‘market value’ of the minerals mined, not after deducting taxes paid. Section 148 (3) defines ‘market value’ as the basis for the royalty calculation, as ‘the sale value receivable in an arm’s length transaction’.</td>
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<td><strong>INCOME TAX RATE</strong></td>
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| 6% for 10 years from the date of the agreement and thereafter a rate of 30%. (Section 5 (c)) | • Years 1-3: 6%  
• Years 4-10: 25%  
• Year 11 and after: The generally applicable rate, but not exceeding 30% (Section 5.3) | Better, but still inconsistent with SL legislation. |
<p>|                                         |                             | Income tax rate for all companies is 30% (Finance Act, 2010) (Recently reduced for mining companies from 37.5%) |</p>
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<tr>
<th><strong>TAX OFFSETTING</strong></th>
<th>Not mentioned</th>
<th>Better, and consistent with the MMA</th>
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<tbody>
<tr>
<td>LM able to offset cumulative financial losses against its royalty payments until the tax value of such losses has been exhausted (Section 5(f)).</td>
<td></td>
<td>The MMA contains only one provision for exemption to paying royalties – in respect of samples of minerals acquired for testing.</td>
</tr>
<tr>
<td><strong>TAX OFFSETTING II</strong></td>
<td>In Years 1-10, LM allowed to offset against chargeable income in any year of assessment an amount that ‘will not be less than 15% of the income tax that would due if no losses were carried forward: any losses disallowed by virtue of this rule may be carried forward indefinitely without restriction’. From year 10 and after, as applicable under the Income Tax Act. (Section 5(f))</td>
<td>Better, but still inconsistent with SL legislation</td>
</tr>
<tr>
<td>LM given no limitation in carrying forward losses that can be offset against chargeable income in subsequent years. (Section 5(f))</td>
<td></td>
<td>The ITA specifies that companies are allowed to offset against chargeable income in any year of assessment ‘in-so-far as the tax payable each year will be less than 50% of the tax due if such loss is not carried forward.’ (Section 32)</td>
</tr>
</tbody>
</table>
| **IMPORT DUTIES ON CAPITAL ITEMS** | • Years 1-8: 1%  
• Years 9-10: 2.5%  
• Year 11 and after: As applicable under the Customs Tariff Act, 1978 | Better, but still inconsistent with SL legislation |
| (ie, mining machinery, plant and equipment) 1% import duty. (Section 5(j)) | | The ITA specifies an import duty of 3% (Section 114). |
| **IMPORT DUTIES ON OTHER ITEMS** | • Years 1-5: 20% of prevailing rate  
• Year 6 and after: As applicable under the Customs Tariff Act, 1978 | Inconsistent with SL legislation |
| (ie, non-capital goods, but excluding fuel) Not mentioned | | The ITA specifies an import duty of 3% (Section 114). |
| **IMPORT DUTIES ON FUEL** | The prevailing rate (Section 5.10) | Better, and consistent with SL legislation. |
| 20% of the prevailing import duty rate (Section 5(k)) | | The ITA specifies an import duty of 3% (Section 114). |
| **ROAD USERS FUEL LEVY** | LM will be exempt (Section 5(o)) | Worse, and inconsistent with SL legislation |
| 20% of the prevailing rate (Section 5(o)) | | The Road Users Charge Act, 1944, requires payment of Road Users Fuel Levy |
### WITHHOLDING TAX ON DIVIDENDS (ie, to shareholders and holding company)
5% for 10 years and thereafter at 10%. (Section 5(d))

- Years 1-6: 5%
- Years 7-10: 10%
- Year 11 and after: As applicable under the Income Tax Act (Section 5.5)

Marginally better, but still inconsistent with SL legislation

The ITA specifies that companies pay 10% withholding tax on dividends (Second Schedule). (Nb. It is unclear why the revised LM agreement differentiates between years 7-10, and year 11 and after)

### WITHHOLDING TAX ON INTEREST ON LOANS
5% for 10 years and thereafter at 10%. (Section 5(d))

- Years 1-6: 5%
- Years 7-10: 10%
- Year 11 and after: As applicable under the Income Tax Act (Section 5.5)

Marginally better, but still inconsistent with SL legislation

The Income Tax Act, 2000 specifies that companies pay 15% withholding tax on interest (Second Schedule)

### WITHHOLDING TAX ON MANAGEMENT FEES
5% for the duration of the agreement. (Section 5(d))

- Years 1-6: 5%
- Years 7-10: 10%
- Year 11 and after: As applicable under the Income Tax Act (Section 5.5)

Better

The ITA does not specify rates applicable to management fees.

### WITHHOLDING TAX ON CONTRACTS TO NON-RESIDENTS
Not mentioned

- Years 1-7: 5%
- Years 8-10: 10%
- Year 11 and after: As applicable under the Income Tax Act (Section 5.5)

Inconsistent with SL legislation

The ITA specifies that companies pay 10% withholding tax on non-resident contractors (Second Schedule). (Nb. It is unclear why the revised LM agreement differentiates between years 7-10, and year 11 and after)

### FISCAL STABILISATION
The agreement states that LM will not have to pay higher taxes even if the government generally increases such taxes (Section 6 (c))

Further, the agreement allows for its renewal for a further 15 years on the same fiscal terms (Section 3 (b)).

There is no stabilisation clause.

The agreement states that its terms will be reviewed in 2020 and that ‘any new fiscal benefits will be subject to negotiation’ (Section 6.8)

Better, and consistent with SL legislation

There is no stabilisation provision in the MMA

### COMMUNITY DEVELOPMENT
LM will pay at least 1% of gross sales to a Community Development Fund. This will be in lieu of the statutory 0.1% contribution to the Agricultural

For the first 5 years in which LM sells at least 1 million tonnes of iron ore, it will pay at least 1% of gross sales to a Community

New agreement is worse than current agreement in terms of years in which company will spend on community development, but
| **Development Fund.** Such spending can be offset against tax (Section 5 (r)) | Development Fund. Such spending can be offset against tax (Section 5.18) | **much better than SL legislation in terms of amount to be spent. It is inconsistent with legislation in terms of tax offsetting.**

Companies are required to spend only 0.1% of gross sales on community development (MMA, Section 139)

There is no provision in the MMA or ITA to offset such spending against tax. |
| --- | --- | --- |
| **NATIONAL SOCIAL SECURITY AND INVESTMENT TRUST (NASSIT)**
LM will pay employer social security contributions (NASSIT) as under prevailing legislation (Section 5(m)) | LM is exempt from NASSIT payments for its expatriate staff working in SL (Section 5.19) | **Worse, and inconsistent with SL legislation**

The National Social Security and Investment Trust Act, 2001, makes no provision for exemptions for expatriates. |
| **SCRAP METAL**
LM is allowed to ‘remove and sell for export any surplus scrap metal not required for the conduct of normal operations situated within the Mining Lease Area, free of any government charges, levies, duties or royalties’. (Section 4 (a)) | LM is allowed to remove and sell such scrap metal for export but is subject to applicable government charges (Section 4.2) | **Better, and consistent with SL legislation**

NACE is not aware that any SL legislation provides for exemption from taxes as in the 2009 agreement. |
| **AGREEMENT / MMA**
The agreement explicitly stipulates that its terms prevail over those of the MMA. (Section 3 (a)) | The agreement requires LM to comply at all times with the MMA (Section 6.2) | **This is consistent with the legislation:** The MMA applies to all mining leases. However, the terms of the agreement contradict legislation in various ways. |
| **EXCLUSIVE RIGHTS**
LM is given ‘exclusive rights’ to use or construct within the mining lease area, any roads, buildings, water supply systems, pipelines, conveyor belts, communications systems, ship loading stations, airstrips or storage facilities owned or otherwise possessed by GOSL. (emphasis added) Section 4 (d). | The agreement does not provide for such exclusive rights and sets out rights and restrictions (Sections 4.2 and 4.3) | **Better, and consistent with SL legislation**

The MMA does not grant such ‘exclusive rights’. It states: ‘The holder of a mineral right shall not exercise any of his rights under the mineral right in respect of any land dedicated or set apart for any public purpose other than mining including any street, road, highway or aerodrome except with the written consent of the responsible Minister or other authority having control over such land.’ (Section 32 (1)) |
REFERENCES

1 See, for example: http://londonminingnetwork.org/2010/03/london-mining-plc-condemned-in-sierra-leone/
2 Verdi Consulting and Grant Thornton, First Sierra Leone EITI Reconciliation Report, March 2010. The report covers six industrial mining companies and three exporters/dealers, thus the major taxpayers in the country. The report is the most extensive review of company tax payments in the country's history.
5 For example, a 2006 report by the African Department of the IMF notes that ‘available empirical evidence... mostly confirms that investment incentives – particularly tax incentives – are not an important factor in attracting foreign investment’. IMF, Kenya, Uganda and United Republic of Tanzania: Selected Issues, 1 December 2006, p.11