REVENUE MOBILISATION IN NATURAL RESOURCE PRODUCING COUNTRIES

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Background

1. Natural resource endowment offers great opportunities for achieving high levels of economic growth and development, through fiscal revenue mobilization to support infrastructure, social services, security and other productive sectors.

2. In order to achieve this noble objective, prudent management of the entire value chain of operations from exploration to extraction, beneficiation and exportation of the final product is necessary.

3. This, however, has not been the case in some resource-rich developing countries, which have not taken full advantage of the resource wealth to mobilise revenue to the fiscus.

4. Sustainable utilisation and management of natural resources such as land, water, minerals, forests, fisheries and wild flora and fauna results in poverty alleviation.

Natural Resource Producing Countries

Examples of countries rich in natural resources and level of resources over a period of five years

5. The major natural resources exports include minerals such as gold, platinum, diamonds, petroleum, other base metals, fisheries and timber, among others. The major exporters of natural resources during the last five years are highlighted in the tables below:

Product	Country	2007	2008	2009	2010	2011
Gold (Kgs)	USA	238 138	233 327	223 323	231 000	234 000
	South Africa	252 345	212 744	197 628	188 702	180 184
	Peru	170 128	179 870	182 390	164 070	164008
	China	275 000	285 000	313 980	340 880	360 960
	Australia	247 000	215 000	223 000	260 00	258 000
Platinum (Kgs)	South Africa	165 835	146 141	140 819	147 790	148 008
	Russia	28 500	25 000	24 400	26 500	26 500
	Canada	8 100	8 500	4 000	3 600	8 000
	Zimbabwe	5 086	5 495	6 849	8 639	10 827
	USA	3 857	3 577	3 826	3 450	3 700
Diamond (Carats)	Russia	38 291 200	36 925 150	34 759 400	34 856 600	35 139 800
	Botswana	33 639 00	32 595 000	17 734 000	22 019 000	22 903 000
	DRC	28 452 496	33 401 928	21 298 459	20 166 220	19 249 057
	Australia	19 231 000	15 670 000	10 795 000	9 998 000	7 562 000
	Canada	17 007 850	14 802 699	10 946 098	11 773 000	10 795 000

Source: British Geological Survey, 2013

Development Status through Indicators such as GDP per Capital and Human Development

6. In spite of the high contribution of natural resources to GDP capita income, poverty levels have remained high, especially in developing countries.

7. The table below highlights the Natural Resource rent as a proportion of GDP and the corresponding Human Development Index for selected countries:

Country	Total Natural Resources Rents (% GDP) 2010	Human Development Index 2011
Angola	46.3	148
Botswana	4.7	118
USA	1.0	4
Australia	8.3	18
South Africa	4.6	123
Zambia	28.1	164
Zimbabwe	3.4	173
DRC	29.8	187
China	4.0	101
Russia	19.9	66
Canada	3.8	6
Peru	11.3	80
Sierra Leone	4.5	180
Algeria	25.7	96
Ghana	10.5	135
Gabon	49.8	106

Source: World Bank Report (2012) and 2011 UNDP Report

8. As noted from the above table, a number of developing countries with a high natural resources share of contribution to GDP are, however, ranked very low on the Human Development Index.

9. The opportunity has, however, not been effectively used to finance socio-economic activities.

Sharing of Benefits from Natural Resources

10. Efficient management of natural resources can be achieved through equality in the distribution of benefits. For example, villagers

cannot be encouraged to conserve the local forests if tourism revenues accrue to external entrepreneurs, whilst wild animals damage their crops.

11. Furthermore, local communities have witnessed environmental degradation whereby hills, flora & fauna are destroyed in the process of mining. Pollution levels have also increased as a result of emission of waste and hazardous substances into the environment.

12. In order to promote equitable and optimal exploitation of mineral resources that underpins broad-based growth and socio-economic development, there is need to put in place a mechanism that ensures mutually beneficial partnerships between the State, local communities and other stakeholders.

Design of the fiscal regime

13. Governments, on behalf of citizens, own valuable renewable and non-renewable natural resources, which include, forests, fisheries and minerals. Non-renewable assets such as platinum, gold, or any other mineral, can only be exploited once.

14. In order to convert natural resources into financial resources, Governments should attract capital on terms that guarantee the greatest possible value for its resources.

15. Both the private entrepreneurs and Government wish to maximize rewards and shift as much risk as possible to the other party. There

is, however, scope through tax design to improve the position of both parties.

16. Design of fiscal arrangements that encourage a stable fiscal environment and efficient resource development maximizes the magnitude of the revenues to be shared. Robust fiscal regime usually includes both profit (income tax) and production (royalties) based levies.

17. In some countries, Government participates more directly as a shareholder.

18. An effective tax regime needs to balance additional risk to the investor, offer the prospect of stability of contract terms and also yield maximum revenue to the State.

19. A wide range of instruments deployed in the mobilisation of revenue from natural resources include the following:

- *Tax on inputs*

A number of countries levy import duties on inputs used in the production of natural resources, despite the consequential increase in costs of production thereby impacting negatively on efficiency.

Minimum level of import duty levied on inputs in various countries ranges between 0 and 10%.

- *Taxes on profits*

Almost all countries levy corporate income tax on profits earned from production of natural resources. Income tax systems usually consist of a basic single rate structure plus provisions for deduction of all costs from the tax base, tax incentives and capital allowance of assets within the year of acquisition.

Some countries, however, levy Additional Profit Tax, depending on the profit level of a company. Different formulae are used to arrive at the Additional Profit Tax.

The rates of corporate tax, vary among countries and range between 15 to 30 per cent.

The generous tax regime, in particular on the mining sector, results in losses being carried over for a long period of time.

- *Royalties*

Royalties are levied directly on the extraction of the resource as payment to the resource owner, usually, the Government. Royalties can be levied on an ad valorem or specific basis. The base for charging royalties can either be on the gross value of the mineral ore or the net value of exports.

Royalty rates vary according to the type of mineral across countries and are levied within a range of 0.2 and 15 per cent.

Royalties can significantly affect decisions on exploration and development of natural resources, especially if they impact negatively on profitability. High royalty rates can also affect the decision on the cut-off grade for extraction thereby leaving costly additional reserves underground.

- *Other Resource Rents*

Other resource rents include surface rentals, licensing and registration fees, competitive bonus bidding and auction fees. The level of the fees vary among countries

- *State equity participation*

Governments embrace state participation in their natural resource sectors in a variety of forms, depending on their objectives and circumstances. The state may participate through equity or a build, operate and transfer model.

The objectives of State Participation may be driven by the need to protect national interests, regulation of private sector investors and maximisation of state revenue.

A number of challenges that arise with State participation include management and funding of the state participation.

Administration of the fiscal regime

20. Mobilisation of revenue from natural resources requires sound fiscal regime and an efficient tax administration system which ensures proper valuation and accounting of natural resources.

Management of Revenues

21. Beyond the question of sustainability, natural resource-dependent economies face other important macroeconomic issues, which are often summarised as the "resource curse".

Boom-and Bust Cycles

22. The boom-and-bust nature of resource markets creates significant problems for Governments that are highly dependent on revenues from natural resources. The tendency to boost consumption expenditure during boom times is difficult to reverse when the bust arrives, resulting in soaring Government deficits, and, ultimately, in inflation and macroeconomic instability.

23. Managing resource income requires ability to buffer revenues, policies to match investment programmes to the economy's absorptive capacity for productive investments, and mechanisms for restraining expenditure when resource prices fall.

24. In the case of Zimbabwe, budgeted revenues for the fiscal year 2012 amounted to US$4.0 billion, of which US$600 million was anticipated from diamond revenue. The US$600 million had been earmarked to finance public sector investment programmes. However, a mere US$43.0 million was received from this revenue source.

25. As a result, Government incurred extra costs on contractors in the form of standing time and demobilisation costs due to disruption of activities.

26. Other countries faced the same predicament when international commodity prices of precious stones and base metals, agricultural commodities and oil tumbled. The resultant instability in prices often translates into fiscal deficits with implications on the balance of payments.

27. In 2002 to 2008, the trend decline in real mineral prices suddenly changed course with prices tripling over a five-year period, largely on account of rapid demand growth in China and other emerging market economies.

Strategies to Mitigate Impact of Burst-and-Boom in Natural Resources

28. A long-term sustainable economic development strategy demands that natural resource endowment revenues should be used to develop the productive base of the economy. Revenues derived from

natural resource should be invested to enhance future growth prospects and support diversification and value addition.

29. Some analysts advocate for the establishment of a separate Fund to manage revenues and isolate them from the general revenue pool. Others argue that the mechanism for channelling the revenues is far less important than the utilisation of the revenues.

30. The building of revenue reserves, whether as budgetary surpluses or specific Funds, and possible concomitant build-up of foreign exchange reserves is an essential element of the strategy. Revenues should be used in a manner consistent with the absorptive capacity of the economy so as to avoid macroeconomic instability and imbalance such as inflationary surges and large chronic budgetary deficits.

31. Some development analysts have argued that Governments should invest part of the large mineral revenues abroad so as not to cause overheating in the domestic economy. This was the strategy adopted by many OPEC countries during the oil boom of the early 1980s.

32. Excessive external borrowing to finance large prestige projects resulted in the collapse of some natural resource based economies. When the export markets experienced a down turn, servicing of external debt became a problem. The economic repercussions were reduction in expenditure, import controls and rationing of foreign exchange in response to reduced inflow of foreign exchange.

33. Intergenerational equity is one important subject based on the position that the present generation has no right to extract all the mineral resources and preclude their use by future generations. However, if the present generation uses the revenues to build productive capital, it is for the benefit of future generations.

34. Future generations, armed with more sophisticated and productive technologies, partly developed with the intellectual capital of preceding generations, may be able to discover many other minerals and engage in more productive activities that the present generation is ignorant about.

Conclusion

35. In conclusion, experiences that developing countries have witnessed with regards to over-dependence on revenues and export earnings from a narrow base raise challenges which require careful management.

36. In this regard, the issue of forward planning and setting aside resources for a buffer is important, in order to enhance and diversify the economy's base, thereby safeguarding future generations.