Global mining and metals tax survey
From backroom to boardroom
Introduction

EY surveyed most of the tax directors from the top 40 global mining and metals houses in the second half of 2012 to examine the challenges and issues they are now facing. This is a follow up to EY’s mining and metals tax survey in 2009, to see where the tax function has moved and how it has been affected by the dramatic changes in the mining and metals landscape over the past few years.

The tax directors provided insight into the key challenges facing the mining and metals industry, specifically around areas of resource nationalism, tax risk management, tax planning and transfer pricing.

We would like to thank and acknowledge the respondents (both named and unnamed) for their valuable time and insights:

- Alpha Natural Resources
- Anglo American
- AngloGold Ashanti
- Antofagasta PLC
- ArcelorMittal
- Barrick Gold Corporation
- BHP Billiton
- Codelco
- CONSOL Energy
- Freeport-McMoRan Copper & Gold, Inc.
- Harmony Gold Mining Company Limited
- KGHM International
- Metinvest Holding, LLC
- Newcrest Mining Limited
- Newmont Mining Corporation
- Peabody Energy
- Polyus Gold
- POSCO
- Vedanta Resources Group

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Executive summary

From backroom to boardroom
Resource nationalism has been at the forefront of the CEO and board agenda for mining and metals companies, with the role of the tax director transforming from a largely compliance-driven role to a more commercial and strategic focus. The dual challenges of resource nationalism and more tax controversy in operating jurisdictions are challenging tax directors like never before.

The tax director has taken a step forward in their role in the mining and metals organization, moving from a largely finance or treasury role to a more strategic focus, with more frequent appearances in the boardroom. To secure a more regular seat at the board table, the development of more commercial skills for tax directors requires:

- The ability to manage commercial dynamics of tax policy with an economic understanding
- Participation in the public debate of influencing tax policy
- Strategic thinking of tax planning around the mine plan

Influencing natural resources tax policy
Two-thirds of tax directors are engaged in responding to proposed or actual resource nationalism, which has become more endemic in the mining and metals sector. The three main forms of resource nationalism — mandated beneficiation, government ownership and increased taxes or royalties — have been spreading in developed and developing countries.

While most tax directors are not currently involved in negotiations with governments or policy-makers in-country on the specifics of policies or mining investment stabilization agreements, they play a supporting but increasingly strategic role in preparing the negotiating team. This is an opportunity for the tax director to step into this role which would add greatly to the negotiation process, providing key commercial solutions for the best outcome for all parties.

Sixty five percent of tax directors are consulted on tax issues before an investment is made. While it often does not set the go/no-go outcome, it does inform the decision as increased taxes are a cash cost of production that can impair investment returns.

Aligning the tax agenda with the business agenda
With the increase in tax take in the form of resource nationalism, tax has become a larger proportion of total cost, making tax planning a key component of cost reduction and cash maximization. It is not surprising that 54% of the respondents emphasized the importance of tax planning to improve cash flow, and we expect this figure to increase substantially as current pressures increase.

Mine planning is all about optimizing cash returns through reserve optimization, pit designs etc. Tax or royalties are one of the largest components of cash costs and hence feed directly into the determination of cut-off grades and mine plans. Therefore, tax planning is increasingly becoming integrated with mine planning. The pursuit of tax incentives such as R&D credits can make a significant impact on cash costs.

In addition, to optimize cash flow, the ability to defer cash tax outflows can impact the political risk assessment, especially in countries where risks are high. For instance, accelerated depreciation, which 29% of the survey respondents saw as a priority, means that the government does not have as large a claim on cash flows until the company has recouped
Global mining and metals tax survey

its costs. Therefore, this can de-risk an investment. In some instances, the deferral of tax may be preferred to a lower tax rate.

Paradoxically, while mining and metals companies are looking to maximize short-term cash flows and reduce risk, the top key performance indicator (KPI) measuring 72% of tax directors is the effective tax rate. While this may result in choices made to lower the overall tax burden, it may not maximize the near-term cash flows the board and shareholders are seeking.

Globalization: the increased importance of transfer pricing

Transfer pricing and tax-effective supply chain management (TESCM) that supports the business strategy will help to maintain competitive advantage and deliver value to shareholders. This remains an area of opportunity for mining and metals companies to optimize their tax profile.

Jurisdictions with limited natural resources are seeking to take advantage of resource wealth in other ways. These countries leverage their favorable tax regimes, an abundance of legal and financial services, stable fiscal and legal regimes and a good network of tax treaties to attract mining and metals companies. Singapore, for example, offers tax rates as low as 5% for marketing and trading operations, attracting 17% of mining and metals companies surveyed for metal trading and procurement centers. Other countries are offering tax holidays to attract downstream beneficiation.

To stem any tax revenue losses through transfer pricing, tax authorities in producer nations have taken steps to restrict tax base erosion. They have also added staff devoted to transfer pricing, as well as secured the support of the Organization for Economic Co-operation and Development (OECD) which is undertaking a major project on base erosion and profit shifting.

A growing wave of mining tax controversy

Nearly three-quarters of tax directors in mining and metals companies have experienced a rise in the volume or aggressiveness of tax audits as governments seek to protect their revenue base, with 40% citing transfer pricing as high on the radar of tax authorities. The increased number of disclosure and transparency schemes has also fueled the rise in tax enforcement.

Taking into account the harsh financial and reputational penalties that can result from a major tax controversy, tax directors and the company leadership realize that successfully and proactively managing uncertainty is a key imperative. This should include a global approach to tax risk and controversy management, making strong corporate governance in tax a priority and staying connected with global legislative, regulatory and tax administrative changes.

The pendulum of risk has swung

There has been a dramatic shift in risk appetite in 2012 where the majority of tax directors indicated their approach was “conservative” vs. “assertive” in 2009. Rising resource nationalism activity, increased focus on cash savings, globalization, and a rise in controversy have all contributed to the shift to conservatism. Reputational risk is a key driver of this conservatism for tax directors in the face of changing legislation and increasing resource nationalism. Many describe the major battleground as resource nationalism and, hence, they choose to become less of a target of revenue authorities and politicians pursuing a more populist agenda.

While this caution is understandable, it may be that striking more of a balance with a more assertive stance would lead to better tax outcomes. It is clear that mining and metals tax directors are taking a more proactive role in advising and planning for resource nationalism, cash conservation, and creating sophisticated transfer pricing structures in order to align tax planning with the strategic imperatives of their global operations. Cash flow and tax rate planning are critical to effective capital project execution, capital allocation decisions and enhancing operating margins.

Investment decisions

“Tax doesn’t drive the decision; the resource base drives the decision”

Tax director, Mining & metals

Favorable jurisdiction from an investment perspective

“The balance of tax effectiveness, business effectiveness and access to different financial resources”

Tax director, Mining & metals

Resource nationalism

“Everything is fine until you dig a hole in the ground, then they hold you hostage”

Tax director, Mining & metals

“Tomorrow’s tax director looks very different, having taken a step forward into the boardroom as one of the strategic advisors.”

Mike Elliott
Global Mining & Metals Leader
EY
From backroom to boardroom

External influences on the tax function

- Tax administrations around the world have become more aggressive and assertive
- The high pace of legislative change has created more risk and uncertainty
- Globalization has had a dramatic effect on business models
- A new breed of tax activism has emerged
- Growing disclosure and transparency requirements are providing fuel for the fire
- Expansion in emerging markets is creating tax risk and uncertainty

Tax function
- Vision and strategy
- Policies
- Resources, processes, systems
- Corporate governance
As the number one strategic risk for the sector over the past couple of years, resource nationalism has been at the forefront of the CEO and board agenda for mining and metals companies. The role of the tax director has, therefore, changed from a largely compliance-driven role to a more commercial and strategic focus. The dual challenges of resource nationalism and more tax controversy in operating jurisdictions are challenging tax directors like never before.

Seventy-two percent of mining and metals tax executives named dealing with tax authorities as their top challenge. Tax administrators and legislators, under pressure to generate more revenue to balance debt-laden budgets and fund infrastructure and social programs, acknowledge that they are more committed than ever to enforcing existing tax law and creating new enforcement mechanisms.

As mining and metals companies have expanded their operating and customer base, there has been an increase in the need to find efficiencies, both in effective tax rate and business operations. Add the significant increase in controversy and compliance requirements to this, and you can see that the tax planning process has become significantly more complex. The survey findings confirm what all tax executives know: they need to do more with less. Successful tax functions are ensuring that the tax planning is aligned with the overall strategy of the business. That way the tax executive can anticipate future planning opportunities such as in transactions and supply chain management (transfer pricing opportunities).

Optimizing the use of information technology in compliance and financial reporting will be critical to the success of a tax function to free up resources to influence tax policy. Streamlining and simplifying the overall business operating model was also an area that needed more focus – improving the internal policies and procedures would enable the tax department to do more with fewer resources. By improving interaction with other departments, the tax team should be able to identify more tax planning opportunities and demonstrate the value of tax to the organization.

In light of these pressures, tax directors have to ensure they have the capability and resources to:

1. Enter into tax policy debates in the context of increased resource nationalism and transparency initiatives
2. Defend increasing controversy
3. Streamline processes and do more with either the same or fewer resources
4. Be able to implement sophisticated transfer pricing solutions
5. Continue to increase their engagement and visibility with the board of directors

Implications for tax directors

1. Develop critical negotiating and relationship-building skills.
2. Establish taxation objectives in line with business strategy and espoused risk appetite.
3. Consider automation of compliance activities to free resources.
4. Spend more time in the business.

What are the main challenges facing your tax function for the next 12 months?

- Dealing with tax authorities and audits: 35% (2012), 72% (2009)
- Resourcing: 28% (2012), 44% (2009)
- Transfer pricing: 16% (2012), 23% (2009)

Global mining and metals tax survey
Influencing natural resources tax policy

The super-cycle of the past decade has fed resource nationalism to become more endemic in the mining and metals sector. This trend is widespread, with the three main forms of resource nationalism — mandated beneficiation, government ownership and increased taxes or royalties — spreading over the past five years in both developed and developing countries.

Resource nationalism (proposed and actual) 2008-12

Source: EY research
We see continued pressure on government budgets driving resource tax policy debates, even as commodity prices decrease. Resource nationalism remains an issue that impacts sustainability and the broader social license to operate of miners.”

Scott Grimley
Oceania Mining & Metals Leader
EY

65% of tax directors are engaged in planning for responses to proposed or actual resource nationalism. This figure will rise as resource nationalism continues to gather momentum.

65% of tax directors are consulted on tax issues before a company invests in exploration, or expands an existing mine in a jurisdiction. EY analysis shows that resource nationalism impacts investor confidence and affects the investment decision of exploration than on later-stage production (where large sunk material costs exist). In many companies, project risk assessment at the exploration stage now includes an assessment of resource nationalism and impacts the “go” or “no-go” decision on major developments.

Once a project is in development or production stage, resource nationalism must be continually monitored to assess risks to mine plan, additional capital deployment, as well as, potential asset divestment and capital redeployment. Tax directors need to be able to advise on the impact of new taxes or other forms of resource nationalism that is introduced mid-way through the project.

Changes in government policy may materially impact future investment decisions. Resource nationalism will have more bearing on the decision to not invest further in a jurisdiction than if capital has already been committed. Only a couple of companies surveyed have decided to divest assets or projects in a jurisdiction, as a result of increased taxes or resource nationalism. While resource nationalism is not always the primary risk in a decision to expand an asset, it may be an important factor in how fast a resource is developed.

Increased taxes are a cash cost of production that likely impairs projected investment returns. If the mine becomes uneconomic, the entire investment may become impaired.

88% of tax directors are not currently involved in the negotiations with governments or policy-makers in-country on the specifics of new or existing policies or mining investment stabilization agreements. However, tax directors have been playing a supporting but increasingly strategic role in providing tax policy information to the government affairs or in-country business team, together with the CEO and government relations officer, who lead the actual negotiations. The long-term view by the company or final decision is usually taken by the CEO and the board.

The leading practice for tax directors is to have an overarching understanding of the location and extent of potential investments to allow them to promote a consistent approach to responding to tax-related policy or legislative changes around the world. This minority of tax directors are then highly active in the negotiations with government. Also, implementing a benchmarking methodology to assess the extent of changes in different countries would be beneficial. Tax directors should be able to advise on the appropriate level of tax in countries based on comparative investment profiles and respond to an assessment of tax risk in the particular jurisdiction.

Has your company decided not jurisdiction in the past two or three years because of resource nationalism?

- Increased taxes are absorbed as a cost of production
- We make sure we have mining investment stability agreements in place so the impact is understood
- Where resource nationalism is deemed too great a threat – the company has decided not to expand
- Considered but hasn’t either made or broken a decision yet
- No, if we were scared of it, we wouldn’t be in business

Global mining and metals tax survey
Responding to the challenges of resource nationalism

In this survey, tax directors gave us their views on how mining and metals companies should respond to the challenge of resource nationalism. These include:

- Increasing engagement with governments
- Being transparent on what a miner can bring to a community, but also be clear about the expectation of shareholder return
- Ensuring a level playing field through transparency initiatives, reporting such as the Extractive Industries Transparency Initiative (EITI), contractual arrangements, tax regimes
- Describing the concept of how long-term costs far outweigh short-term gains
- Working with local governments through local representatives
- Using independent analysis to help educate policy-makers about optimizing returns to the host jurisdictions
- Ensuring the board has reputable and influential directors
- Participating in and being a member of local country industry bodies (e.g., Chamber of Mines, etc.)
- Lobbying through formal channels
- Negotiating tradeoffs - streamlined permitting processes, efficient tax regime, eliminating certain tax levies, etc.

These additional responsibilities in responding to resource nationalism are challenging the skill sets of tax directors and their teams in mining and metals companies. Increasingly, the tax function is looking to regularly access more valuation, economics and public policy skills.

We see mining and metals companies adopting more transparent approaches with governments and describing in greater detail the respective risk and reward for both the government and the company. We believe collaboration and communication need to remain open so there are no surprises and an appropriate share of the wealth generated is established without either side risking the withdrawal of investment.

To ensure this, transparency of both the tax administration process and taxpayer behavior is necessary. In addition, compliance by all parties to any investment stabilization agreement and a consistent application of law and regulations is critical to long-term sustainable development of a country’s natural resources.

Implications for tax directors

1. Upskill in areas such as valuations, economics and public policy engagement and negotiation.
2. Network with other stakeholders impacted by resource nationalism.
4. Integrate tax alternatives with other potential policy trade-offs.
Aligning the tax agenda with the business agenda

“Mining and metals companies are seeking to maximize short-term cash flows and tax as a very significant cash cost has an important role to play to deliver this goal.”

Corlie Hazell
African Mining & Metals Tax Leader
EY

Cash is king in a volatile operating environment, with shareholders demanding greater distribution of operating cash flow. With the spread of resource nationalism, tax has become a larger proportion of total cost, making tax planning a key component of cost reduction and cash optimization. It is not surprising that 54% of respondents emphasize the importance of tax planning to improve cash flow.

Mine planning is all about optimizing cash returns through reserve analysis, pit design, etc. Tax or royalties are one of the largest components of cash costs and hence feed directly into the determination of cut-off grades and mine plans. Therefore, tax planning is increasingly becoming integrated with mine planning. The pursuit of tax incentives can make a significant impact on cash costs.

Progressive tax directors are treating tax cash flow holistically and are looking at the tax-efficient repatriation of cash, releasing cash trapped in supply chains, taking advantage of government incentives such as research and development, accelerated depreciation, reduced employment taxes and refundable duties.

In addition, when looking at optimizing tax cash flow, the ability to defer cash tax outflows can be a de-risking strategy in countries where political risk is high. Twenty nine percent saw this as a tax planning priority. For instance, accelerated depreciation means that the government does not have a claim on as much cash flows until the company has recouped its costs. This lowers the amount of un-recouped investment at risk and can de-risk a project. In some instances, this deferral of tax may be preferred to a lower tax rate.

What are your top considerations in tax planning?

<table>
<thead>
<tr>
<th>Consideration</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Cash flow savings</td>
<td>54%</td>
</tr>
<tr>
<td>Risk mitigation</td>
<td>29%</td>
</tr>
<tr>
<td>Efficient tax structure/simplification of process</td>
<td>21%</td>
</tr>
<tr>
<td>Reputation risk – government reaction/media</td>
<td>21%</td>
</tr>
</tbody>
</table>
Deferring taxes paid can also postpone a decision to put a mine on care and maintenance, providing the opportunity to keep a marginal property operating. This degree of sophistication requires extensive tax planning.

The companies with best-practice cash tax programs have considered and can answer the following questions in their tax planning:

- Is cash repatriation optimized?
- Where are the available refund opportunities?
- Have all incentives arising from fiscal stimulus been considered?
- Is there a trade-off between income and indirect tax cash optimization?
- What can be done to optimize the timing of tax collections and payments?
- How can we reduce our overall taxes and create opportunities for cash repatriation?
- What can we do to reduce our global tax liability and facilitate cash repatriation to service our debt?

Increased scrutiny by the tax authorities as they seek to maximize their take from resource companies and increased legislative requirements mean tax directors have become more conservative in their approach to tax planning. For example, tax authorities are increasingly looking to see what business drivers exist for tax planning – see recent amendments to Part IVA in Australia and the proposed introduction of the General Anti-Abuse rule (GAAR) in the UK. In the recent EY Global Tax risk and controversy survey, 81% of tax policy-makers see growth in GAAR and other anti-avoidance legislation in the next three years. The recent OECD paper on Base Erosion and Profit Shifting (BEPS) is another example where tax policy makers are looking at anti-avoidance measures. Resource nationalism is increasing differentials in tax rates between countries providing incentives to undertake greater

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Which incentives and types of offsets is your company interested in?

<table>
<thead>
<tr>
<th>Incentives/Offsets</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower corporate tax rate</td>
<td>29%</td>
</tr>
<tr>
<td>Accelerated depreciation</td>
<td>29%</td>
</tr>
<tr>
<td>Mining investment stability agreements</td>
<td>24%</td>
</tr>
<tr>
<td>Tax credits (e.g., for R&amp;D/exploration)</td>
<td>24%</td>
</tr>
</tbody>
</table>

What are the key performance indicators for senior tax function personnel within your organization?

<table>
<thead>
<tr>
<th>Key Performance Indicators</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effective tax rate/minimizing tax burden</td>
<td>72%</td>
</tr>
<tr>
<td>Timely compliance</td>
<td>38%</td>
</tr>
<tr>
<td>Risk mitigation</td>
<td>25%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Key Performance Indicators</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>Effective tax rate/minimizing tax burden</td>
<td>72%</td>
</tr>
<tr>
<td>2009</td>
<td>Effective tax rate/minimizing tax burden</td>
<td>43%</td>
</tr>
</tbody>
</table>

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1. New start date for proposed amendments to Australia’s general anti-avoidance rule, EY, 19 November 2012.
tax planning but enforcement activity is dampening this desire.

It is interesting that while mining and metals businesses are looking to maximize short-term cash flows and reduce risk, the principal KPI used to assess tax directors is the effective tax rate. This may result in choices that while lowering the overall tax burden, may not maximize near-term cash flows.

The continued external pressures — a weak global economy, continued resource nationalism, greater pressure on mining companies to be transparent and increased aggressiveness by revenue authorities — has led to greater importance of tax management leading to greater engagement of the tax director at board level. This is borne out of the fact that 36% of tax directors surveyed felt they were more engaged at board level than when we conducted this survey in 2009. Engagement has become a two-way dialog, particularly as boards of directors set the risk appetite for tax and need to understand the tax profile of the company. This enables the board to have the information it needs to drive the broader business agenda.

Over the past three years, how has your tax function engaged at board level?

<table>
<thead>
<tr>
<th>Engagement</th>
<th>Percentage</th>
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</thead>
<tbody>
<tr>
<td>More engaged</td>
<td>36%</td>
</tr>
<tr>
<td>Just the same</td>
<td>32%</td>
</tr>
<tr>
<td>Through CFO</td>
<td>12%</td>
</tr>
<tr>
<td>Less engaged</td>
<td>4%</td>
</tr>
</tbody>
</table>

Implications for tax directors

1. Look at cash flow strategically and from a whole of mine point of view.
2. Pro-actively approach mine planning to identify tax or royalty cash flows.
3. Ensure that tax planning for cash flow savings has clear business drivers.
4. Adjust KPIs of the tax director and tax team to reflect their role of near-term cash maximization.
5. Play an important role in informing the board of the tax implications of the broader business agenda.
6. View incentives as a component of cash costs not effective tax rates.
Globalization: the increased importance of transfer pricing

"Transfer pricing principles can be used to properly push expenses to the operating subsidiaries and bring income back to the parent company. Indeed parent host country tax authorities generally require the allocation of these expenses to the foreign operations. Likewise, foreign operations tax authorities require those expenses to be duly supported."

Alicia Dominguez
South American Mining & Metals Tax Leader
EY

Transfer pricing and tax-efficient supply chains remain an area of opportunity for the mining and metals sector. The best-in-class companies can move from being run as multinational to truly global, integrated organizations with an optimized taxation profile properly aligned with the business operations.

More than ever, transfer pricing and tax-effective supply chain management (TESCM) that supports the business strategy will help to maintain competitive advantage and give value to shareholders. However, the new government initiatives to ensure that transfer pricing and other cross border structuring is not undermining their own revenue stream means it has to be done carefully.

Increasing globalization and the growing tax rate differential between countries with natural resources and those without is increasing the importance of transfer pricing optimization. Jurisdictions without natural resources are seeking to take advantage of resource wealth in other ways. These countries leverage their favorable tax regimes, an abundance of legal and financial services, stable fiscal and legal regimes and a good network of tax treaties to attract mining companies to set up downstream functions in their jurisdictions. Singapore for example, offers tax rates as low as 5% for marketing and trading operations compared to 10% in Swiss hubs of Geneva and Zug. Other countries are using tax holidays to attract downstream beneficiation activities.

Mining and metals companies are centralizing or considering centralizing functions or activities to reduce cost and enhance operating efficiency. In particular, we noted an increase in respondents (39% of the total) considering the centralization of commodity trading. Recent media reports that major commodities houses and natural resources companies are either moving their incorporation into Singapore, such as Trafigura, or locating regional hubs there – Xstrata, BHP Billiton or Anglo American.

Tax authorities are, however, taking a closer look at transfer pricing structures and tax efficient supply chains. In producer nations, governments are focusing attention on the potential for loss of tax revenues through international activity that may reduce their corporate tax bases. For example, look at recent changes in Brazil and Peru where the transfer price
of metals must be based on market prices, thus diminishing the ability to impose discounts to the advantage of related party trading hubs. With support from the G20 and individual finance ministers, the OECD is undertaking a major project on Base Erosion and Profit Shifting (BEPS).

As noted, it will become more complex to implement these centralized activities because countries are implementing more market-based pricing rules such as those recently introduced in several Latin American countries. There is also the more aggressive policing of OECD-style transfer pricing rules.

Tax authorities are also adding staff devoted to transfer pricing. In a climate of budget freezes for many government agencies, tax authorities appear to have made the cost/benefit calculation to incur additional staffing costs in order to investigate transfer pricing. The penalty burden is also increasing. The particular danger areas are Argentina, Brazil, China, Colombia, Ecuador, Finland, Hungary, Indonesia, Italy, Kazakhstan, Malaysia, Mexico and Venezuela because of their high penalty rates and their demonstrated willingness to impose these penalties.

In light of this government action, tax directors need to ensure that they:
- Are not complacent on their transfer pricing risk as it changes over time
- Pursue with more certainty and evaluate advance pricing agreements (APAs) and rulings more than ever to better manage the growing geographic footprint of transfer pricing requirements, as well as the additional risk of adjustments and penalties
- Adopt new approaches to consistent global documentation and benchmarking to remain efficient and cost-effective when preparing transfer pricing documentation

Implications for tax directors

1. Ensure a global, integrated approach is taken to tax optimization, moving away from an operational or jurisdictional lens.
2. Understand what benefits are available from non-producer locations.
3. Be vigilant about changes to global and government regulation of transfer pricing and ensure you are complying.
4. Correctly implement transfer pricing and tax efficient supply chains to support business strategy and provide a competitive advantage.
5. Invest in high quality documentation to defend any future challenges.

Do you currently have, or have you considered centralizing any of the following functions or activities?

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Function</th>
</tr>
</thead>
<tbody>
<tr>
<td>57%</td>
<td>Financing</td>
</tr>
<tr>
<td>52%</td>
<td>Procurement</td>
</tr>
<tr>
<td>43%</td>
<td>Technical services (incl. R&amp;D)</td>
</tr>
<tr>
<td>39%</td>
<td>Commodity marketing hub (trading)</td>
</tr>
<tr>
<td>26%</td>
<td>Logistics/shipping</td>
</tr>
<tr>
<td>17%</td>
<td>Exploration hub</td>
</tr>
<tr>
<td>17%</td>
<td>Processing</td>
</tr>
</tbody>
</table>

A growing wave of mining tax controversy

Enforcement has climbed rapidly and tangibly as governments seek to protect their revenue base; 72% of tax directors in mining and metals companies confirm that they have experienced a rise in the volume or aggressiveness of tax audits.

The increased number of disclosure and transparency schemes has also fueled the rise in tax enforcement and shows continued growth potential. Such schemes cover both the reporting of uncertain tax positions at the time of filing a tax return and the required disclosure of tax-planning schemes classified as supporting tax avoidance.

Not surprisingly, 40% indicated that transfer pricing is high on the radar of revenue authorities. We would expect this to be the case with increasing enforcement across the world, following the financial crisis, and in line with the increase in resource nationalism activity. Raising revenue often appears to be more of a focus than points of tax principle.

In which areas have you seen an increase in focus by revenue authorities?

<table>
<thead>
<tr>
<th>Area</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transfer pricing</td>
<td>40%</td>
</tr>
<tr>
<td>Transactions</td>
<td>20%</td>
</tr>
<tr>
<td>All areas</td>
<td>16%</td>
</tr>
<tr>
<td>Indirect taxes</td>
<td>16%</td>
</tr>
<tr>
<td>Income tax</td>
<td>12%</td>
</tr>
<tr>
<td>Tax credits</td>
<td>12%</td>
</tr>
<tr>
<td>Withholding taxes</td>
<td>8%</td>
</tr>
</tbody>
</table>
Global controversy management

Tax directors are now simultaneously managing changing business models, a shifting economy, complex and fast-paced legislation, and an approach to tax enforcement that is evolving rapidly. Taking into account the harsh financial and reputational penalties that can result from a major tax controversy, the leaders realize that successfully and proactively managing uncertainty is a key imperative.

What success looks like:

- A global vision and strategy for controversy management is developed. Taking a global approach to tax risk and controversy management is important, because tax administrators are increasingly taking a global view of companies.
- A focus is in place on developing and improving the relationships with local tax authorities in key jurisdictions by demonstrating appropriate behaviors of transparency, collaboration and accountability.
- Tax controversy risk management protocols and processes are built into tax planning and compliance processes.
- The board and audit committee receive regular reports regarding the tax implications of specific business decisions.
- The proper corporate governance is in place over tax risk and controversy management, illustrated by the existence of aligned and complementary tax risk policy and tax controversy policies.
- The right talent and resources to deal with controversy and risk management – across a matrix of leadership, geographic and technical dimensions – is obtained, retained and appropriately trained on an ongoing basis.
- Criteria are developed and put in place for the proper identification of those business transactions that should be managed proactively to avoid or mitigate controversy.
- All major tax areas for potential tax policy, legislative and regulatory change, and tax administration focus areas in key jurisdictions are closely monitored, and change is integrated into tax risk planning.
- Increased disclosure requirements bring challenges in terms of onerous compliance, but they also bring opportunities to approach government and tax administrations and ask for clearer guidance.

Implications for tax directors

To effectively manage your organization’s tax risk and increased controversy, a five-step approach can be taken:

- Adopt a global approach to tax risk and controversy management
- Evaluate global resources, processes and systems for tax risk management
- Address tax risk and controversy at a strategic level – and execute well
- Make strong corporate governance in tax a priority
- Stay connected with global legislative, regulatory and tax administration change

Disclosure of government payments

Three major transparency efforts have emerged to require disclosure of government payments. The first was the Extractive Industries Transparency Initiative (EITI), which is a set of reporting standards published by a coalition of companies, governments and non-governmental organizations. EITI was followed by legislation, enacted in the United States under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which requires certain disclosures by natural resource extractive companies that are subject to the reporting requirements of the US Securities and Exchange Commission (SEC). Finally, the European Union (EU) is considering a new directive dealing with financial reporting that would require that certain large natural resource extractive industry undertakings and public interest entities to report payments to governments.

Forty eight percent of the companies surveyed are preparing to report under these new disclosure rules. A further 24% already make voluntary disclosures – this has helped them to negotiate effectively in-country and seems to be an emerging best practice in the industry.
The pendulum of risk has swung

“Recent developments, including greater government scrutiny, increased resource nationalism and reduced staffing, have led to a more conservative focus on tax risk. However, it may be that a more assertive stance would lead to better tax outcomes.”

Salim Amersi
EMEIA Mining & Metals Tax Leader
EY

There appears to be a dramatic change in risk appetite in 2012 where the majority of tax directors indicated their approach was “conservative” vs. “assertive” in 2009.

Rising resource nationalism activity, increased focus on cash savings, globalization and a rise in controversy have all contributed to the momentous shift in risk appetite. Reputational risk is a key driver of this conservatism for tax directors in the face of changing legislation and increasing resource nationalism. Many describe the major battleground as resource nationalism and hence they choose to become less of a target of revenue authorities and politicians pursuing a populist agenda.

While this caution is understandable, it may be that striking more of a balance with a more assertive stance could lead to better tax outcomes. It is clear that mining and metals tax directors are taking a more proactive role in advising and planning for resource nationalism, cash conservation, and creating sophisticated transfer pricing structures in order to align tax planning with the strategic imperatives of their global operations. Cash flow and tax rate planning are critical to effective capital project execution, capital allocation decisions and enhancing operating margins.

Would you describe your focus on tax planning and reporting as conservative, passive, aggressive or assertive?
An increasingly proactive approach that incorporates tax risk management into strategic decision-making can reap benefits that include:

- Gaining greater certainty and ability to plan
- Releasing of cash from the provision
- Resolving issues in a more timely manner
- Reducing tax compliance costs
- Freeing up the best people from managing complex tax controversies and litigation
- Increasing prospects of a lighter tax audit focus in the future

**Implications for tax directors**

1. Need to integrate tax risks with overall risk appetite.
2. Redeploy resources to areas of greatest tax risk.
4. Use technology to improve the level of tax risk visibility.
5. Welcome reviews of internal or external audits.
6. Create greater certainty by entering “enhanced” relationships with revenue authorities.
7. Be prepared to report on tax risk to the audit committee at regular intervals.
About EY’s Global Mining & Metals Center

With a strong but volatile outlook for the sector, the global mining and metals sector is focused on future growth through expanded production, without losing sight of operational efficiency and cost optimization. The sector is also faced with the increased challenges of changing expectations in the maintenance of its social license to operate, skills shortages, effectively executing capital projects and meeting government revenue expectations. EY’s Global Mining & Metals Center brings together a worldwide team of professionals to help you succeed – a team with deep technical experience in providing assurance, tax, transactions and advisory services to the mining and metals sector. The Center is where people and ideas come together to help mining and metals companies meet the issues of today and anticipate those of tomorrow. Ultimately it enables us to help you meet your goals and compete more effectively.

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