Committee of Experts on International Cooperation in Tax Matters

29th Session, Geneva, 15-18 October 2024

Co- coordinator's Report
on
Taxation of the Extractive Industries

DESA Department of Economic and Social Affairs

UN Tax Committee

Financing for Sustainable Development

Draft papers for the Committee

1) **Mineral Product Valuation:**

   The report outlines the significance of accurate product valuation in preventing profit shifting in the natural resources sector. It reviews available examination techniques for tax administrations and addresses the practical challenges they face, and proposes ways for governments to better address these valuation issues.

2) **Energy transition:**

   This paper explores the intersection of tax policy and energy transition, with a focus on energy production. It examines various approaches to energy transition, and proposes tax policies to boost clean energy investment in developing countries. It also provides practical guidance, using examples from various countries to illustrate potential outcomes.

Draft papers for the Committee

3) Tax Incentives:

This paper addresses the interaction between Global Minimum Tax rules and incentives in the extractive industries, ensuring that incentives remain effective without causing unintended consequences.

It builds on the comments received at the Twenty-seventh Session. It is now structured as a supplement to Chapter 5 on Tax Incentives in the UN Handbook on Selected Issues for Taxation of the Extractive Industries by Developing Countries.

Mineral Product Valuation

Products Valuation is Complex and Requires Judgment, Often Leading to Tax Controversy:

- In many cases, valuation begins by identifying a posted, or index, price for the product. Identifying an index price (if one is even available for the particular product) is only the beginning, however, of the valuation process.

Mineral Product Valuation

- To determine an arm's-length price, the index price must be adjusted to account for, among other things, product quality (e.g., presence of impurities in extracted ore), any processing or refining that occurs prior to export, the duration or other terms of the contracts by which the MNE group sells the extracted product to customers, and arrangements within the MNE group for hedging of foreign currency or product-price risks. See OECD TP Guidelines paragraph 2.20.
- The necessary adjustments typically requires judgment on which taxpayers and tax authorities can disagree, resulting in extended controversy and uncertainty for both government and taxpayer. Controversy can include difficult disputes over access to taxpayer group's sales contracts with third-party customers.

Mineral Product Valuation

Procedural Measures Addressed in Report:

- Paper discusses several procedural approaches that might, in some circumstances, promote more effective resolution of valuation questions:
  - "Administrative pricing" modeled on Norway's system for pricing North Sea oil
  - Advance pricing agreements (APAs) and similar arrangements
  - Pricing safe harbors
  - Simplified valuation methods under "Sixth Method"

Mineral Product Valuation

Three Central Recommendations:

- Countries' laws should ensure tax authorities **access to taxpayer documents and records of sales to third parties,** to permit high-quality review of pricing under arm's length principle.
- Countries should **consider fiscal mixes weighted ore toward royalties, especially variable royalties,** as royalties are less sensitive to product undervaluation, and less vulnerable to profit shifting, than taxes based on net income.

Mineral Product Valuation

Three Central Recommendations:

- **Technical assistance and capacity-building should give greater emphasis to long-term, direct involvement of experts** in tax examinations and negotiations with investors, while maintaining safeguards of taxpayer confidentiality.

Energy transition

Scope of paper and changes from 28th session

- Considers the working mandate to
  - Extend scope of work to cover electricity production
  - Limit focus to tax issues related to transition in energy production
  - Improve focus on developing countries
- Shaping the paper
  - Uses International Renewable Energy Agency's (IRENA) 1.5°C pathway as a roadmap for energy transition to zero-carbon sources by 2050
  - Accordingly, paper focuses on decarbonisation of energy production - transition to renewables, hydrogen, CCS and sustainable biomass
  - Considers examples from both developed and developing countries but focuses on workable options for developing countries.
- Limitation in scope
  - Interaction with carbon taxation/pricing and fossil fuel subsidies
  - Avoid wider issues of climate change
  - Avoid other market based or regulatory measures to achieve energy transition
  - Avoid discussion of local/subnational taxation while acknowledging importance

Energy transition

Changes made from version in 28th session

- In Section 1
  - Inclusion of an Exec. Summary

- Narrowing down to tax issues (Section 2)
  - Reduction of discussion of broader climate goals and commitments
  - Sharpened focus on developing countries
  - Consolidated and shortened “diversification of energy portfolio” Section (previous 3) into this Section
  - Enhanced discussion circular economy
  - Consolidated subsection on role of tax policy in transition including addressing current energy sector

- The comparative landscape (Section 3)
  - Narrative paragraphs reduced and cross reference made to Incentives paper and PCT Toolkit update
  - Inventory of measures updated for more developing country examples

Energy transition

Changes made from version in 28th session:

- Direct tax measures (now Section 4)
  - Text updated in line with comments from 28th session
  - Edit made to cross border issue on taxation of resource rights to reference just UNMC
- Indirect tax measures (now Section 5)
  - Text shortened where possible
- Transition in the extractive industry (now Section 6)
  - Discussion on nuclear energy removed
  - Consolidation of text around green hydrogen and removal of duplicative sections
- Tax policy design (now Section 7)
  - Narrative paragraphs reduced
  - Edits to address limited fiscal headroom in developing countries
- Ancillary matters and tax administration (Now Secs 8 & 9)
  - Edits to text
  - Increased emphasis on coordination and building capacity

Tax incentives and the extractive industries

Supplement to Chapter 5 of the Handbook on Taxation of the Extractive Industries

Tax incentives and the extractive industries

Role of the supplement

- Aim
  - To specifically address the interaction between Global Minimum Tax rules and extractives industry incentives
  - To ensure incentives remain effective while not having any unintended consequences
- Built on Tax Incentives in the Extractives Industries chapter
- Structure:
  - Framework for considering tax incentives
  - Application of the framework
  - Typical incentives in the sector
  - Cost and benefits of incentives

Tax incentives and the extractive industries

Evolution of this supplement

- Newly presented to the Twenty-ninth Session of UN Tax Committee
- Initially presented at the Twenty-seventh Session as a separate paper, where it received comments for improvement
  - Recrafted as a supplement to the existing chapter
  - Additional review to ensure that this is wholly explanatory
- May technical meeting focused on addressing Committee concerns
- Reviewed and updated by the Sub-committee
- Now asking for approval for the Supplement

Issues for the Committee

The Subcommittee submits for ***first consideration:***

- A draft guidance on the Valuation of Mining Products for Tax Purposes;
- A draft supplement to Chapter 5 of the UN Handbook, addressing the interaction between Tax Incentives and the Global Minimum Tax in the Extractive Industries;

The Subcommittee submits for ***second reading:***

- A draft paper on Energy Transition in extractive industries.

Thank you