



# Financial analysis of the Acacia Mining tax dispute

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**Acacia Mining PLC (Acacia) is a UK listed company that owns three gold mines in Tanzania.** Acacia Mining PLC owns – either directly or via other subsidiaries - 100% of the shares of a number of Tanzanian companies that directly own the mines.

**Over 2010 – 2015 Acacia has paid \$444 million dividends to its shareholders, despite not yet paying any income tax in Tanzania.**

**The Tanzanian Revenue Authority seeks to impose 10% withholding tax on these dividends, as would apply if Acacia were a Tanzanian company.** TRA's argument is that Acacia Mining PLC has a "Permanent Establishment" in Tanzania, and is therefore itself taxable in Tanzania rather than just its Tanzanian subsidiaries. Acacia's likely counter-argument is that day to day management is done by the management team in Tanzania, while Acacia Mining PLC is simply a holding/investment company and only resident for tax in the UK. The Tanzanian courts have so far rejected Acacia's appeals.

**Open Oil's analysis, based on a reading of company accounts and a [full financial model of the Bulyanhulu mine](#), available online, reveals:**

1. A feature in the tax rules originally applied to the mines - the Additional Capital Allowance (ACA) - means that income tax only applies after positive cashflows cover 100% of investment plus a 15% margin. Our modelling suggests that Bulyanhulu alone accumulated some \$500 million of ACA, which is yet to be fully offset by profits – this is why Bulyanhulu has not yet paid tax. Each \$1 of ACA reduces Tanzania's tax by 30 cents.
2. Acacia could have used intergroup debt financing - possibly via their Barbados Group Financing Company - to repatriate net cashflows from its Tanzanian subsidiaries back to the UK parent company without any of its three operating Tanzanian subsidiary companies having to declare dividends.
3. From 2009 to 2015 period, Acacia's Tanzanian mines generated \$2.5 billion of profits (before deducting depreciation), but most of this has been reinvested as capital expenditure in the mines, which is immediately tax-deductible. So the mines *are* profitable, but have required more capital, so net cashflows to date are modest.
4. Over this period the \$191 million of dividends paid by Acacia out of profits are broadly consistent with the \$239 million in cash generated. The \$253 million special dividend paid in 2010 is a return of capital to shareholders who tried to buy shares at flotation.
5. There appears to be confusion between current period profitability and a carried forward tax-loss position that 100% immediate write off of capital and the ACA has resulted in. A mine can be currently profitable and yet still have a net carried forward tax loss.

6. Our modelling suggests Bulyanhulu should start to pay income tax in 2020.

## Background

Acacia Mining PLC (Acacia) is a UK listed company, majority owned by mining giant Barrick Gold, that owns several of the major gold mines in Tanzania.<sup>1</sup> So far these mines have paid little if any income tax in Tanzania, despite years of production at high gold prices. Bulyanhulu alone has produced over three million ounces of gold since start up, which have sold for over three billion dollars on world markets.

Up to the end of 2015 Acacia Mining had paid dividends to its shareholders of \$444 million. The Tanzanian Revenue Authority (TRA) is seeking to impose withholding tax on these dividends [link to article], arguing that despite it being a UK company Acacia Mining is subject to Tanzanian tax rules as it has a “permanent establishment” in Tanzania.

We consider two questions:

1. How is it that Acacia Mining is paying dividends in the UK – which have to be out of profits – but still not paying tax in Tanzania?
2. How likely is it that the Tanzanian government will be able to collect withholding tax?

We have analysed Acacia financial statements from 2009 to 2015, summarized in Table 1. Most of the numbers we use come from the Segment Reporting note that shows the breakdown of Acacia group profit and other key information across each of the mines.<sup>2</sup> From that note we use EBITDA (Earnings Before Interest, Tax, Depreciation and Amortization) as a proxy for profit before capital expenditure or depreciation deductions. EBITDA minus capital expenditure is thus consistent with net cashflows generated.

**The dividends:** Acacia has paid \$444 million in dividends, of which \$253 million was a “special dividend” in 2010. This was in effect a return of capital to shareholders after an oversubscribed initial public offering (IPO) in March 2010. So, \$191 million has been paid out of profits. We see it as unlikely that the Tanzanian government will get to impose withholding tax on the special dividend, thus the question is whether Tanzania collects 10% dividend withholding tax (on what would then be classified as branch profits) on the \$191 million.

**The profits:** Acacia generated \$239 million of net cashflows over 2009 – 2015. This is made up of \$2,483 million EBITDA generated by the Tanzanian mines, minus \$265 million corporate costs minus \$1,929 million capital expenditure minus \$51 million finance charges. So Acacia has paid out \$191 million dividends out of \$239 million net cashflows. The Tanzanian mines are generating substantial profits but these have been largely soaked up through continued capital investment and corporate costs.

**The Tanzanian fiscal regime:** Acacia’s Tanzanian mines operate under fiscal rules agreed at the end of the 1990’s that remain fixed (“stabilized”) under confidential Mining Development Agreements - though the main fiscal terms of these are in the public domain, as documented in Open Oil’s report on Bulyanhulu [link]. After a 4% royalty, the projects pay 30% tax on profits. But, capital expenditure is immediately deductible and - until 2006 – the mines were also allowed to

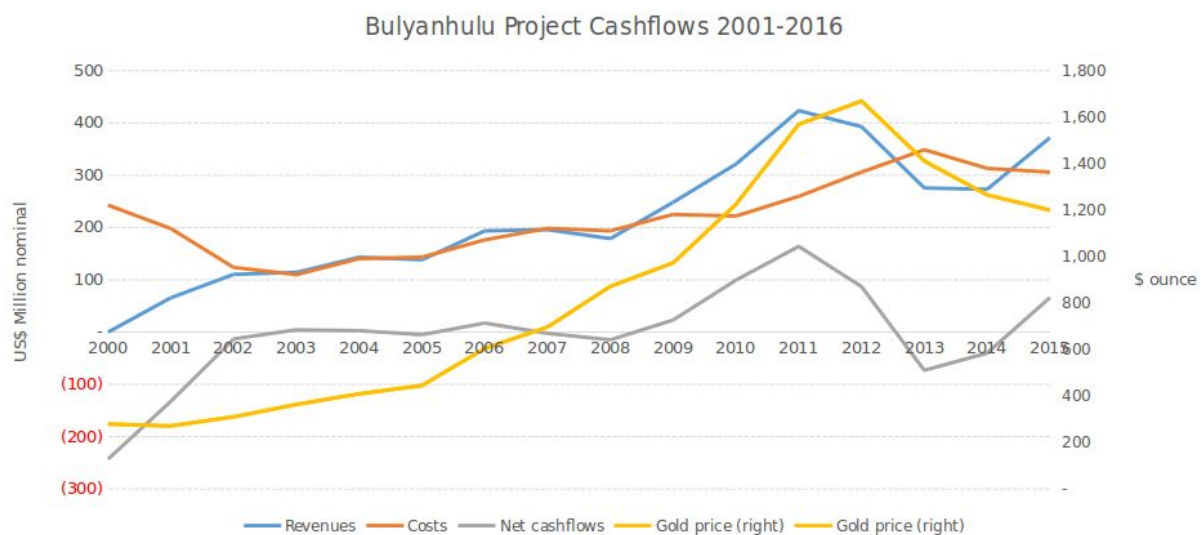
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<sup>1</sup> North Mara, Bulyanhulu, and Buzwagi. Tulawaka stopped producing in 2011

<sup>2</sup> [The 2015 annual report](#). See page 118. The Segments are North mara, Bulyanhulu, Buzwagi, Tulawaka (up to 2012) and “Other” being non-allocated corporate and exploration costs

add 15% Additional Capital Allowance (ACA) on capital costs not yet offset against positive taxable income.<sup>3</sup> This was designed to attract foreign investment to Tanzania. In effect it turns the Tanzanian income tax into a form of Resource Rent Tax, where income tax is only paid if a project generates enough profit to earn a 15% pre-tax rate of return on its capital investment.

Without the ACA, Tanzanian gold mines would pay tax as soon as their cumulative cashflows (profits minus capital expenditure) became positive. But with ACA, this is pushed back until the cumulative cashflows are enough to offset the accumulated ACA. Our Bulyanhulu analysis shows that even without ACA it would take until 2017 for Bulyanhulu to reach cumulative positive net cashflows - for this mine at least there have not so far been material net cashflows for Tanzania to tax.



Our calculations also suggest Bulyanhulu would have accumulated some \$500 million of ACA up till 2006 (when Acacia agreed to stop accruing it), pushing back the start of tax payments for that mine by three full years to 2020. We expect substantial ACA would also have been earned by the other two mines, North Mara and Buzwagi, deferring the point at which they would become taxable.<sup>4</sup> Each \$1 of ACA reduces tax paid in Tanzania by 30 cents.

Lastly, the fiscal regime includes a 10% withholding tax on dividends paid by Tanzanian companies to non-resident shareholders. Dividends are distributions of after tax profits. A Permanent Establishment (PE) operating in Tanzania other than through a company pays 10% on “repatriated profits” defined in section 72 of the Income Tax Act 2004; it basically the same as a dividend withholding tax.

**The financing structure – getting the cash to London**

Acacia Mining PLC owns its Tanzania gold mines indirectly, by owning 100% of the shares in the Tanzanian companies that own the mines<sup>5</sup> – possibly through a chain of subsidiaries. Acacia’s subsidiaries are listed in note 1 to the financial statements. Acacia could provide equity funds to

<sup>3</sup> In effect. The 15% is actually added to unredeemed qualifying capital expenditure”, meaning capital costs not yet offset against positive taxable income.

<sup>4</sup> In Tanzania tax is paid by each individual company. North Mara and Bulyanhulu are separate corporate taxpayers. We do not have that information for Tulawaka and Buzwagi.

<sup>5</sup> Bulyanhulu Gold Mine Ltd; North Mara Gold Mine Ltd; Pangea Minerals Ltd are listed in note 1 as “Operating Gold Mine”

its Tanzanian subsidiaries which would earn profits in Tanzania and then distribute those profits to Acacia - after any Tanzanian tax - as dividends, on which Acacia would pay 10% withholding tax.

However, in practice Acacia would likely have had the option to provide at least some of the funds to Tanzanian subsidiaries in the form of intercompany debt rather than equity. Repayments of such debt would not attract withholding tax. We understand there were minimal restrictions on use of debt (so-called “thin capitalisation” rules) in place in Tanzania when the MDAs were signed.

In addition, the Acacia accounts describe two instances of 3<sup>rd</sup> party project finance taken out for the Bulyanhulu project; \$200 million in 2002 and \$142 million in 2013. We presume that interest on these loans would be tax deductible and not attract withholding tax.

If interest was charged on any intercompany debt it would be tax deductible in Tanzania, further deferring the start of tax payments.

Acacia Mining (Barbados) Corp Ltd. is described in Acacia accounts (note 1) as “Group Finance Company”. Though we cannot tell from the financial statements, this entity could have received equity from Acacia and provide this to its Tanzanian subsidiaries as intergroup loans. So equity raised by Acacia could become debt to Tanzanian subsidiaries, potentially reducing Tanzanian income tax and minimizing withholding taxes. This type of structuring is common practice among multinational companies.

We see \$51 million net finance charges in Acacia’s segment note. However this is net transactions with third parties. Any loan transactions between group companies are “eliminated on consolidation” (offset) and are thus invisible in the accounts.<sup>6</sup>

So it is quite possible that Acacia could pay dividends to its shareholders out of the net cashflow generated by its Tanzanian mines, whilst those mines were still paying off accumulated ACA and therefore not taxable, and without the Tanzanian subsidiaries having yet declared dividends themselves due to funds having been advanced as debt. In any case, by definition the mines reach positive cumulative cashflows some time in advance of becoming taxable, because of the ACA.

### **International Tax considerations**

Barbados is a low tax jurisdiction which charges close to zero income tax on profits earned by “International Business Companies”, and imposes no withholding taxes on dividends paid to non-resident shareholders.<sup>7</sup> Thus debt repayments and profits in the form of interest paid by a Tanzanian group company would be virtually tax free after they left Tanzania and remitted back to the UK parent as dividends. The UK has a territorial tax system so that profits earned outside the UK are exempt from UK tax.

### **Does Acacia Mining PLC have a permanent establishment in Tanzania?**

For the TRA to prevail would mean the court agreeing to look through the group structure and deem that Acacia Mining PLC is directly “carrying on a business” in Tanzania and that the Tanzanian companies that own the mines are in effect only its agents. Acacia will likely argue that

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<sup>6</sup> Except any transactions with the parent company itself, Acacia Mining PLC. Accounts for this entity stand-alone are included in the financial statements. However transactions between any two subsidiaries would be invisible.

<sup>7</sup>

<http://www.ey.com/GL/en/Services/Tax/Worldwide-Corporate-Tax-Guide---XMLQS?preview&XmlUrl=/ec1images/taxguides/WCTG-2016/WCTG-BB.xml>

Acacia PLC is just a holding company and that day to day management decisions are made by the Tanzanian companies.

We do not venture an opinion on this, except to note that the norm in international tax architecture has been to allow separate legal entities to be treated as if they were independent even where these are part of the same group. It is this basic feature of the tax system that has facilitated multinational tax planning and shifting of profits to low - or zero - tax jurisdictions.

In any case, it seems clear that the special dividend of \$253 million was not remitted out of profit generated in Tanzania, and therefore should not attract Tanzanian tax, so the TRA has at most \$19.1 million in tax to gain (10% x \$191 million).

### **Open Oil's Bulyanhulu model and analysis**

Open Oil aims to empower stakeholders in countries dependent on natural resources by giving them the skills and tools to do their own analysis; to go beyond the current reporting scope of EITI - which tracks what revenues a government receives - into what a government *should have* received, and how those revenues arose and how they might evolve in the future under various production, commodity price and costs scenarios. We are developing open source models for several major projects around the world, and a methodology and tools that stakeholders can apply themselves.

We have developed a model of Acacia's Bulyanhulu gold mine, and use this to explain why that mine has not paid income tax despite producing over 4 million ounces of gold to date.

### **About Open Oil**

Open Oil is an analysis and open data publishing company founded in 2012 to provide data and analysis which improves governance of the world's extractive industries. It has published over 20 books on the industry, the world's first open map of oil concessions, and the largest collection of oil contracts. Clients include the United Nations, Petroleum Economist, the UK and German development agencies and a number of governments and research institutes and foundations. OpenOil is a social enterprise. Under its articles of association it may not undertake consultancy work for extractives companies.

Analysis of Acacia Segment reporting notes from Annual Reports								
US\$ Million	2009	2010	2011	2012	2013	2014	2015	2010-2015
EBITDA (Earnings before Interest, Tax Depreciation and Amortization)								
North Mara	89	153	129	100	168	156	135	928
Tulawaka	50	39	68					157
Bulyanhulu	59	181	257	185	68	69	59	877
Buzwagi	86	96	166	55	56	80	2	542
Other (discontinued operations)				10	(31)	1		
Total	283	469	619	349	261	307	195	2,483
Cumulative	283	753	1,372	1,721	1,982	2,288	2,483	
Less: Corporate costs								
Acacia Mining EBITDA	(34)	(50)	(74)	(13)	(21)	(53)	(20)	(265)
	249	419	545	336	240	253	175	2,219
Capital expenditure								
Finance charges	(223)	(224)	(345)	(351)	(354)	(254)	(177)	(1,929)
	(5.6)	(0.6)	(8.5)	(8.2)	(8.0)	(8.6)	(11.2)	(51)
Acacia Mining Cash generated								
Cumulative	21	194	192	(23)	(122)	(9)	(13)	239
	21	215	406	383	261	252	239	
Acacia Dividends paid								
Special dividend	-	7	28	70	55	14	17	191
Cumulative dividends	-	253	288	358	412	426	444	253
		260	288	358	412	426	444	444

**Table 1 Analysis of Acacia Segment notes**