BINDING PRIVATE RULING: BPR 146

DATE: 10 May 2013

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)

SECTION : SECTIONS 1, DEFINITION OF "MINING OPERATIONS" AND/OR "MINING", 11(*a*), 15(*a*), 23(*g*) 36 AND 37A(1)(*d*)(ii)

SUBJECT : MINING TAX – CONTRACT MINING AGREEMENT

1. Summary

This ruling deals with–

- whether a company appointed as a contractor in terms of a contract mining agreement is conducting mining operations and entitled to deductions under section 11(*a*), 15 and 36 of the Act during a transition period when the company is awaiting the transfer of mining rights to it; and
- the deductibility of contributions made by such company under section 37A(1)(*d*)(ii) in respect of environmental obligations.

2. Relevant tax laws

This is a binding private ruling issued in accordance with section 78(1) and published in accordance with section 87(2) of the Tax Administration Act No. 28 of 2011.

In this ruling references to sections are to sections of the Act applicable as at 10 July 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of –

- section 1, definition of "mining operations" and "mining";
- section 11(*a*);
- section 15(*a*);
- section 23(*g*);
- section 36; and
- section 37A(1)(*d*)(ii).

3. Parties to the proposed transactions

The Applicant:	A company incorporated in and a resident of South Africa that is the ultimate holding company of Co-Applicant A and Co-Applicant B (all forming part of a group of companies that carry on mining activities) (the A Group)
Co-Applicant A	A limited liability company that is incorporated in and a resident of South Africa and a wholly owned subsidiary of the Applicant
Co-Applicant B	A limited liability company that is incorporated in and a resident of South Africa and a wholly owned subsidiary of the Applicant

4. Description of the proposed transactions

In order to streamline the mining operations of the A Group, the Applicant intends to restructure and consolidate the current mining operations conducted by Co-Applicants A and B within Co-Applicant A.

In terms of the proposed restructure:

- Co-Applicant B will transfer certain mining assets (including mining rights) and liabilities to Co-Applicant A in terms of section 42, in exchange for equity shares to be issued by Co-Applicant A.
- Under the Mineral and Petroleum Resources Development Act No 28 of 2002 (the MPRD Act) the transfer of the mining rights will be subject to the consent of the Minister of Mineral Resources and the registration of the transfer of the mining rights will be done in the Mining and Petroleum Titles Registration Office. Accordingly, it is envisaged that there will be a delay in completing the proposed restructure until such time as the registration of the transfer of the mining rights is affected.
- In view of the fact that the provisions of the MPRD Act do not allow anyone who does not hold a mining right to mine for its own account, it is proposed that Co-Applicants A and B enter into a contract mining agreement for the period between the effective date of the transfer of the mining assets and the actual date of transfer of the mining rights (the interim period) in terms of which Co-Applicant A will mine on behalf of Co-Applicant B.
- Co-Applicant A will be appointed as a contractor in terms of section 101 of the MPRD Act and the applicable legislation to conduct

and to perform the mining operations in favour of and for the benefit of Co-Applicant B will apply.

- For the purposes of the contract mining agreement the term “mining operations” will mean all procedures, operations, functions and duties conducted, undertaken or performed in the normal course or in connection with or implicit in the recovery of ore from mining operations in accordance with the mine plan.
- Co-Applicant A will receive a contract mining fee for performing such mining operations. This fee will be a cost recovery fee for all the costs and expenses to be incurred by Co-Applicant A in terms of the contract mining agreement to perform the mining operations. The fee will include value-added tax (VAT) thereon at the applicable rate, as well as all amounts to be paid by Co-Applicant A on behalf of Co-Applicant B as royalties in terms of the MPRD Act.
- In terms of the contract mining agreement the ore to be mined will belong to Co-Applicant B. However, the contract mining agreement stipulates that Co-Applicant B will sell the ore to Co-Applicant A, and Co-Applicant A will purchase the ore to be mined from Co-Applicant B. Co-Applicant A will sell the same to the external market on the following basis:
    - The purchase price for the ore to be sold to Co-Applicant A will be an amount equal to the contract mining fee which includes the royalties referred to in the contract mining agreement, which will be payable monthly by Co-Applicant A to Co-Applicant B.
    - Co-Applicant A will dispose of all minerals and/or products derived from the exploitation of the minerals at competitive market prices which will mean, in all cases, non-discriminatory prices or non-export prices in accordance with the terms and conditions of the mining rights held by Co-Applicant B.
- Following the transfer of the mining rights from Co-Applicant B to Co-Applicant A, Co-Applicant B will distribute the equity shares to be received in Co-Applicant A to the Applicant in an unbundling transaction under section 46.

5. Conditions and assumptions

This ruling is made subject to the conditions and assumptions that:

- Co-Applicant A will not qualify for the partial relaxing of the ring fencing provisions of section 36(7F) as a result of the application of section 36(7G) in respect of the mining assets to be acquired from Co-Applicant B.

- Co-Applicant A must obtain approval from SARS Mining Tax division for the amount sought to be deducted under section 37A(1)(*d*)(ii) prior to the contribution being made to the designated rehabilitation trust or company for the years of assessment that Co-Applicant A will mine on a contract basis. It is noted that only approved amounts qualify for the deduction provided for in section 37A(1)(*d*)(ii).

6. Rulings

The ruling made in connection with the proposed transaction is as follows:

- Co-Applicant A will be recognised as holding the necessary mining rights to carry on mining activities on the mine areas of Co-Applicant B and will, therefore, be treated as carrying on “mining operations” and/or “mining” for the purposes of the Act.
- The contract mining fee payable to Co-Applicant A by Co-Applicant B in terms of the contract mining agreement will be regarded as income directly connected to such mining operations and as such will be regarded as income derived from mining.
- The revenue derived by Co-Applicant A from the sale of any ore during the interim period will be regarded as income directly connected to such mining operations and as such will be regarded as income derived from mining.
- Co-Applicant A will be entitled to capital expenditure deductions under section 15(*a*) read with section 36 against such mining income during the interim period.
- Expenditure incurred by Co-Applicant A in acquiring the ore from Co-Applicant B during the interim period, in terms of the contract mining agreement, will be regarded as a deductible expense under section 11(*a*) against the income derived by Co-Applicant A from the mining operations.
- Co-Applicant B will be regarded as carrying on trade during the interim period for the purpose of section 11(*a*), despite the absence of any profit, and will be entitled to claim the contract mining fee to be paid to Co-Applicant A in terms of the contract mining agreement as a section 11(*a*) deduction against the income earned from the sale of the ore to Co-Applicant A.
- Co-Applicant A will qualify in principle to claim as a deduction under section 37A(1)(*d*)(ii) contributions to be made in respect of environmental obligations, provided that the required approval is obtained from SARS. Notwithstanding the foregoing, a positive ruling is given to the effect that the payment of the contributions will not be

regarded as part of any transaction, operation or scheme designed solely or mainly for purposes of shifting the deduction contemplated in this subsection from Co-Applicant B to Co-Applicant A.

7. Period for which this ruling is valid

This binding private ruling is valid for a period of 2 years from 10 July 2012.

Issued by:

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