

GLENCORE

INTERNATIONAL DEVELOPMENT SELECT COMMITTEE INQUIRY INTO THE LINK BETWEEN TAXATION AND DEVELOPMENT

RESPONSE FROM GLENCORE INTERNATIONAL PLC

1. Introduction

(1.1) Glencore International plc, headquartered in Baar, Switzerland, is one of the world's leading integrated producers and marketers of commodities. Glencore has worldwide activities in the production, sourcing, processing, refining, transporting, storage, financing and supply of metals and minerals, energy products and agricultural products.

(1.2) Glencore's industrial operations directly or indirectly employ over 54,800 people in 30 countries. Over 2,700 people work in Glencore's marketing operations in 50 offices in 40 countries. Glencore's oil department employs around 400 people in London.

(1.3) Glencore's customers around the world are active in a wide range of industries, such as automotive, oil, power generation, steel production and food processing. They rely upon Glencore's established global network for the supply of metals and minerals, energy products and agricultural products. These commodities either originate from Glencore's own production assets or are sourced from third parties. Glencore also provides financing, logistics and other supply chain services to producers and consumers of commodities.

(1.4) Glencore owns and operates mines and other industrial facilities throughout the world, including in developing countries across Africa, Asia and Latin America. As a result of these investments Glencore has gained significant knowledge and experience in building sustainable businesses in collaboration with local communities and national governments.

(1.5) Glencore is listed on the London Stock Exchange and is a constituent of the FTSE 100, with a secondary listing on the Stock Exchange of Hong Kong.

2. Conducting Business in Developing Countries

(2.1) As a leading natural resources company, and investor in the developing world, our presence and business activity serves to promote development. Our investments and the jobs, entrepreneurial opportunities and Government revenues they generate contribute to local, regional and national economic well-being and growth.

(2.2) Working in the developing world entails particular challenges and responsibilities. Glencore puts sustainability at the top of its agenda and it is an integral part of everything we do.

(2.3) For this reason, we have put a corporate sustainability framework in place to balance social, environmental, ethical and commercial interests at every level of our group. This framework is called Glencore Corporate Practice, or GCP. We have designed and implemented the GCP to meet internationally recognised, sector-specific, good practice standards.

(2.4) The Committee is undertaking an inquiry into tax in developing countries and as part of that inquiry is using Zambia as a case study. One area of focus is whether large investors in countries such as Zambia are contributing sufficiently to Government revenues and to the development of society more broadly.

(2.5) For Glencore, our main priorities in resource-holding countries are to invest for the long run, conduct our operations responsibly, provide good quality jobs and indirect economic opportunities, and generate taxes, royalties and other dues to Governments. In addition we make substantial voluntary contributions to improve the lives of the people in the communities where we operate. Our commitment to continual improvement of environmental protection and safety is also an integral part of our operations.

3. Glencore's Operations in Zambia

(3.1) Glencore owns 73.1% of Mopani Copper Mines plc. The other shareholders are First Quantum (16.9%) and the Zambian government (10%).

(3.2) Mopani is an integrated copper and cobalt producer located in the Copperbelt Province of Zambia. Mopani's operations consist of four underground mines, a concentrator and a cobalt plant at Nkana in the town of Kitwe and an underground mine, concentrator, smelter and refinery in the town of Mufulira.

(3.3) Mining began at Nkana in 1931. The town of Kitwe started as a railway station to support the growing copper operations on the Copperbelt. Mining began at Mufulira in 1933 and the town grew around the mine.

(3.4) Glencore acquired its shareholding in Mopani through a competitive tender as part of a general privatisation, supported by the World Bank, of copper mining assets in 2000. Following years of under-investment prior to privatisation, the business was in a parlous financial and physical condition and its 10,000 jobs were at risk. Safety performance was poor. In addition the Mufulira smelter had been emitting sulphur dioxide unconstrained since it was built in 1937.

(3.5) Since privatisation the shareholders have and continue to make a very substantial contribution to local, regional and national economic well-being and growth.

(3.6) The corporate shareholders have committed \$2 billion in investment since privatisation to redevelop and expand Mopani's operations. The Government is carried, which means it does not contribute to this investment whilst benefiting from the results. This investment has secured the long-term future of the business, increased employment and production, and improved safety. The shareholders will continue to invest at high levels going forward as the cost and challenges of mining at deep underground levels increases.

(3.7) Some 16,300 people work at Mopani today (8,300 employees and 8,000 contractors). We estimate that each employee has an average of eight dependents. Over 6,000 new jobs have been created since privatisation. Mining is the highest paying sector in Zambia. The salary of the most junior employees is \$508 per month (K2,620,000) compared to the national minimum wage of \$81 per month (K419,000). Mopani believes it is the second highest payer of its most junior employees amongst the mining companies in Zambia.

(3.8) Mopani spent \$775 million on contractor and supplier companies in 2011. Of this, 82% of the total was spent in Zambia, 69% of the total in the Copperbelt and 61% of the total in Mufulira and Kitwe.

(3.9) Production has increased from 135 thousand tonnes of copper and two thousand tonnes of cobalt in 2003 to 204 thousand tonnes of copper and nine thousand tonnes of cobalt in 2011.

(3.10) Mopani has paid \$425.1 million in taxes, royalties and other dues to Government since privatisation.

(3.11) Taxes, royalties and other dues to Government as declared above include Pay As You Earn (PAYE), Mineral Royalties and Import Customs & Excise Duty. Mopani also pays Import VAT & Reverse VAT as well as property rates on a monthly basis.

(3.12) In 2011, due to the increases in the number of employees, import duties on capital goods and mineral royalties, Mopani paid \$104 million (K508 billion).

(3.13) With the continued capital investment and the doubling of the royalty tax in the current year it is expected that this amount will be higher again in 2012 and into the future.

(3.14) From April 2012, the royalty tax that companies extracting base metals, including copper, pay to the government doubled from 3% to 6%. The royalty is calculated using the London Metal Exchange copper and cobalt prices and is based on revenue rather than profits. There were a number of meetings held between the Government and the Zambian Chamber of Mines regarding the royalty increase when it was proposed. The industry expressed concerns it may discourage investment and reduce the overall Government take in the long-term, however the Government decided to implement the new rate.

(3.15) The effective tax rate for Mopani in 2012 will be approximately 52%. This estimate takes account of the doubling of the royalty tax during the year and is based on budgeted sales.

(3.16) The tax system in Zambia allows for a 100% tax deduction against corporate Income Tax in the year in which capital investment on mining and processing is spent. This results in no direct Income Tax being paid in the years in which large investments are made and creates tax

losses/credits that are carried forward to be used against taxable income in future years.

(3.17) Due to the high level of capital investment undertaken by Mopani at privatisation, and since, to continue the operations and address a number of legacy issues, Mopani currently has Income Tax losses/credits available for offset. The level of capital investment in the future will also affect the amount of Income Tax payable by Mopani in the coming years.

(3.18) These capital allowances are similar to those included in the tax legislation of other African countries such as South Africa, the Democratic Republic of Congo and Namibia and other countries outside Africa including Australia, Japan and the United States. The tax allowances encourage capital investment thereby supporting economic development.

(3.19) Due to the continuous investment required in keeping Mopani running as well as upgrading the mines and processing facilities, to date the corporate shareholders have not received any dividends as they continue to invest in Mopani's long-term future. This investment includes addressing legacy issues such as the emission of sulphur dioxide at Mufulira.

(3.20) Currently about half of all sulphur dioxide emissions are captured and this has been enabled by phased investments in a modern smelting technology that has provision for gas capture. The final phase of a \$145 million project to capture 97% of emissions, a world-class performance, has been fast-tracked and will be complete by the end of 2013, some 18 months ahead of the deadline set by the Government at privatisation.

(3.21) Exposure to elevated levels of sulphur dioxide can cause impairment of respiratory function and aggravation of existing cardiovascular disease and respiratory disease (especially bronchitis). Workers at the Mufulira smelter are provided respirators as part of their Personal Protective Equipment for this reason.

(3.22) The Mufulira smelter is one of just three copper smelters in Zambia. It plays an important role in ensuring the economic viability of other operators' mines by processing their concentrate into metal in return for a small tolling fee. About half of the smelter's metal output is generated in this way.

4. Mopani's voluntary contributions in community development

(4.1) In addition to creating jobs and generating revenue for Government, Mopani makes further contributions voluntarily to improve living standards in the communities in which it operates.

(4.2) These voluntary contributions are made based on local needs and in line with the priorities of the Government for the development of the country, which include health, education and infrastructure development.

(4.3) Mopani's voluntary contributions total over \$140 million since privatisation and have averaged \$15 million per annum on on-going projects in recent years. Spending in 2011 was substantially higher due to additional spending on sanitation and road projects.

(4.4) Mopani operates two major hospitals (treating 120,000 patients per annum) and seven township clinics (130,000 patients treated per annum). Both hospitals have attained the highest ISO:9001 standard. Spending on health has increased by 300% from 2002 to 2011.

(4.5) Over 14,000 people are on HIV/AIDS antiretrovirals and care funded by Mopani, 85% of them non-Mopani employees or their dependents.

(4.6) A malaria reduction programme implemented since October 2000 has reduced incidence from the national average of 216 per 1,000 to fewer than 20 per 1,000 in Mopani's catchment area. An average of \$650,000 is spent annually on this programme which included indoor residual spraying of 30,000 households in 2011.

(4.7) Mopani operates two primary schools and two secondary schools. Children are enrolled on merit and about half are from families in which no one works at Mopani. Some 2,000 children are currently enrolled with a further 700 on the waiting list. These schools are amongst the very best in the country and have achieved a 100% exam pass rate since Mopani has operated them.

(4.8) During 2011 Mopani spent \$4.5 million building 1,500 individual sanitation units in a residential area in Kitwe where households shared communal facilities which caused disease. A second phase of this project has begun. Mopani also began a \$10.5 million project to repair

two key roads in the Copperbelt which are arteries of economic growth. This project will be completed in 2012.

(4.9) Mopani has also set up a cooperative farm for retired employees who wish to continue to be active economically. This cooperative farm now operates independently and Mopani is in discussions with the local authority to acquire land to build a second similar project to replicate its success.

(4.10) Around 50% of Mufulira town's total water requirements are met by Mopani, which supplies the water free of charge to the local utility. The proportion supplied by Mopani will significantly increase on commissioning of new water pipeline from the nearby Kafue river. This has been extended to Kankoyo township, where residents all have access to potable water, courtesy of a newly installed pipeline.

5. Draft tax audit

(5.1) Mopani is audited every year by Deloitte and its accounts have always been given a clean bill of health. As a public company, Mopani's accounts are lodged with Securities and Exchange Commission as well as the Companies Registry in Lusaka and are publicly available.

(5.2) Mopani is convinced that the taxes, royalties and other dues to the Government have always been calculated and paid in the proper manner in line with the applicable legislation.

(5.3) In February 2011 a draft provisional report prepared by advisers to the Zambia Revenue Authority was unofficially circulated in Zambia. The report was described as "confidential, preliminary and an incomplete draft" by the Zambia Revenue Authority.

(5.4) The draft provisional report contained fundamental factual errors and both Mopani and Glencore have publicly refuted its 'conclusions' on numerous occasions.

(5.5) The most fundamental flaw incorporated by the authors of the report was the inclusion of toll treated material in the volumes used to calculate Mopani's average sales price. Ownership of the toll material does not transfer to Mopani which only receives a treatment and refining charge and returns the final product of copper cathode to the contracted third party.

(5.6) In addition, the authors alleged that Mopani manipulated copper prices to engage in transfer pricing in favour of Glencore, when in reality all copper is sold on arms-length terms basis prevailing London Metal Exchange prices. The London Metal Exchange is a transparent forum for trade that provides worldwide reference pricing for metals. Mopani's copper brand, MCM, is one of the most historic copper brands approved for delivery against the London Metal Exchange copper contract. Mopani also undertakes production hedging on the London Metal Exchange, a standard practise within the mining industry, and the results of these hedging activities were not taken into account by the authors during their desktop review.

(5.7) The authors also alleged that gold and silver hedges were improperly recorded and used to impact taxable income. In fact any hedges recorded were entered into to offset physical price exposure and the net financial impact on Mopani's taxable income was zero. They further alleged that operating costs rose for unexplained reasons without making any attempt to clarify these facts, for instance they used general inflation rates for their calculations despite mining cost inflation exceeding the general inflation rate and despite Mopani's labour, and fuel costs having risen at substantially higher levels than inflation.

(5.8) In response to a request from Glencore to review the draft provisional report, Deloitte described "fundamental flaws in terms of methodology and approach applied" and reiterated that "for each of the years subject to audit, Mopani's statutory financial statements were audited by Deloitte Zambia and unqualified audit opinions were issued". Deloitte's full letter is posted on Glencore's website.

(5.9) Mopani has engaged in a detailed and constructive dialogue with the Zambia Revenue Authority on these matters. The Zambia Revenue Authority has completed its audits of all the years in question. Thus far they have found all the allegations to be unsubstantiated. We continue our dialogue with the Zambia Revenue Authority and expect the audits to be finalised and closed out shortly.

(5.10) In 2005 the European Investment Bank signed a Finance Contract with Mopani for an amount of \$50 million to partially fund the rehabilitation of the Mufulira smelter. The European Investment Bank has informed the European Anti-Fraud Office (OLAF) and launched its own investigation about the tax allegations made in Zambia against Mopani. Discussions continue with the European Investment Bank on this matter.

Mopani's position with regards to the European Investment Bank process is entirely consistent with the position it has taken with the Zambia Revenue Authority.

6. The relationship between taxation and development

(6.1) Glencore fundamentally believes that inward investment has a positive impact in developing countries, creating employment and entrepreneurial opportunities which are the only route out of poverty. Feeding the mineral requirements of China, India and other fast-growing economies has the potential to create transformative economic growth in resource-holding countries in Africa and beyond.

(6.2) In addition, in the natural resources industry, investment in developing countries has a positive impact globally. The world needs minerals to sustain and improve living standards worldwide. Demand is growing and supply is constrained. Some of the best remaining sources of supply lie in developing countries and failure to develop them will result in higher prices for everyone.

(6.3) It is Glencore's view that progress in building durable economic growth in less developed countries is more likely in open economies with taxation systems that are transparent, welcoming to foreign investors and accountable.

(6.4) We agree that the link between taxation and development is fundamental and that the failure to collect tax in developing countries is a major issue of concern. Businesses such as ours, which are based on significant investment in fixed assets that will deliver returns only over decades, have no interest in taxation systems that are unfit for purpose, arbitrary or misdirected.

(6.5) However, as a major investor in the developing world Glencore cannot and should not be expected to adopt aggressive political postures over the proper conduct of Government and its taxation policy.

(6.6) Glencore does not make political contributions or seek to become involved in party politics in any way.

(6.7) The issues of wealth distribution, public service provision and poverty reduction matter to Glencore, but go far beyond the subject of this Committee's inquiry and indeed the capacity or proper remit of

Glencore or any other corporate in any particular country. These matters are of concern to us all, but their resolution in individual countries, whether in Zambia or elsewhere, must be resolved by the legitimate governments of those countries and the properly constituted international agencies within whose remit these matters lie.