Canadian Mining Investment in Mexico vis á vis Sub-national Governments

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The change

- NAFTA place the Mexican territory inside a dynamic that break with the traditional regional policy.
- Local governments were forced to offer their region in the North American market and compete with outside actors, mainly, the U.S states and Canadian provinces.
- For the first time, the Sub-national states must react in an individual way to the dictates of the supply and demand under the rules of NAFTA and build up a particular strategy to attract investment to their region.
- The Sub-national entities had to share with new players their region, its natural resources and human capital.
Governance at stake

- The implementation of NAFTA in regards of investment, generate some disagreements in the three levels of government: the Federation, the States and the Municipal level.
- The competition for the North American investment, but also in some cases, the imposition of some kind of investment from the Federation to the local instances, has been a break between the three governments levels. (Metalclad)
- In some cases, states governments and/or local communities, have given free rein to a sort of decomposition of the governance, related with the growing of FDI in natural resources.
How did it come to this?

- NAFTA takes away the discretionional power that traditionally enjoys the federal government in regards to the location of foreign investment.
- Before NAFTA, the assignment of foreign investment in Mexico, to a particular regional entity, was part of the federal privileges upon the local governments (the allegiance quota).
- That privilege collapsed as did the number of local governments did not belong to the PRI, and the laws restricting foreign investment were liberalized.
Before NAFTA

- The strategy of attract foreign investment was mostly a federal task.
- Rarely, state governments taking the initiative to compete with other regions for foreign investment (the opposite situation of Canadian provinces and U.S. states)
- The norm that prevailed was, that the Mexican Federation, tax relieved 30%, and then distributed to the states under its own criteria through the budget line 33.
- Hence the local authorities didn't t have a genuine interest to compete for foreign investment.
The roots of the conflict

- Frequently, the investment priorities don't fit with local interest (government or communities, or both). That brings to a conflict between federal and local priorities.
- NAFTA establish, in the case of disputes, that the company has the right to sue the federal government, in spite that the conflict came from the local level.
- When the NAFTA disputes settlements mechanism start to be implemented, the Federal authorities complained about the fact that the payment of a sue were always a federal responsibility.
The core of the problem

- Initially, the Federal government tried to collect the indemnization from the local governments through the transfers (San Luis Potosi State & Metalclad).
- But this attempt was strongly rejected for the States and the Supreme Court of the Nation.
- Therefore, the federal government is paying all claims under NAFTA rules and BITS.
- No matter if the conflict was triggered by a state government, Municipal authorities, or directly by the community.
The first phase

- From 1961 to 1991, the Mexican mining law stipulated that minerals assets must be at least 50% owned by Mexican companies.

- There was little incentives to explore because of low landholding fees and rich long lived deposits that just kept on churning out metals.

- From 1988 to 1996 the Mexican government carried out a process of privatization of state enterprises in favor first of the Mexican capital.

- In this period were awarded 6.6 million hectares with mining reserves.
The second stage

- In 1996, the new foreign investment law allows 100% of foreign ownership in the mining sector.

- The mining law was amended in 2005 (promotes concessions and grants rights to individuals up to 50 years).

- From that period, Mexican corporations compete and sharing with foreign companies for a mineralized territory.
FDI Flows to Mexico and to the Mining Sector

**Source:** General Direction of Foreign Investment, Ministry of Economy, 2013
Evolution of the FDI to Mexican Mining Sector
1994-2012

Source: General Direction of Foreign Investment, Ministry of Economy, 2013
Canadian FDI flows to the Mining Sector
1999-2012

Source: General Direction of Foreign Investment, Ministry of Economy, 2013
Distribution by Country Origin of Foreign Mining Companies, 2012

<table>
<thead>
<tr>
<th>Country</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total</td>
<td>285</td>
</tr>
<tr>
<td>Canada</td>
<td>204</td>
</tr>
<tr>
<td>United States</td>
<td>46</td>
</tr>
<tr>
<td>China</td>
<td>8</td>
</tr>
<tr>
<td>Australia</td>
<td>5</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>4</td>
</tr>
<tr>
<td>Japan</td>
<td>4</td>
</tr>
<tr>
<td>Korea</td>
<td>4</td>
</tr>
<tr>
<td>India</td>
<td>2</td>
</tr>
<tr>
<td>Peru</td>
<td>1</td>
</tr>
<tr>
<td>Belgium</td>
<td>1</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>1</td>
</tr>
<tr>
<td>Chile</td>
<td>1</td>
</tr>
<tr>
<td>Italy</td>
<td>1</td>
</tr>
<tr>
<td>Netherlands</td>
<td>1</td>
</tr>
<tr>
<td>Spain</td>
<td>1</td>
</tr>
<tr>
<td>Brazil</td>
<td>1</td>
</tr>
</tbody>
</table>

Source: Ministry of Economy, Statistical Yearbook of the Mexican Mining 2012
The Paradox

- In 2010, the Mexican government gave in concession more than 4 millions of hectares to companies, but the fiscal revenues from the mining operations was only 20 millions dollars.
- In the same period, the corporate revenues were more than 15 000 millions dollars.
- This is because in Mexico the fiscal revenues only taxed according to the number of conceded hectares to companies, and not to the amount of minerals that extracted.
# Main Taxes on Mining Sector

<table>
<thead>
<tr>
<th></th>
<th>Income tax</th>
<th>Perquisite /Extraction tax</th>
<th>Withholding Tax</th>
<th>VAT and rights on imported equipment</th>
<th>Rights to the export /taxes</th>
<th>Participation of profits to the workers</th>
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<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Dividends</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Argentina</td>
<td>35%</td>
<td>0% to 3% of value of the mineral to mouth of mine</td>
<td>0%</td>
<td>10%</td>
<td>Standard rates 21% other rates the 10.5%</td>
<td>5% to 10% according to the metal</td>
</tr>
<tr>
<td>Australia</td>
<td>30%</td>
<td>Variable rate according to mineral and value. Between 0% to 10%</td>
<td>30% likely to be reduced</td>
<td>30% or less in some cases</td>
<td>10% VAT. Rate of Customs Duty of 5%</td>
<td>ND</td>
</tr>
<tr>
<td>Brazil</td>
<td>34%</td>
<td>0.2 % to 3% of the sales value</td>
<td>0%</td>
<td>15%</td>
<td>Standard rate 17% to 18%</td>
<td>ND</td>
</tr>
<tr>
<td>Canada</td>
<td>8% federal tax, 10 or 16% state tax</td>
<td>2.5% to 17.5%, according to the territory</td>
<td>25% likely to be reduced</td>
<td>Up to 25% likely to be reduced</td>
<td>5%-13%</td>
<td>N.D.</td>
</tr>
<tr>
<td>Chile</td>
<td>17%</td>
<td>0% to 5% operating margin</td>
<td>35%</td>
<td>35%</td>
<td>19%</td>
<td>N.D.</td>
</tr>
<tr>
<td>China</td>
<td>25%</td>
<td>There are no royalties</td>
<td>10% likely to be reduced</td>
<td>10% likely to be reduced</td>
<td>17% and exoneration under certain circumstances</td>
<td>Copper 30% Zinc 30%. Neither gold nor the iron exported</td>
</tr>
</tbody>
</table>

**Source:** Minería en México Referencias Generales, Centro de Estudios Sociales y de Opinión Pública, 2011
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<tr>
<td><strong>Colombia</strong></td>
<td>33%</td>
<td>1% -12% of the value of mouth of mine</td>
<td>0% on earnings subject to corporate tax</td>
<td>0% Interest of loans of the abroad</td>
<td>0%-16% for certain equipment</td>
<td>N.D.</td>
</tr>
<tr>
<td><strong>United States</strong></td>
<td>35%</td>
<td>12.5% and 18.5% if you are extracted to federal lands</td>
<td>30% Subject to treaties</td>
<td>30% Subject to treaties</td>
<td>N.D.</td>
<td>ND</td>
</tr>
<tr>
<td><strong>Mexico</strong></td>
<td>30%</td>
<td>None</td>
<td>0% if is distributed of the income taxed</td>
<td>30%</td>
<td>0% -16% applicable under certain conditions</td>
<td>ND</td>
</tr>
<tr>
<td><strong>Peru</strong></td>
<td>30%</td>
<td>1-35 on gross sales</td>
<td>4.10%</td>
<td>30% or less in certain cases</td>
<td>19%</td>
<td>N.D.</td>
</tr>
<tr>
<td><strong>Russia</strong></td>
<td>15.5% to 20%</td>
<td>The rates fluctuate between 3.8% to the 8.0%</td>
<td>Russian companies 0% to 9%, foreigners 15%</td>
<td>20% likely to be reduced</td>
<td>18%</td>
<td>N.D.</td>
</tr>
<tr>
<td><strong>South Africa</strong></td>
<td>Variable</td>
<td>Refined minerals 5%, 7% unrefined</td>
<td>10% of taxes on dividends</td>
<td>N.D.</td>
<td>14%</td>
<td>N.D.</td>
</tr>
</tbody>
</table>

Source: Minería en México Referencias Generales, Centro de Estudios Sociales y de Opinión Pública, 2011
Canadian Projects of Mining Companies at Exploration Phase (853) 2012

Source: Prepared by the Author based on data from Mining Chamber of Mexico, Annual Report 2012
Canadian Projects of Mining Companies at Exploration Phase by type of mineral 2012

Mineral association, Canadians Companies

- **Gold**: 39%
- **Silver**: 34%
- **Cooper**: 9%
- **Zinc**: 7%
- **Lead**: 7%
- **Molibdeno**: 1%
- **Otros**: 3%

**Source**: Prepared by the Author based on data from Mining Chamber of Mexico, Annual Report 2012
Canadian Projects of Mining Companies at Mining Phase by type of mineral 2012

**Source:** Prepared by the Author based on data from Mining Chamber of Mexico, Annual Report 2012
Canadian Mining Companies at Development Phase by type of mineral 2012

Mineral Association, Canadian Companies

- Gold: 28%
- Silver: 25%
- Copper: 19%
- Zinc: 12%
- Lead: 7%
- Iron: 5%
- Mercury: 2%
- Cobalt: 2%

Source: Prepared by the Author based on data from Mining Chamber of Mexico, Annual Report 2012
Reversing the current situation

- Two separates bills to reform Mexico’s mining laws, one from the government and the other from activists, agree on the urgent need for major changes in the rules governing the industry.
- Royalties for 5% on revenues, before taxes will go to the States and Municipalities where foreign mines are operating.
- Huge opposition from the companies and also from the Mexican Chamber of Mines.
- The owners argue that they already pay a security tax.