Speech by Julian Payne, President, Canadian Chamber of Commerce of the Philippines
On "A Foreign Investor's View on Mining in the Philippines"
At the Development Academy of the Philippines, Pasig City, on July 10, 2014

Mr. Chairman,

Ladies and Gentlemen:

It is a pleasure to speak today to this panel discussion on mining in the Philippines. DAP is well placed to host such a discussion and I welcome being invited to speak.

I come from Canada whose development as a major economy has been based in significant measure on mining. I have been involved professionally in bilateral and multilateral development cooperation for 30 years before moving to the private sector and am aware of the benefits and risks of mining for developing economies.

To be transparent, I have no personal investments in mining either directly or through mutual funds. I have never worked for a mining company. However I do benefit directly from mining: I use a computer that includes various precious metals; I live in a condo building reinforced with iron rods; and I eat food cultivated with machines using various metals. I am dependent on mining for my way of life and cannot conceive of enjoying the benefits of modern civilization without mining. The basic question is not <u>whether</u> there should be mining. It is <u>where</u> there should be mining and <u>how</u> to maximize the benefits and minimize risks of mining.

In this context, foreign investors considering the potential for mining in the Philippines are perplexed by the attitudes of the Philippines' authorities.

On the one hand:

- The country has enviably-huge mineral reserves just waiting to be developed.
- The 1995 Mining Act is highly regarded internationally as one of the more complete and progressive examples of such legislation in the world.
- There are statements by national authorities that they want more foreign investment, particularly that supporting inclusive growth and employment, with mining providing a major opportunity for such inclusive growth and employment.
- There have been statements by national authorities that they support environmentally and socially responsible mining.

On the other hand foreign investors see few concrete measures implemented to support mining. Instead they see many actions by national and local authorities that discourage mining. They see what best may be described as "forward talk with backward walk".

I will summarize some actions by national and local authorities that foreign investors say discourages their interest in mining.

Actions by national and local authorities that discourage large-scale mining

- Despite a low level of total foreign direct investment (FDI) flows to the Philippines compared with that to its ASEAN neighbors, foreign investors see little support by the authorities to ease such restrictions to facilitate FDI, including for mining which is capital investment intensive and would benefit from eased restrictions.

- Despite the vast rural areas with little obvious value for profitable agriculture and/or major tourism, foreign investors see no opposition by national authorities to the multiplying declarations by local governments of outright bans or moratoria on mining in many areas. Indeed, the national government has just published a series of its own regional maps establishing an enormous number of "no go" zones. A consolidation of information in these maps reveals that nearly 85% (and I mean 85%, not 8.5%) of the total land area of the Philippines is within such zones! (I will talk more on this hugely negative development later).

- Despite a recent objective assessment by the IMF that the total share of mining revenues received by the Philippine public sector is much higher than that received in most other mining economies such as Chile, Peru and Papua New Guinea, foreign investors see the authorities considering an *even higher* share of mining revenues. This increase will render the Philippine mining industry totally uncompetitive with the other mining economies. It will in all likelihood kill the mining industry in the Philippines … along with all the opportunities for inclusive growth and employment in remote and poor areas where most mining is located.

- Despite the fact that large-scale mining is financially risky in terms of both non-productive investment in exploration and, even when exploration successful, in potential profitability due to volatile commodity prices, foreign investors see the authorities wanting to tax profits excessively when they are due to high commodity prices while leaving all the downside risks of losses with low commodity prices to be borne by the mining companies.

- Foreign investors look at the latest Development Plan published by the National Economic Development Authority (NEDA) and the latest investment priorities set out by the DTI/Board of Investments (BOI) and see hardly any positive reference to supporting let alone promoting the mining industry.

- Finally foreign investors see actions that limit foreign investment in legal large-scale mining while mining policy is reviewed (such as a freeze on new permits for large-scale mining) but no comparable actions being directed to freeze new permits for rapidly expanding small-scale mining nor concerted action to curb the rampant scourge of illegal mining.

The obvious conclusion that foreign investors interested in large-scale mining in the Philippines are reaching is that, despite rhetoric to the contrary, the national as well as most local authorities do not want or welcome foreign investment in large-scale mining in the Philippines.

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I will now address four main substantive arguments against and issues concerning mining that I hear that discourage foreign investment in large-scale mining in the Philippines … and how I understand foreign investors view these arguments and issues.

1. The argument that large-scale mining is environmentally damaging

The reality is that many economic development activities are potentially environmentally damaging. Building dams for hydro-electric generation, undertaking large-scale land-reclamation projects, clearing of forest-lands for agriculture, planning urban developments without proper wastewater treatment systems, over-development of tourist sites – and of course wide-spread and illegal small-scale mining – are all environmentally risky and can be environmentally damaging. But the issue is never whether these development activities should be banned per se but how we *minimize* the environmental impacts to acceptable levels and mitigate what actual impact there is. It is the same for mining, large-scale as well as small-scale.

In this respect problems faced in the past do not have to be assumed as certainties in the future. In the recent decades of growing environmental consciousness, lessons have been learned about how environmental risks can be mitigated, including in large-scale mining. This has been achieved with more sophisticated environmental impact assessments and risk mitigation requirements as well as more rigorous regulatory and monitoring environment. Further, many civil society groups now play an important and valued role in alerting authorities to risks. The alleviation of these risks in countries with successful environmentally-responsible mining such as Australia and Canada has been achieved by effective environmental and social planning in relation to mining activity as well as strict adherence to and enforcement of regulatory requirements, *not* by banning mining activities altogether.

It is also claimed that when mines are depleted, the large-scale mining corporations leave and the country is left with ruined environments. This argument usually refers to abandoned open-pit mines – and in the past, this was often true. But once again, contemporary management by an effective regulatory agency with private sector involvement can make it a non-issue today. While it may be the case that open-pit mines cannot be restored to the original pre-mine topographical state of nature, it is incorrect to assume that such depleted open-pit mines cannot used for productive and environmentally attractive purposes.

There are many examples of this being done successfully. Two in my own country Canada are: the famed 100 year abandoned quarry which is now the Butchart Gardens in Victoria in British Columbia (a world-class tourist site that attracts millions of visitors annually); and the Lac Lemy area in the Canada's National Capital region alongside which an expanded lake with casino has been built to also attract tourists. There are other examples around the world of tourist developments placed in abandoned mines. Other open-pit mines have been turned into water reservoirs. Some have even suggested that depleted open-pits could be used as solid-waste landfill sites (the solid waste must be put somewhere!) and when full, topped-off with earth and greenery. The challenge here is in the use of imagination, not in the banning of open-pit mining.

2. <u>The argument that large scale mining companies pay the State too little</u>

The authorities have argued that under present arrangements, the State does not get a "fair share" of the revenue of large-scale mining operations for the value of the State's natural resources being mined. This is an important issue that has several aspects.

The first issue is what is included within the "fair share". The fact is that the Department of Finance/BIR is not the only recipient of a total "fair share for governments". From a foreign investor's perspective its total share is what it gives to the public sector. In the Philippines that includes taxes to the national government, local taxes, and royalties to Indigenous People. However, as mining is usually in remote and often mountainous interior areas, it also includes enormous investments by the large-scale mining investor in public sector infrastructure in roads, health and education where government would be required to spend, and this is done by foreign investor so government doesn't have to do it. And finally it includes the huge amounts of a company's funds poured into local economies through operations and procurement, to develop businesses and generate income that results in further taxation to the various levels of government, not just the cash taxation revenue received directly from mining operations by the national government.

A second issue related to fair share is the split between what goes to the national government and what goes to provincial and municipal governments. In the Philippines the national authorities receives most, if not all, the revenues in the first instance and the LGUs face long delays in receiving their "fair share". As LGUs often face additional local infrastructure and social costs associated with the development of mining in their areas, this delay fuels anti-mining sentiment by LGUs which foreign investors then have to face. I understand that one element of the Minerals Industry Coordinating Council's recent proposals to the President include the creation of Mining Economic Zones, to be managed like the Philippine Economic Zone Authority (PEZA) – so that tax revenues can be managed directly and the LGU share distributed immediately. This is a good initiative.

A third issue about "fair share" actually means something else: it means, "The Department of Finance/BIR does not get enough tax for the national budget from large-scale mining". This is a different issue. Most governments look for and need additional sources of revenue and that possible from large-scale mining is tempting. However an important consideration is that foreign investment in large-scale mining is fungible between countries with companies engaged in large scale mining usually international with global perspective and alternative opportunities. In this respect the Philippines competes for foreign investment in large-scale mining with mining economies such as Chile, Indonesia, Mongolia, and PNG to name a few. And foreign investment in large-scale mining will go where the overall return of the investment is highest which includes, amongst other things, consideration of tax rates.

If the government tax rate on mining revenues is increased the interest of foreign investors will fall and the government may receive less total tax revenue (even though the tax rate may be higher). Conversely, if the government decreases its tax rate, the interest of foreign investors may increase and the government may actually get much more in total tax revenue (even when the tax rate is lower). Obviously if the government increases its tax rate too high there will be no investment in mining, no mining and no tax revenue from mining. This would be a classic case of authorities ignoring market economics and of killing the goose that lays the golden egg.

This issue is so important that we should look at the numbers and what foreign investors understand the MICC is recommending to the Administration as a new fiscal regime for large-scale mining to take a larger "fair share" and increase tax revenue. The key measure is the Average Effective Tax Rate (AETR). The AETR is the measure used by the International Monetary Fund and other international agencies to evaluate the total discounted cash flows of the public sector "take" of a project.

<u>Under the current fiscal regime there are two situations</u>:

Under a *Mineral Production Sharing Agreement* (in which ownership must be 60% Filipino) in an Ancestral Domain and without the Investment Tax Holiday (which used to be available but the government has recently cancelled) the AETR is 60%. This government tax "take" is somewhat higher than Canada and Australia at 58% (but remember that these countries provide stability and infrastructure support); is significantly higher than Peru and South Africa at 50-55%; and is much higher than Chile (41%) and Papua New Guinea (35%).

Under the *Financial and Technical Assistance Agreement* – which is the fiscal regime for *foreign* investors – AETR is an enormous 96%, now that the government has unilaterally abrogated its previous commitment to allow a five-year cost recovery period. This number is not even in the same order of magnitude as those for Peru, South Africa, Chile and Papua New Guinea.

Please note these numbers are the result of modeling a typical project the way investor companies model it – with real values for inputs, based on real projects – but outputting the IMF's AETR measure to give total discounted government take.

Under the new fiscal regime recommended by the MICC:

According to newspaper reports, the MICC has recommended to the President a new fiscal regime for large-scale mining that: INCREASES the tax rates; taxes projects even when they become loss-making including when commodity prices are low; and imposes windfall-profit taxes when commodity prices are high.

I understand that foreign investors have been prepared to invest in large-scale mining in the Philippines in the past because of the "prospectivity" of the geology and given the AETR was high but not excessive. But with the proposed new fiscal regime the feedback we are getting from potential foreign investors is that this is unlikely to continue given other opportunities in other mining economies.

A third aspect of the "fair share" issue is the argument that raw minerals from mines will be exported, without giving a fair share of lasting value for Filipinos during the mine operations and also leave no continuing economic benefits for Filipinos after the mine is depleted and closed. However economic history in other countries such as Great Britain and USA has shown that, while in some cases "ghost towns" have been left (particularly in Hollywood movies) when mines have been depleted, in most cases initial mining communities have been the seed for and centers of wide-spread diversified business communities. Further this argument ignores that in other cases the raw output of mines may be shipped to other areas within the Philippines for further processing and use…as also has happened in other countries in their economic development.

3. The claim that large-scale mining companies abuse local communities

There are repeated high-profile allegations in the media that large companies force their way onto communities, have security forces that intimidate and commit violent acts (i.e. human rights abuses) and then do nothing for communities that is sustainable. It is also alleged that communities are bribed into supporting large-scale mining, and then left high and dry, socially and economically, worse off than they were before.

However these allegations are often the result of fraudulent anti-mining campaigning, or of actual activities as alleged by small and unregulated companies – often illegal mining. Foreign large-scale companies, from most OECD countries at least, are subject to the public scrutiny of exchange listings, proactive shareholders concerned about environment, human rights, and labor conditions, and international watchdog groups – both governmental and non-governmental. They are much easier to monitor, regulate and hold accountable than smaller and ineffectively regulated companies.

A related argument is that large-scale mining abrogates indigenous peoples' land rights and cultures. By their nature mines are often located in remote mountainous areas where indigenous peoples live, have land rights, and traditions. In the past in countries such as Australia, Canada and the USA with major mining industries such land rights and cultures have not always been adequately respected. But times have changed. There is now globally much greater consciousness of indigenous peoples' land rights and cultures that have to be taken into account in all economic and social development including mining. International institutions such as ADB now have policies to safeguard indigenous peoples' rights. Countries such as Canada negotiate with indigenous peoples who have rights by treaty or custom to ensure these rights are respected and indeed that the indigenous peoples will also benefit from the mining.

The real challenge is for a country where there is mining potential is to have an effective policy for protecting local communities and indigenous peoples to ensure that these are respected in the planning and operation of mines. It is not to just banning mining which may be to the disadvantage of local communities and indigenous peoples (as well as others) in denying them the opportunities and benefits that come with mining.

4. <u>The view that mining is bad: we should focus on agriculture and tourism</u>

Unless one takes the extreme view that there should be no mining globally and we should be prepared to live back in the Stone Age, this is the "NIMBY" argument, "Not in my back yard" – on a national scale. Apart from its moral ambiguity, there are some economic consequences to this position. Since minerals in raw, processed or manufactured form are essential for economic growth and development, the products needed in the Philippines and dependent on mineral inputs will have to be sourced in some other country's backyard. This will result in higher prices for these products in the Philippines and no commensurate added employment for Filipinos. An interesting policy to defend given cost-of-living and unemployment issues in the Philippines!

Moreover it begs the question as to whether the country's long term economic development should assume being primarily a food basket and playground for foreigners (as well as Filipinos) to enjoy; or whether the country needs its long term development to include a more diversified economy with a much expanded range of industries and manufacturing using its own natural resources as well as just its own labor. The bottom line is that the Philippines is blessed with agricultural, tourist, and mineral resources…and that all can be exploited where most appropriate in each area. It does not have to be a zero-sum game as there is room and a place for all to expand!

The argument "our land is better used for development of agriculture and tourism industries" has some merit where specific areas of land are best suited for agriculture and/or tourism. However despite the agricultural productivity in some rural areas and the beauty/interest of some other locations, it is unrealistic to believe that the 85% of the total area of the Philippines – now to be covered by "no go" and/or "mining free" zones – has such potential.

I say 85% because I'm taking the liberty of releasing to you today a composite of the "no-go" zone maps that were recently uploaded to the Mines and Geosciences Bureau web site. Interestingly, as far as I am aware, the maps made available publicly were by region only, and fail to give a cumulative picture. The map I am providing today, was put together independently, rolling up the information in all the MGB regional maps into one national map. As you can see, roughly 85% of the country will be off limits to even minerals exploration, let alone mining (which, by the way, currently occupy only a tiny portion of the country's total area). Relative to agriculture and many other land uses, mining actually has a very small footprint; and it does not always exclude other uses.

In fact in many cases the declaration of "no go" zones, especially by Local Government Units, appears based on local anti-mining lobbying rather than on a realistic assessment of the international market potential for agriculture and/or tourism. The bottom line is that widespread declarations of "no go" zones may not just mean no mining but also no foreign investment for anything else in many of these "no go" zones … certainly many declared "no go" zones will never be a new Boracay for tourism or a new Pampanga for agriculture!

As a final footnote to the argument that agriculture and tourism are better alternatives than mining, I recall a seminar on mining some years ago in the Philippines which concluded with a resolution that large-scale mining should be banned but small scale mining should be allowed as an alternative because it benefitted directly local inhabitants. It struck me as rather odd and naive given reality of small-scale mining:

- Small-scale mining cannot achieve economic benefits of large-scale mining.
- It is extremely hard to effectively regulate small scale-mining.
- Small-scale mining opens opportunities for corruption allowing illegal mining
- Illegal small-scale mining does not pay tax or give a "fair share" to the state.
- Illegal "small-scale" mining can be quite large
- Illegal small-scale mining has had disastrous adverse environmental impact
- Illegal small-scale mining leads to unsafe labor practices including child labor.

It is not within the scope of my speech to comment more on small-scale mining except to say it does not appear to be an environmentally, socially, economically or practical alternative to large-scale mining.

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Observations on discussion of large-scale mining in the Philippines

I would like to add some general observations about the nature of the pro vs anti-mining debate from a foreign investors' perspective:

- The arguments and issues raised are substantive, and should be discussed.
- Most public discussion has been by the anti-mining and the pro-mining groups with inadequate input from other third-party stakeholders.
- Most argumentation by anti-mining groups appears to focus on large foreign corporations, rather than on domestic and small scale mining
- Most argumentation has been inward-looking and ignores advances and experience in mining in other developed mining economies in recent years.
- The main advisory committee on mining in the national government … the MICC … does not include adequate representation of the private sector in general and in the mining industry in particular.
- As a result the MICC appears to have an anti-mining industry bias and does not always fully understand modern mining practices and economics of mining.

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Conclusions

My understanding of what foreign investors want as support large-scale mining is:

(1) A strong statement by the President in the next SONA that he supports a minerals industry in the Philippines — *including* foreign investments;

(2) A strong statement by the President in the next SONA that he intends to retain the current Mining Act of 1995, to strictly enforce it by allocating greater resources to the relevant regulatory agencies, and to make one change in it: To allow foreign investors to invest on an equal footing with national investors in order to encourage the deployment of foreign capital, technology and best practices. With this, the onerous FTAA contract could be dropped, and foreign investors allowed to participate in MPSA contracts. This change would have an enormous effect in stimulating investment in the industry (provided the fiscal terms are not increased from their already high levels (by comparison with competitor countries).

(3) The government scrap the recent, excessive "no go" zone maps; and start afresh in confronting the land use issue of minerals development vs. other uses. In revising the "no go" zone policy for areas where there is identified mineral potential, a "no go" zone should only be confirmed where there is also a demonstrated, *mutually exclusive* agriculture and/or tourist potential in the same area, with these 'no go" zones having a sunset clause that, if development of the agriculture and/or tourism potential has not been started within five years, the "no go" zone will be cancelled.

(4) Given the dispute about appropriate "fair share" revenues from mining, the government wait until the first report by the Extractive Industries Transparency Initiative (EITI) before making changes to the fiscal regime.

(5) As part of review of "fair share", the national government consider allocating 50% of total mining revenues collected by the public sector to LGUs, with 50% of this going directly to the province in which the mine is located and the remaining 50% to split and go directly to the municipalities and barangay(s) in which the mine is located.

(6) The government follow-up on Executive Order 79 to intervene forcefully with concerned Local Government Units who have imposed mining bans in contravention with national law. In particular, it should intervene to ensure that the law is properly applied in the case of the Tampakan Project, so the country's single largest economic development project can be evaluated and permitted in accordance with the Mining Act.

(7) The current MICC be expanded to be a new Consultative and Advisory Council on Mining (CACM) with wider stakeholder representation including in equal number, representatives of the national government (including DENR, DTI, DOF, NEDA, and NCC), LGUs, and the mining industry (including Chamber of Mines and JFC) with the Council co-chaired by the government and private sector like the National Competitiveness Council.

Thank you.