



**WILL IMPLEMENTING PILLAR TWO MEASURES HINDER THE
REHABILITATION OF SOUTH AFRICAN MINES?**

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Minor research dissertation presented for the approval of Senate in fulfilment of part of the requirements for Master of Commerce (MComm) Specialising in International Taxation in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

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DEDICATIONS

I dedicate this dissertation to my family, whose support, love, and encouragement are the firm foundation upon which my academic journey could follow. Thank you to my father for his endless hard work and devotion, where education was always within reach. Your sacrifices have helped pave my path because education is the most powerful asset the world can have.

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ABSTRACT

South Africa imposes rehabilitation obligations on mining right holders to address the damage caused by mining operations. The National Environmental Management Act, 17 of 1998 (“**NEMA**”) requires each mining right holder to make financial provision to cover their rehabilitation costs in the future. A rehabilitation trust is one of the allowable financial vehicles listed under NEMA for purposes of financial provisioning.

The mining right holder funds the rehabilitation trust through contributions that the trust invests in. Under section 37A, read with section 10(1)(cP) of the South African Income Tax Act, 1962 (“**ITA**”), the mining right holder can deduct these contributions for income tax purposes. The rehabilitation trust is also granted a tax exemption for all receipts accruing to it.

In December 2024, the Global Minimum Tax Act, 46 of 2024 (“**GMT Act**”) was enacted in South Africa to implement Pillar Two measures in South Africa. Pillar Two imposes a global minimum tax of 15 per cent on multinational entities with revenue of EUR750 million or more to prevent large multinationals from shifting their profits to low-taxed jurisdictions. The Global Anti-Base Erosion (“**GloBE**”) rules and commentary guide the calculations to determine the effective tax rate and resulting top-up tax payable in terms thereof.

This dissertation evaluates whether imposing Pillar Two measures in South Africa would render rehabilitation trusts ineffective and inefficient due to the ITA tax incentive that may result in a lower GloBE effective tax rate, ultimately forcing mining groups to pay a top-up tax for rehabilitation compliance.

The main finding of this dissertation is that rehabilitation trusts, as members of a multinational group (“**MNE**”) with revenue of EUR 750 million or more, will have their financials included in the mining group's effective tax rate calculation regarding Pillar Two. The tax incentive provided in the ITA could affect the calculation by lowering the mining group's effective tax rate to below 15 per cent, resulting in the payment of top-up taxes. The concern is that mining groups will be deterred from using rehabilitation trusts, which would abandon them and complicate their regulation, as the other vehicles are not as regulated. The solution presented in this dissertation is to include rehabilitation trusts as an excluded entity for purposes of Pillar Two, as they operate similarly to governmental entities.

KEYWORDS

The following words (or abbreviations) have been used:

Art	Article
BEPS	Base erosion and profit shifting
CFC	Controlled foreign company
CGT	Capital gains tax
Decommissioning	The process of shutting down an operation with the removal of buildings and the withdrawal from service of equipment, plant and machinery used in relation to an operation regulated in terms of the Minerals and Petroleum Resources Act, 2002.
GloBE	Global Anti-Base Erosion
GloBE Commentary	Tax Challenges Arising from the Digitalisation of the Economy – Consolidated Commentary to the Global Anti-Base Erosion Model (2023), published 25 April 2024.
GloBE Rules	Global Anti-Base Erosion Model Rules (Pillar Two) published 20 December 2021.
GMT	Global minimum tax
IFRS	International Financial Reporting Standards
IIR	Income Inclusion Rule
ITA	Income Tax Act, No. 8 of 1962
MNE	Multi-national enterprise
MPRDA	Minerals and Petroleum Resources Development Act, 28 of 2002
NEMA	National Environmental Management Act, 107 of 1998
OECD	Organisation for Economic Cooperation and Development
PE	Permanent establishment
SA	South Africa
SARS	South African Revenue Service
Treasury	South African National Treasury
UPE	Ultimate Parent Entity

1 CHAPTER ONE: INTRODUCTION

1.1 Background

In 2007, the Department of Mineral Resources and Energy (“**DMRE**”) estimated costs of about R100 billion to rehabilitate closed and disused mines.¹ Mining rehabilitation refers to the process whereby the land damaged by the mining operations is repaired to a safe and stable state.² This amount would be significantly higher in 2025 due to inflation and the increase in mine closures due to the economic downturn.³ In 2021, the number of abandoned mines, according to the Auditor General, was at 6,100, an almost 3% increase since its last report in 2007.⁴ Of these abandoned mines identified in 2007, only 0,7% had been rehabilitated by 2017.⁵

These statistics are further emphasised by the World Bank’s predictions that within the next 25 years, several mines in developing countries will close.⁶ The rate at which mines are rehabilitated against the increase in abandoned mines presents the stark reality that insufficient enforcement is in place to protect the health and well-being of the environment and the communities.⁷

To improve the management of mine closures and rehabilitation, the South African legislature, through the Mineral and Petroleum Resources Development Act No. 28 of 2002 (“**MPRDA**”), required all mining rights holders to set aside funds to discharge their mining rehabilitation obligations.⁸

One way to make financial provision for the above is for the mining right holders (the “**contributor**”) to establish a trust or company (a “**rehabilitation trust**”) to which they can make contributions to fund rehabilitation at closure.⁹ As an incentive, South African National Treasury (“**Treasury**”) provides approved rehabilitation trusts with a tax exemption of all their receipts and accruals in terms of section 37A of the South African Income Tax Act 58 of 1962 (the “**ITA**”).¹⁰

¹ Zoe Almano ‘The Rehabilitation and Closure of Mines: A Failure in the Protection of Human Rights’ *UCT Mineral Law in Africa* 10 November 2022, available at <https://law.uct.ac.za/mineral-law/articles/2022-11-10-rehabilitation-and-closure-mines-failure-protection-human-rights>, accessed on 2 February 2025.

² Preamble to the Minerals and Petroleum Resources Development Act, 28 of 2002.

³ Ibid.

⁴ Ibid.

⁵ Ibid.

⁶ World Bank ‘and International Finance Corporation ‘It’s not over when it’s over: Mine closure around the world’ available at <https://www.mineclosure.net/elibrary/it-s-not-over-when-it-s-over-mine-closure-around-the-world>, accessed on 4 February 2025.

⁷ Almano op cit note 1.

⁸ R Krause and L Snyman “Rehabilitation and mine closure liability: An assessment of the accountability of the system to communities” (2014) unpublished paper presented at the *9th International Conference on Mine Closure* hosted by the University of the Witwatersrand at the Sandton Convention Centre, Johannesburg, 01-10-2014 - 03-10-2014.

⁹ B Strydom & D McMeekin ‘Mining rehabilitation funds’ South African Institute of Taxation (28 October 2014), available at <https://www.thesait.org.za/news/210176/Mining-rehabilitation-funds.htm>, accessed on 11 February 2025.

¹⁰ Section 10(1)(cP) to the ITA.

Due to the importance of promoting and ensuring proper rehabilitation of mines, it is questionable whether the two-pillar approach to global base erosion and profit shifting (“**BEPS**”) introduced by the Organisation of Economic Cooperation and Development (“**OECD**”) could affect the use of rehabilitation trusts. In particular, the recent imposition of Pillar Two rules in the South African tax legislative framework. Pillar Two imposes a global minimum tax rate (“**GMT**”) on multinational enterprises (“**MNEs**”) to ensure a minimum tax rate of 15 per cent is levied, regardless of where it is headquartered or where its profits arise (“**Pillar Two**”).¹¹ It must, therefore, be investigated whether this global development could impact large mining companies’ tax incentives and overall tax strategy.

1.2 Research question

This dissertation investigates whether introducing Pillar Two measures in South Africa will undermine the tax benefit granted by Treasury as part of an effort to encourage the rehabilitation of disused mines.

The research question is investigated by considering the difference between the tax and accounting treatment of rehabilitation trust contributions and interest receipts.

In addition, the research question is tested by examining how Pillar Two calculates the effective tax rate and how this calculation will be applied to rehabilitation trusts and the mining groups it forms part of. Against this backdrop, the policy rationales of the tax incentive and Pillar Two must be investigated to determine whether applying the tax incentive and Pillar Two provisions will undermine either rationale.

This dissertation concludes by addressing where mining companies could risk showing an effective tax rate below 15 percent and whether any amendments to the GloBE Base Erosion Rules (“**GloBE Rules**”) could be proposed to address this risk specifically posed to mining companies with rehabilitation trusts.

1.3 Structure of the dissertation

This dissertation provides an overview of rehabilitation trusts' history, workings, and purpose in Chapter Two.

Chapter Three further provides the criteria identified by the OECD against which a tax incentive must be reviewed.

¹¹ OECD ‘GloBE Anti-Base Erosion Model Rules (Pillar Two)’ Available at: <https://www.oecd.org/en/topics/sub-issues/global-minimum-tax/global-anti-base-erosion-model-rules-pillar-two.html>, accessed on 11 February 2025.

Chapter Four provides an analysis of the accounting treatment of rehabilitation trusts according to the International Financial Reporting Standards (“IFRS”) and the tax treatment under the ITA.

This dissertation, in Chapter Five, briefly discusses the GMT as presented in the GloBE Model Rules in Pillar Two, published by the OECD.

Chapter Six looks at rehabilitation trusts from an international perspective by investigating the tax incentives for mining rehabilitation provided by Australia and Canada in their mining tax regimes.

Further, Chapter Seven of this dissertation briefly examines the criteria against which a good and efficient tax incentive is measured and reviewed in the context of the imposition of Pillar Two measures.

Lastly, Chapter Eight analyses the impact that Pillar Two measures may have on mining groups with rehabilitation trusts, considering the findings of this dissertation holistically. In addition to discussing the conclusions reached, recommendations are discussed to address the identified problems.

1.4 Research Methodology

This dissertation seeks to investigate the research question through doctrinal research, which refers to the systematic process of ‘identifying, analysing, organising and synthesising statutes, judicial decisions, and commentary.’¹² It considers information from various forms of literature, including industry reports, academic commentary, academic textbooks, online publications, and various other communications and publications disseminated by appropriate institutions.

The legislative framework was also considered alongside the South African income tax and GMT legislation. Further, as the GloBE Rules inform the Global Minimum Tax Act, 46 of 2024 (“GMT Act”) and the Global Minimum Tax Administration Act, 47 of 2024 (“GMT Admin Act”), the most recent commentary published by the OECD was also researched.

1.5 Limitations of scope

South African courts and Treasury have not yet provided clear guidance on Pillar Two's effect on rehabilitation trusts and the tax incentives they receive.

¹² Margaret McKerchar ‘Philosophical paradigms, inquiry strategies and knowledge claims: applying the principles of research design and conduct to tax’ (2008) 6 *eJournal of Tax Research* 5 at 18-19.

As discussed in more detail in Chapter Two, this dissertation only considers contributions recognised as revenue for the discussions in Chapters Two and Three due to their characteristics in terms of South African mining law and tax laws and the common practice within the mining industry of recording them as such.

2 CHAPTER TWO: REHABILITATION TRUSTS

2.1 The brief history of mining rehabilitation

The discovery and development of the mining industry in the 1880s placed South Africa on the industrial map.¹³ By the start of the 20th century, South Africa was the largest producer of diamonds and gold globally.¹⁴ However, this rampant economic growth came at a high price: the mining industry destroyed most of South Africa's natural environment during this time.¹⁵

In the early years of gold mining, the resultant mining waste was poorly disposed of due to a lack of legislative regulation.¹⁶ Mining waste is the natural materials left over after extracting and/ or processing ore bodies.¹⁷ Mine waste residues can take many forms, such as waste rock or overburden material removed when accessing the ore body.¹⁸ By contrast, slimes, sands, or tailings are waste products from extracting the ore from the geological strata through physical and chemical processes.¹⁹

Gold digging was illegal in the 1870s, and after its legalisation in the 1880s, the state remained reluctant to formalise any regulatory framework for mining rehabilitation."²⁰ The lack of legislation resulted in miners disposing of mine waste on disused land near their mining operations.²¹ The only change in practice in the following twenty years resulted from urbanisation in the surrounding areas, creating a shortage of disposable areas.²² Mostly, the resultant mining waste deposits (left untreated) were merely seen as "the cost of doing business" – deemed an inevitable result of mining operations.²³

With the advent of the twentieth century, the shortage of suitable disused land for deposition became too large to ignore, with increased health and safety risks.²⁴ More formalised efforts were made to address deposition and rehabilitation, albeit experimental and ad hoc.²⁵

Unfortunately, the mining industry's reactive attitude towards rehabilitation remained a common thread throughout the industry's first 50 years.²⁶ Only in the 1940s did the mining

¹³ Markus Reichardt 'The Wasted Years: A history of mine waste rehabilitation methodology in the South African mining industry from its origins to 1991 (unpublished Doctor of Philosophy thesis, University of the Witwatersrand, 2013) 39.

¹⁴ Ibid.

¹⁵ Ibid.

¹⁶ Ibid.

¹⁷ Ibid under "Glossary".

¹⁸ Ibid.

¹⁹ Ibid at 21.

²⁰ Ibid at 46 - 47.

²¹ Ibid at 45.

²² Ibid at 47.

²³ Ibid at 39.

²⁴ Ibid 47.

²⁵ Ibid at 39, 47.

²⁶ Ibid at 39.

industry start employing a group of people to research rehabilitation methodology specifically.²⁷

Following a decade of experimentation, gold mining industry players combined efforts with the Chamber of Mines of South Africa (“**CoM**”) to initiate mining rehabilitation.²⁸ The collaborative effort was called the Vegetation Unit (the “**Unit**”), and it conducted large-scale experiments on developing rehabilitation methodologies between 1959 and 1963.²⁹ Unfortunately, the Unit's efforts were short-lived following the premature rollout of its rehabilitation methodology in the 1960s and 1970s.³⁰

The Unit's collapse was, among other things, due to insufficient technical staff who needed more knowledge to continue advancing the methodology.³¹ With the systematic demise of the Unit, the industry was ultimately left without any capacity to address mining rehabilitation when the world started to acknowledge the environmental concerns related to the mining industry.³²

In the 1980s, private companies identified a gap in the mining rehabilitation market. The Unit operated under severe capacity constraints, and despite regaining some of its former glory by developing rehabilitation guidelines, it could not compete with new entrants to the market.³³

The 1990s were formative years of collaboration between industry stakeholders and the government to align mining rehabilitation and closure policies.³⁴ As a modernised and formalised adaptation of the Mines and Works Act, 27 of 1956 (repealed), a significant landmark in the South African mining rehabilitation landscape was the introduction of the Minerals Act, 50 of 1991 (repealed) (“**Minerals Act**”).³⁵ The promulgation of the Minerals Act, for the first time in South African mining history, provided for the obligation of continuous rehabilitation of mines and at-closure rehabilitation.³⁶ Due to the imposition of this obligation on mining right holders instead of the Unit, the Unit struggled to retain its importance in the industry. Eventually, it was privatised, and the CoM was restructured.³⁷

The Minerals Act provided for the continuous and post-closure rehabilitation of mines by linking the responsibility to rehabilitate to the right to mine.³⁸ In addition, mining right holders

²⁷ Ibid at 39.

²⁸ Ibid at 30.

²⁹ Ibid Abstract.

³⁰ Ibid.

³¹ Ibid.

³² Ibid.

³³ Ibid.

³⁴ Ibid at 566

³⁵ Ibid Abstract.

³⁶ Ibid.

³⁷ Ibid.

³⁸ Ibid.

were required to ensure that they would have adequate funds to finance their rehabilitation responsibilities and obligations.³⁹ The ability to pay for rehabilitation costs was inserted as a requirement before a mining right was granted and held.⁴⁰ This was the first time a post-closure liability was created in law, together with a corresponding financial provision to be made for such liability.⁴¹

From an economic perspective, the Minerals Act improved the environmental management industry by creating rehabilitation requirements, increasing local and international business opportunities within the private sector, and forcing mining groups to enhance their in-house functions.⁴² Despite the movement to rehabilitation seemingly being profit-driven by private firms exploiting the economic opportunity posed by a growing mining rehabilitation market, more funds were raised for research and development regarding rehabilitation and closure of mines between 1991 and 2012 than in the 60 years before the Mineral Acts were enacted.⁴³

However, the government failed to successfully implement mining rehabilitation regulations due to policy disagreements within and between government departments and a lack of specificity in implementation. Accordingly, the mismanagement of abandoned mines continued.

2.2 South African mine rehabilitation in the twenty-first century

The Constitution of the Republic of South Africa, 1996 (the “**Constitution**”) protects people’s right to an environment that is not harmful to their health or well-being. It makes the government responsible for ensuring that reasonable legislation is in place to protect these rights.⁴⁴

The MPRDA repealed the Minerals Act to expand on the imposition of the obligation on mining rights holders to ensure that mines are properly rehabilitated for environmental purposes at the end of use.⁴⁵ Aptly, the preamble to the MPRDA states that:

“South Africa’s mineral and petroleum resources belong to the nation, and the South African government, as custodian of these resources, must protect the environment and the longevity of these resources.”

³⁹ Ibid at 142.

⁴⁰ Ibid.

⁴¹ Ibid at 564 – 565.

⁴² Ibid at 566.

⁴³ Ibid at 585.

⁴⁴ Section 24 to the Constitution.

⁴⁵ J K McLean, P J Carrick ‘Environmental Management and Rehabilitation under the Minerals and Petroleum Resources Development Act: A Biodiversity Outlook’ (2007) 14 *SAJELP* 187 191.

The key objective behind the promulgation of the MPRDA is to ensure mining companies take responsibility for the development and growth of the communities in which they operate.⁴⁶ To ensure a uniform and adequate standard of mine closure practice, the MPRDA provides objectives that mining companies must meet.⁴⁷ These objectives include eliminating any potential harm to the community's health and safety, ensuring the safety of the water quality for domestic use, and ensuring the well-being of animal and plant life in the area.⁴⁸

Financial provisions within the context of mine rehabilitation mean the funds required to be set aside by mining companies to meet their statutory rehabilitation obligations at mine closure.⁴⁹

The statutory obligations relating to rehabilitation trusts imposed on holders of prospecting and mining rights were initially provided for in section 41 of the MPRDA. Regarding the MPRDA, the responsibility to make financial provisions for the rehabilitation of mines includes rehabilitation costs incurred during the premature closing of mining operations, the final closure of the operations, and post-closure management.⁵⁰ The MPRDA Regulation 55 provided that the financial provision required for rehabilitation could be provided for by way of one or more of the following methods:

- a) An approved contribution to a trust fund in the format as approved by the Director-General from time to time (also commonly known as a rehabilitation trust)⁵¹;
- b) A financial guarantee from a South African bank (or any other bank or financial institution approved by the Director-General) guaranteeing the financial provision relating to the environmental management program or plan in the format as approved by the Director-General from time to time;
- c) A deposit into the account specified by the Director-General in the format as approved by the Director-General from time to time or
- d) Any other method the Director-General may use is also available.

In December 2014, the Department of Mineral Resources and Energy (“**DMRE**”), the Department of Environmental Affairs (“**DEA**”) and the Department of Water Affairs and Sanitation agreed to integrate different aspects of the environmental management of mining activities into one system, named the “One Environmental System”.⁵² The need arose to

⁴⁶ A Fourie, A C Brent ‘A project-based mine closure model (MCM) for sustainable asset life cycle management’ (2008) 14 (12-13) *J Clean Prod* p 1085–1095.

⁴⁷ *Ibid.*

⁴⁸ J Stacey, A Naude, M Hermanus, P Frankel ‘The economic aspects of mine closure and sustainable development. Literature overview of lessons for the socioeconomic aspects of closure’ 110(7) (2010) *J.S.Afr.Inst.Min.Metall* 379 – 381.

⁴⁹ National Environmental Management Act, 107 of 1998 Regulations pertaining to the financial provision for prospecting, exploration, mining or production operations, Government Gazette Notice No. 39425.

⁵⁰ Regulation 53(1) and 54 of the regulations promulgated under the MPRDA (the “**MPRDA Regulations**”).

⁵¹ As was then required in terms of section 10(1)(cH) of the ITA (now repealed and replaced by section 37A of the ITA).

⁵² S Mappinga ‘The One Environmental System for the Mining Industry: Has it given rise to intra-governmental conflict of interest?’ available at: <https://law.uct.ac.za/mineral-law/articles/2017-12-05-one-environmental-system-mining-industry-has-it-given-rise-intra-governmental-conflict-interest>, accessed on 8 February 2025.

consolidate the ecological management legislation after concerns were raised about the environmental regulation of mining operations in South Africa.⁵³ Investors found the regulatory framework convoluted and over-regulated, resulting in a duplication of bureaucratic processes.⁵⁴

The One Environmental System is structured so that the National Environmental Management Act No. 17 of 1998 (“**NEMA**”) regulates the provisions relating to mining's environmental management. The MPRDA Amendment Act, 49 of 2008 (which only commenced in 2013), removed all environmental clauses from the MPRDA.⁵⁵ NEMA entrenched the DEA's power to set a regulatory framework for environmental management.⁵⁶ The DMRE is, however, mandated to implement it.⁵⁷

Under NEMA, a mining right holder must determine and make financial provisions to guarantee the availability of sufficient funds to undertake the rehabilitation and remediation of the adverse impacts of its mining operations to the satisfaction of the Minister.⁵⁸

The requirements and method for determining the financial provision, as well as the financial vehicles that may be used for it, are set out in the Regulations to the Financial Provision for Prospecting, Exploration or Production Operations (Government Gazette No. 39425) (the “**NEMA Regulations**”).

Under Regulation 6 of the NEMA Regulations, the financial provision for annual and final rehabilitation and future remediation must be determined. Annual rehabilitation means rehabilitation “as reflected in the annual rehabilitation plan” to restore or repair the damaged area every year (“**Annual Rehabilitation**”).⁵⁹ Final rehabilitation refers to the “decommissioning and closure of the ... mining or production operations, as reflected in a final rehabilitation, decommissioning and mine course plan” (“**Final Rehabilitation**”).⁶⁰ Future remediation, on the other hand, refers to “remediation of latent or residual environmental impacts which may become known in the future” (“**Future Remediation**”).⁶¹

Similarly to the repealed Regulation 55 of the MPRDA, Regulation 8 to the NEMA Regulations now provides for a limited number of ways through which a holder of a mining right may only

⁵³ Ibid.

⁵⁴ Ibid.

⁵⁵ Ibid.

⁵⁶ Section 50A NEMA.

⁵⁷ Section 50A(b) of NEMA.

⁵⁸ Section 24P of NEMA.

⁵⁹ NEMA Regulation 6(a).

⁶⁰ NEMA Regulation 6(b).

⁶¹ NEMA Regulation 6(c).

make provision for the rehabilitation of environmental damage by one or a combination of the following:

- (a) A financial guarantee from a bank or financial institution registered by the Financial Services Board (the “**FSB**”) as an insurer or underwriter;⁶²
- (b) A deposit into an account administered by the Minister for Mineral Resources;⁶³ or
- (c) A contribution to a trust fund.⁶⁴

However, regulation 8(1)(c) of the NEMA Regulations provides that a contribution to a trust fund may not be used for annual and final rehabilitation; it may only be used for future remediation. Therefore, the financial provision through a trust fund is limited.

From November 2017 to May 2019, the DEA issued several notices setting out proposed amendments to the NEMA Regulations for comment by interested parties (the “**Notices**”).⁶⁵ The notices suggested amending Regulation 8 to provide that a rehabilitation trust may be used to make financial provisions for annual and final rehabilitation.⁶⁶ In addition, it was proposed that one or a combination of the allowable financial vehicles may be used to make financial provisions for both annual and final rehabilitation and future remediation.⁶⁷ Further, it suggested that a mining or prospecting right holder must provide funds for the costs required to implement the activities for annual rehabilitation from its operational budget.⁶⁸

The proposed amendments to the NEMA Regulations in the Notices are yet to be promulgated. Accordingly, as promulgated on 20 November 2015, the NEMA Regulations are still in full force and effect.

Notwithstanding some developments regarding the NEMA Regulations, there remains uncertainty as to whether and how they will be changed, especially in the current environment regarding rehabilitation trusts and their scope.

⁶² NEMA Regulation 8(1)(a).

Take note that since 1 April 2018, the responsibilities of the FSB have been split into two new agencies, namely the Financial Sector Conduct Authority (“**FSCA**”) and the Prudential Authority (“**PA**”). This change was effected by the implementation of the Financial Sector Regulation Act, 2017.

⁶³ NEMA Regulation 8(1)(b).

⁶⁴ NEMA Regulation 8(1)(c).

⁶⁵ GN 1228 GG 41236 of 10 November 2017 (“**2017 Notice**”); GN 991 GG 41921 of 21 September 2018 (“**2018 Notice**”) and GN 667 GG 42464 of 17 May 2019 (“**2019 Notice**”).

⁶⁶ Regulation 6 of the 2017 Notice.

⁶⁷ Regulation 8 of the 2017 Notice.

The vehicles listed include:

“(a) Cash deposited in an account managed by the Minister of Mineral Resources;

(b) A trust fund;

(c) A closure rehabilitation company;

(d) Insurance from an institution registered under the relevant insurance sector legislation benefiting the Minister of Mineral Resources; and

(e) A financial guarantee from an institution registered under the relevant financial sector legislation benefiting the Minister of Mineral Resources.”

⁶⁸ Regulation 7 of the 2019 Notice.

Despite the above, these Notices indicate the legislature's intention to expand the scope of these rehabilitation funds further by allowing funds to accumulate for Annual Rehabilitation, as opposed to solely Closure Rehabilitation, in this financial vehicle.

2.3 The use and workings of rehabilitation trusts

The mining right holder (as the “**contributor**”) establishes a trust or company to which it can contribute cash.⁶⁹ The rehabilitation trust's accumulated funds will fund the mine's future remediation.⁷⁰ In the interim, the rehabilitation trust will invest the contributions made by the contributor, which will grow as the return on its investments increases.⁷¹

Funds in such a rehabilitation trust can only be used to meet its established objectives of funding Future Remediation for a mining operation governed by NEMA.⁷² This applies to final closure, decommissioning, and any latent environmental impacts that arose after the mine's closure.⁷³

The NEMA Regulations provide for a prescribed form of the mining rehabilitation trust deed and the requirements it must contain.⁷⁴ One requirement is that the rehabilitation trust may only invest in so-called “capital-guaranteed” instruments.⁷⁵ Despite this, the NEMA Regulations fail to define this term. Capital-guaranteed instruments generally refer to investments with capital preservation as their primary purpose. In addition, the prescribed form of the trust deed in Appendix 2 of the NEMA Regulations provides a list of allowable investments.⁷⁶ Thus, limiting investments to those that are “capital-guaranteed” essentially safeguards contributions from being eradicated through risky investment mandates.⁷⁷

Section 37A of the ITA mirrors the list of permissible investments for rehabilitation trusts in the prescribed trust deed.⁷⁸ These include financial instruments issued before 18 November 2003 by collective investment schemes, long-term insurers, banks, mutual banks, the government, listed companies, or investments.⁷⁹

⁶⁹ J Kotze ‘Mining Rehabilitation Vehicles’ *KPMG Tax and Legal* October 2020 at 1, available at <https://assets.kpmg.com/content/dam/kpmg/us/pdf/2020/10/mf-south-africa2-oct15-2020.pdf>, accessed on 14 February 2025.

⁷⁰ *Ibid.*

⁷¹ M Stiglingh *Silke: South African Income Tax* (2024), ch 16 para 16.8A ‘Environmental rehabilitation’, accessed on Lexis Nexis 15 February 2025.

⁷² *Ibid.*

⁷³ *Ibid.*

⁷⁴ Appendix 2 of Chapter 5 to GNR 1147 of 20 November 2015.

⁷⁵ Clause 1.8 of Appendix 6 of GG 45058 of 27 August 2021.

⁷⁶ Clause 12.5.1 of the Deed as found in Appendix 2 of the NEMA Regulations.

⁷⁷ Stiglingh *op cit* note 100.

⁷⁸ *Supra* note 74.

⁷⁹ Section 37A(2)(a) – (d) to the ITA.

Funds will only be released to the contributor to enable it to perform rehabilitation activities; no withdrawal of funds is permitted for any other purpose.⁸⁰

Upon completion of rehabilitation activities, any remaining excess funds must be transferred to another rehabilitation trust or the DMRE.⁸¹ Excess funds may not be returned to the original contributor.⁸² Section 37A(3) of the ITA provides that to the extent that the Minister of Minerals and Energy is satisfied that the relevant areas have been rehabilitated, the rehabilitation company or trust must be wound up or liquidated, and its assets remaining after satisfaction of liabilities must be transferred to another company or trust qualifying under this provision and approved by the Commissioner.

In addition, when the Minister of Minerals and Energy is satisfied that a company or trust will be able to meet its liabilities and that it has sufficient assets to rehabilitate and restore all areas, it may transfer non-required assets to another company or trust established in terms of section 37A, as approved by the Commissioner to attend to the rehabilitation of other mines it may still need to rehabilitate.⁸³

The Commissioner may apply significant penalties for non-compliance with the above rules, primarily where financial instruments not allowed under section 37A of the ITA are held or where the funds are used for purposes other than those prescribed.⁸⁴ These penalties equal 50% of the highest market value of that prohibited financial instrument acquired or property unduly disposed of during the assessment year. The mining right holder's gross income will include the penalty amount.⁸⁵

⁸⁰ Regulation 15(1) of the NEMA Regulations.

⁸¹ Section 37A(3) to the ITA.

⁸² Supra note 80.

⁸³ Section 37A(4) of the ITA.

⁸⁴ D French & R Stretch 'Mining, Oil and Gas' in *LexisNexis SA Income Tax of South Africa*, accessed on <https://www-mylexisnexus-co-za.ezproxy.uct.ac.za/> on 15 February 2025.

⁸⁵ Section 37A(6) and (7) to the ITA.

3 CHAPTER THREE: OECD CRITERIA FOR REVIEWING TAX INCENTIVES

3.1 The OECD Practice Note

The OECD published a practice note on how governments can review tax incentives to mining sector stakeholders, providing criteria against which a tax incentive can be reviewed.⁸⁶ The OECD recognises that many developing countries, such as South Africa, rely heavily on the revenue generated by the mining sector.⁸⁷ Policymakers are, therefore, tasked with designing tax regimes that incentivise investment and sustainability in the industry.⁸⁸ It is, hence, important for policymakers to review these tax incentives considering international policy changes to evaluate whether they still serve their purpose, have become overly generous, or may result in losing significant tax revenues.⁸⁹

3.1.1 Efficiency and Efficacy

The first test when reviewing a tax incentive is efficiency.

The tax incentive must remain efficient. Efficiency relates to the cost of meeting the policy objective of the relevant tax incentive.⁹⁰ This involves testing whether the policy objective can be met at a lower price in other ways.⁹¹ Some factors considered when evaluating the efficiency of a tax incentive are:⁹²

1. What investment (or contribution) would have been made if the incentive had never existed?
2. Whether the government costs and resultant revenue losses are low.
3. Whether the administration costs of the incentive are low.

Conducting a cost-benefit analysis is helpful when evaluating effectiveness and efficiency.⁹³ The comparison helps identify whether the envisaged benefits of the tested tax incentive will still outweigh the costs.⁹⁴ Table 1 below provides some factors to consider when performing the cost-benefit analysis.

Costs	Benefits
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⁸⁶ A Readhead 'Tax Incentives in Mining: Minimising Risks to Revenue' (2018) *International Institute for Sustainable Development and the Organisation for Economic Co-Operation and Development*, Published by the International Institute for Sustainable Development, 11.

⁸⁷ *Ibid* at 2.

⁸⁸ *Ibid*.

⁸⁹ *Ibid*.

⁹⁰ *Ibid* at 13 - 14.

⁹¹ *Ibid*.

⁹² *Ibid*.

⁹³ *Ibid*.

⁹⁴ *Ibid*.

<ul style="list-style-type: none"> • Immediate revenue loss. • Additional revenue loss due to behavioural responses (covered in detail in Part Two). • Administrative costs of implementing and monitoring incentives (which are usually incurred by the tax administration). • Economic distortions introduced due to differential treatment of certain investments (e.g., import duty exemptions for foreign mining equipment suppliers make it harder for local manufacturers to compete, potentially undermining local content goals). 	<ul style="list-style-type: none"> • GDP or gross value added: the amount of economic value the mining operation brings to the economy. • Employment: the number of jobs created by the mining operation. • Government revenues: the amount of revenue generated for the mining country government
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Table 1: Costs and benefits of mining tax incentives (from Readhead *OECD* 2018)⁹⁵

3.1.2 Potential behavioural responses

The second inquiry involves determining the likelihood of mining groups changing their behaviour or views of the tax incentive provided.⁹⁶ Behavioural changes examine how taxpayers respond to the introduction of tax incentives.⁹⁷ These responses are often strategic, aiming to maximise the tax benefits offered, which can sometimes lead to unintended consequences for government revenues.⁹⁸

The impact of these behavioural responses must also consider the government's potential fiscal revenues and mining rehabilitation enforcement. This will be regarded broadly by looking at (i) the nature of the incentive, (ii) the design of the incentive, and (iii) the potential revenue impact on the government and taxpayers.⁹⁹

3.1.2.1 The nature of incentives/ exemptions

This section provides a framework for determining the likelihood that mining stakeholders will change their behaviour depending on the type of tax incentive, its design, and its impact on government revenues.

⁹⁵ Ibid at 14.

⁹⁶ Ibid.

⁹⁷ K Walsh 'Understanding Taxpayer Behaviour New Opportunities for Tax Administration' (2012) *The Economic and Social Review*, Vol. 43, No. 3 451 457.

⁹⁸ Ibid 464.

⁹⁹ Readhead op cit note 86 at 14 – 18.

It is essential to relate the analysis of tax incentives to the broader fiscal package. In Table 2 below, the risk ranking is based on (i) the likelihood that the incentive will trigger a behavioural response and (ii) the subsequent impact on government revenues. It is grounded in practitioners' experience and judgment rather than statistics.

Tax Incentive	Potential Behavioural Response	Risk
Income tax holidays	Investors may increase their income during the tax-free period by speeding up the rate of production and shifting the profits offshore.	HIGH
Export processing zones (EPZs)	EPZs may set up a competing fiscal regime between the mineral processing facility and the mine. In response, investors may seek to reduce their taxable income by selling their mineral production at a below-market rate to its related party smelter, which is subject to a lower rate of tax in the EPZ.	
Royalty-based incentives	Investors may shift revenues into the tax-free period, like the response to a tax holiday. A sliding-scale royalty may encourage tax planning strategies to avoid falling into a higher royalty bracket.	
Fiscal stabilisation assurances (i.e., the mining fiscal regime is frozen)	Fiscal stabilisation does not trigger a specific behavioural response. But combining incentives with excessive use of broad and long-term fiscal stability provisions will magnify the adverse impact of tax incentives, including the unintended consequences, by potentially cutting off government's ability to correct mistakes and unexpectedly large revenue losses.	
Withholding tax relief on interest and services	Investors may increase the amount of interest expense and charges for administrative services paid to foreign affiliates, usually in low tax jurisdictions.	MEDIUM-HIGH
Cost-based incentives (e.g., accelerated depreciation)	Investors may inflate their capital expenditure (i.e., money spent on assets, building and equipment) above what is needed in order to maximise the tax benefit. This may be in actuality ("gold plating") or merely on paper in related party transactions. Note that investment tax credits are higher risk than other cost-based incentives. If not well designed, such a regime may also encourage companies to export fully depreciated assets to claim further deductions in other mining jurisdictions (i.e., the same asset may cycle through multiple countries).	MEDIUM
Import duty relief	Investors may increase the cost of machinery and equipment purchased from related parties to increase their deductible expenses.	

Table 2: Type of tax incentive and the related behavioural response (sourced from Table 3 Readhead *OECD* 2018)¹⁰⁰

¹⁰⁰ Readhead op cit note 86, 15.

3.1.2.2 The design of incentives/ exemptions

As part of evaluating the effect on behavioural responses, the design of the tax incentive must be considered.¹⁰¹ The following questions can be considered to assess the design of the tax incentive under review:¹⁰²

Table 3: (Adapted from Readhead *OECD* 2018, p 16)¹⁰³

Creation of parallel fiscal regimes	Where incentives are not consistently applied to all segments of the mining value chain, transfer pricing abuse may occur.
Clarity of the applicable tax base	Where the incentive is applied to expenditure clarity with regards to the type of qualifying expenditure, whether losses may be carried forward and offset against income in future assessment years and lastly whether these qualifying expenditures are tax deductible.
Interaction with other tax incentives	A risk exists that the use of multiples tax incentives may increase the revenue lost by the government.
Certainty of the treatment of the tax incentive	Clear parameters and specific applicable dates must be evident from tax legislation to prevent abuse by taxpayers taking advantage of badly designed tax incentives.

3.1.2.3 The Impact on Revenue

Reviewing a tax incentive and its potential cost to the fiscus is essential.¹⁰⁴ This cost analysis should not be linear but holistic, including fiscal and socio-environmental costs.¹⁰⁵

The legislature and policymakers must have complete information to conduct a financial modelling analysis to predict the potential impact of a tax incentive on the fiscus. To protect the fiscus against any gross risk of revenue loss, this model must include a list of assumptions

¹⁰¹ Ibid at 16.

¹⁰² Ibid.

¹⁰³ Ibid.

¹⁰⁴ Ibid.

¹⁰⁵ Ibid at 13.

that could materially affect the conclusions reached and their sensitivity to changes in key inputs (for example, prices).¹⁰⁶

3.2 Illustration of the OECD's criterion and section 37A of the ITA

Section 37A tax exemption can positively and negatively affect taxpayers' behavioural responses.¹⁰⁷ As discussed above, the OECD focuses on the nature, design, and impact on revenue as factors that influence the actions of mining companies and their rehabilitation vehicles.¹⁰⁸

The nature of the exemption determines its scope and purpose, which shapes how taxpayers respond.¹⁰⁹

On the one hand, the tax exemption is directly targeted at rehabilitation and the accumulation of funds exclusively for mine rehabilitation. The limited focus of the exemption could encourage mining companies to allocate adequate funds to their rehabilitation trust and comply properly with their rehabilitation obligations. Because the contributions are tax-deductible, companies are further rewarded and more likely to start contributing earlier and at higher levels.

However, as the exemption does not provide strict timelines, companies may use the tax break to their advantage well beyond the point where rehabilitation is needed, or they may even delay closing their mines.¹¹⁰

As mentioned above, the structure and conditions of the exemption influence whether companies use it appropriately or exploit loopholes.¹¹¹

The Section 37A exemption clearly defines what income is exempt and what rehabilitation trusts can benefit from it.¹¹² Therefore, the exemption design ensures that the funds accrued are directed towards genuine mining rehabilitation in the future.

The financial implications of exemptions from short-term revenue losses and long-term fiscal gains may affect how companies behave.¹¹³

The section 37A exemption will significantly reduce the tax burden of the rehabilitation trust and the mining company due to the income's exempt status and the contributions' deductibility.

¹⁰⁶ Ibid at 17.

¹⁰⁷ Supra note 115, p 14 – 15.

¹⁰⁸ Ibid.

¹⁰⁹ Ibid 16 - 17.

¹¹⁰ Ibid.

¹¹¹ Ibid.

¹¹² Ibid.

¹¹³ Ibid.

Mining companies may then be encouraged to contribute more funds, knowing that the tax burden is neutral or positive.

Generally, tax exemptions create the risk that companies may shift profits into tax-exempt entities to reduce their taxable base elsewhere.¹¹⁴ However, the fact that the mining company will not be entitled to any remaining funds after rehabilitation would deter mining companies from shifting their profits to rehabilitation trusts.¹¹⁵

There is also a risk that companies may prioritise their tax savings and efficiency over meaningful rehabilitation efforts; however, due to the strict nature of the rehabilitation trust, this is a low risk.¹¹⁶

In conclusion, governments can maximise the efficacy of rehabilitation incentives while minimising the risks of abuse or revenue leakage by aligning the nature and design of exemptions with revenue goals and behavioural oversight.

In the context of the tax exemption and deduction provided in section 37A read with section 10(1)(cP) of the ITA, it remains crucial to keep its purpose and limited application in mind. As the exemption is directly linked to a mining right in South Africa, it serves the purpose of encouraging environmental responsibility rather than profit-seeking behaviour. Therefore, the tax exemption under section 37A of the ITA provides a good incentive for driving environmental rehabilitation.

¹¹⁴ Alexander Klemm and Li Liu, 'The Impact of Profit Shifting on Economic Activity and Tax Competition' (2019) WP/19/287 IMF Working Paper, 4.

¹¹⁵ Supra note 80.

¹¹⁶ NEMA Regulations.

4 CHAPTER FOUR: THE ACCOUNTING AND TAX TREATMENT OF REHABILITATION TRUSTS

4.1 Scenario

It is crucial to consider the accounting treatment of rehabilitation funds in the context of rehabilitation trusts as it determines the effective tax rate for Pillar Two purposes, as discussed in Chapter Five below. For illustrative purposes, this chapter will be guided by examples based on the following factual scenario:

The mining right holder contributes R15,000 to the rehabilitation trust, and interest income of R20,000 is earned on accumulated funds of R1 million in the financial year. At the time of this dissertation, the corporate income tax rate in South Africa was 27 percent.¹¹⁷

4.2 The accounting treatment in the financial statements of rehabilitation trusts

Under the interpretation provided by the International Financial Reporting Committee (**IFRIC**) 5¹¹⁸, rehabilitation trusts secure funding for decommissioning, rehabilitation, or restoration by segregating assets (mostly financial instruments) to ensure that future costs can be funded.¹¹⁹

The accounting treatment of contributions received by the rehabilitation trust depends on the nature of the contributions and the terms of the trust deed.¹²⁰

Conditional contributions are subject to specific restrictions on how the rehabilitation trust must use them, and the trust is required to repay any unused contributions.¹²¹ Conversely, unconditional contributions are made free of restrictions, and the rehabilitation trust can use them to fulfil its purpose.¹²²

4.2.1 Conditional contributions

Contributions received by a rehabilitation trust from a mining right holder can be recognised as liabilities if they are subject to conditions that must be fulfilled in the future.¹²³ Another

¹¹⁷ SARS Tax Pocket Guide 2024/25, available at <https://www.treasury.gov.za/documents/national%20budget/2024/sars/Budget%202024%20Tax%20guide.pdf>, accessed on 14 February 2025.

¹¹⁸ The IFRIC is a committee established by the International Accounting Standards Board (“IASB”) to assist with developing interpretations and applications of IFRSs. IFRIC 5 deals with the rights to interests arising from decommissioning, restoration and environmental rehabilitation funds and was published by the IASB in December 2004.

¹¹⁹ IFRIC 5 paragraph 1.

¹²⁰ International Accounting Standard (“IAS”) 37, accessed online at <https://www.ifrs.org/issued-standards/list-of-standards/ias-37-provisions-contingent-liabilities-and-contingent-assets/>, accessed on 14 February 2025.

¹²¹ *Ibid* and IFRS 15, available at <https://www.ifrs.org/issued-standards/list-of-standards/ifrs-15-revenue-from-contracts-with-customers/>, accessed on 14 February 2025.

¹²² *Ibid*.

¹²³ IFRS 9 (Financial Instruments) accessed online on <https://www.ifrs.org/issued-standards/list-of-standards/ifrs-9-financial-instruments/>, on 14 February 2024/5.

scenario is where the contributions are made based on a contractual agreement and will be used as payment for future services.¹²⁴

Conditional contributions are recognised as deferred income (liability) upon receipt in the rehabilitation trust's statement of financial position (“SFP”).¹²⁵ This is because the rehabilitation trust must fulfil the conditions attached to them.¹²⁶ Therefore, the rehabilitation trust remains indebted to the contributor for repayment of the contributions until the obligation has been fulfilled.

Illustrative example 1:

Rehabilitation trust	Dr	Cr
Bank (SFP)	15000	
Deferred Income (SFP)		15000

Where the rehabilitation trust fulfils its obligations and applies, for example, R10,000 of the contributions to its specific purpose, the liability is reduced, and income is recognised in the rehabilitation trust’s statement of profit and loss (“P/L”).¹²⁷

Illustrative example 2:

Rehabilitation trust	Dr	Cr
Rehabilitation Expense (P/L)	10000	
Bank (SFP)		10000
Deferred Income (SFP)	10000	
Income (P/L)		10000

¹²⁴ IFRS 15 (Revenue from Contracts with Customers), accessed online at <https://www.ifrs.org/issued-standards/list-of-standards/ifrs-15-revenue-from-contracts-with-customers/>, accessed on 14 February 2025.

¹²⁵ Ibid, para 22.

¹²⁶ Ibid, and IAS 37 para 14 and 19.

¹²⁷ Ibid para 31.

4.2.2 Unconditional contributions

More commonly, contributions are recognised as revenue in the hands of the rehabilitation trust based on the trust deed prescribed by NEMA.¹²⁸ This is because rehabilitation trusts in South Africa are structured as a fund where money is accumulated to meet future rehabilitation obligations at mine closure.¹²⁹ The rehabilitation trust may only account for these contributions as income where there is no direct obligation of repayment and where it is made for purposes of complying with its future rehabilitation obligations.¹³⁰ As prescribed by NEMA, the rehabilitation trust structure in South Africa does not allow the contributor to be repaid for any contributions made.¹³¹ All contributions must be used to meet future rehabilitation obligations at mine closure.

Since there is no future repayment obligation and the mining right holder, as a contributor, does not impose conditions on the contributions, the rehabilitation trust will record them as income upon receipt.¹³² The rehabilitation trust will record the contribution receipts as a debit amount in its SFP, which provides for a bank increase, and as a credit amount in its P/L, reflecting income received.

Illustrative example 3:

Rehabilitation trust	Dr	Cr
Bank (SFP)	15000	
Contribution Received (Income) (P/L)		15000

4.2.3 Recognition of the investment receipts by the rehabilitation trust

The rehabilitation trust manages and invests the contributions received to accumulate sufficient funds to satisfy its rehabilitation obligation in the future.¹³³

Investment income will accrue on the contributions made by the contributors, such as interest in this scenario. These interest receipts will be recorded as a debit amount in the SFP of the

¹²⁸ Supra note 74.

¹²⁹ Supra note 69.

¹³⁰ Supra note 74.

¹³¹ Supra note 79.

¹³² IAS 1 paragraph 82(a).

¹³³ Supra note 69.

rehabilitation trust, reflecting the increase in bank or cash, and as income, being a credit amount in the P/L of the rehabilitation trust as interest income.¹³⁴

Illustrative example 4:

Rehabilitation trust	Dr	Cr
Bank (SFP)	20000	
Interest Income (P/L)		20000

4.2.4 The accounting treatment by the mining right holder

4.2.4.1 Recognition of the rehabilitation provision

Suppose the mining right holder contributes to a rehabilitation trust as the contributor, as discussed in Chapter Two. In that case, this obligation creates a rehabilitation asset and a corresponding rehabilitation liability for the mining right holder. This dual recognition ensures that the costs of rehabilitation and the benefits of the mining operations are matched.

International Accounting Standard 37¹³⁵ (“**IAS 37**”) states that a provision¹³⁶ is recognised in the mining right holder’s SFP when an obligation exists to perform rehabilitation at a mine’s closure.¹³⁷ In South Africa, the NEMA Regulations must be considered when determining whether such an obligation exists and what it entails.

The closure provision is based on the present value of the expected future cash flows required for decommissioning and rehabilitation.¹³⁸ The rehabilitation provision may be adjusted to reflect any changes in estimations or legislation.¹³⁹

4.2.4.2 Rehabilitation Liability

For liability to be recognised under IAS 37, it must meet the following recognition criteria:¹⁴⁰

- (a) Legislative requirements or industry norms must impose a present obligation;
- (b) It must be probable that there will be an outflow of economic benefits to settle the obligation and

¹³⁴ IFRS 9 paragraph 5.4.1.

¹³⁵ IAS 37 deals with the accounting and disclosure requirements for provisions, contingent liabilities and contingent assets.

¹³⁶ A “provision” in terms of IAS 37 is a “liability of uncertain timing or amount.” The liability may be created either through a legal or constructive obligation. In this case, the provision for rehabilitation funds is a legal obligation.

¹³⁷ Para 14

¹³⁸ IAS 37 para 45.

¹³⁹ IAS 37 para 59.

¹⁴⁰ IAS 37, Paragraph 14.

(c) The cost to fulfil the obligation must be reliably estimated.

The obligation imposed by NEMA on the mining right holder is a present obligation to rehabilitate their mines at closure.¹⁴¹ The rehabilitation trust will use its funds to finance the rehabilitation costs, resulting in an outflow of economic benefits. Lastly, the estimated cost of rehabilitation can be reliably calculated based on industry data and legal prescriptions.

Therefore, the rehabilitation liability will be measured at the present value of the expected future rehabilitation costs and discounted to account for the time value of money and associated risks.

4.2.4.3 Rehabilitation Asset

The rehabilitation asset recognised in the mining right holder's SFP represents the capitalised cost of the rehabilitation obligation. It is part of the mining right holder's property, plant, and equipment.¹⁴² The rehabilitation asset at initial recognition is equal to the rehabilitation liability.

Illustrative example 5:

Mining Right Holder	Dr	Cr
Rehabilitation Asset (SFP)	1000000	
Rehabilitation Liability (SFP)		1000000

4.2.4.4 Recognition of contributions made by the mining right-holder

The contributions are made by the mining right holder's statutory obligation under NEMA.¹⁴³ Therefore, they are mandatory to ensure sufficient funds are available at the time of mine closure.

The mining right holder transfers these funds to the rehabilitation trust without any prospect of repayment in the future. The contributions are thus similar to prepaid expenses to meet its future

¹⁴¹ O Tambo & S Theobald 'Financial Provisioning for Rehabilitation and Mine Closure: A study of South African platinum and coal mining companies' *Intellidex Research Report* (May 2018), available at <https://fulldisclosure.cer.org.za/2018/wp-content/uploads/2018/06/Intellidex-financial-provisioning-for-rehabilitation-and-closure-in-SA-mining.pdf>, accessed on 14 February 2025, p 8.

¹⁴² IAS 16.

¹⁴³ Supra note 71.

rehabilitation obligation.¹⁴⁴ The contributions are, therefore, recognised as restricted assets upon transfer to the rehabilitation trust.¹⁴⁵

As mentioned above, IAS 16 and IAS 37 state that an asset must be recognised when (a) it provides a future economic benefit, (b) there is control over the resources, and (c) the costs thereof can be reliably measured. The contributions will meet the criteria as the contribution is a prepayment to fulfil a future obligation and not an immediate expense. The contributions will allow the mining right holder to meet its rehabilitation obligations as required by NEMA. Secondly, the funds accumulated in the trust may only be used for the rehabilitation activities provided for in the trust deed. Thus, the mining right holder controls the payment of contributions to the rehabilitation trust for future rehabilitation activities. Lastly, the contribution amounts will be known and reliably measured.

Illustrative example 6:

Year 1

Mining Right Holder	Dr	Cr
Rehabilitation Trust Asset (SFP)	15000	
Bank (SFP)		15000

When the rehabilitation funds use these accumulated contributions for the specific rehabilitation purposes provided for in NEMA, the expended costs will be set off against the rehabilitation provision (i.e., the rehabilitation liability).¹⁴⁶ To achieve the set-off, the following journal is needed:

Mining Right Holder	Dr	Cr
Rehabilitation Liability (SFP)	15000	

¹⁴⁴ IAS 1.

¹⁴⁵ IFRS 9 5.1.1.

¹⁴⁶ IAS 37.

Rehabilitation Expense (P/L)		15000
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The principle is that the rehabilitation expense payments made by the trust should, in effect, simply be funding transactions. The P/L expense for the mining right holder is recognised over the life of the mine by amortising the Rehabilitation Asset (separate from the Rehabilitation Trust Asset) that was created initially when the Rehabilitation Liability was recognised. So, when the eventual rehabilitation cost payments are made at the end of the life of the mine, the net impact on the P/L should be zero.

Conceptually, there are two distinct SFP assets:

1. The Rehabilitation Asset is created through a journal upfront (R1 million in Illustrative Example 7). By the end of the mine's life, its value should be amortised to zero. The amortisation expense is recognised in the P/L as a rehabilitation cost to match the mining income over the life of the mine.
2. Secondly, the Rehabilitation Trust Asset starts at zero and then increases in value as the mine regularly contributes to the trust. At the end of the mine's life, the value of the Rehabilitation Trust Asset should be equal to the Rehabilitation Liability, and an equal amount of cash or investments should be held in the trust to fund the Liability. So, instead of the mining company holding cash directly on its SFP to fund the liability, it is held in the Rehabilitation Trust.

One could ask why all the complexity, but the answer is that it ensures that the mining company has the cash to fund the liability. There is a tax incentive of tax-free interest income if it is done via the trust.

4.2.4.5 Consolidation of the rehabilitation trust

Entities that recognise a liability to pay rehabilitation costs and contribute to such rehabilitation entities must determine whether it has control, joint control, or significant influence over the fund and, if so, account for the fund accordingly by applying the relevant accounting standards to determine how the financial results and balance sheet position of the rehabilitation trust should be incorporated into the results of the mining company.¹⁴⁷

¹⁴⁷ PwC 'Financial reporting in the mining industry International Financial Reporting Standards (6 ed) (2012) available at <https://www.pwc.com/id/en/publications/assets/eumpublications/financial-reporting-in-the-mining-industry.pdf>, accessed on 14 February 2025, p 8.

Determining control, joint control, and significant influence are the requirements for determining whether to consolidate the financial results of entities.¹⁴⁸ An entity must present consolidated financial statements when it controls one or more entities.¹⁴⁹

“Control” is determined when an entity has power over another entity, exposure or rights to variable returns, and the ability to influence returns from the other entity.¹⁵⁰ Power in this context emanates from rights, such as voting or contractual rights.¹⁵¹ An entity must be exposed to or have rights to variable returns due to its involvement with the other entity. The entity must also be able to influence these returns through its performance or contributions.¹⁵²

In this regard, the contributor will have the power to appoint the trustees, who will have to act according to the prescripts of the trust deed as provided by NEMA.¹⁵³ In addition, the contributor will be allowed to use the returns generated from the rehabilitation trust for rehabilitation purposes at the closure of its mines. Finally, the contributor can influence these returns as it contributes to the trust, leading to an increased capacity for investment and return within the rehabilitation trust.

Thus, the rehabilitation trust’s financial results will be consolidated with the contributor, the mining company’s financial results.

The following adjustments are required to be made in terms of IFRS 10 upon consolidation:

(a) Elimination of inter-company transactions

The consolidated financial statements remove all transactions between the rehabilitation trust and the mining right holder to avoid double counting. They also eliminate all receipts in the form of contributions to rehabilitation.¹⁵⁴

The contribution made by the mining right holder is an asset in its hands, whereas it is recognised as income in the rehabilitation trust’s hands. To exclude internal financial results, these entries must be eliminated upon consolidation.¹⁵⁵

¹⁴⁸ IFRS 10 para 1.

¹⁴⁹ Ibid.

¹⁵⁰ Ibid para 5-6; 8.

¹⁵¹ Ibid para 11, 14.

¹⁵² Ibid para 15

¹⁵³ Supra note 74.

¹⁵⁴ IFRS 10 para B86.

¹⁵⁵ Ibid.

The inter-company income, the contribution receipt, will be eliminated from the rehabilitation trust, and the contribution paid will be removed from the mining right holder's books.¹⁵⁶

The net effect of the consolidation is that all the Rehabilitation Trust's assets are reflected as assets in the mining company's consolidated SFP, and the Rehabilitation Trust's interest income is reflected as interest income in the mining company's consolidated P/L.

Illustrative example 7:

Group	Dr	Cr
Contribution Income (Rehabilitation Trust)	15000	
Rehabilitation Trust Asset (Mining Right Holder)		15000

(b) Recognition of the rehabilitation trust's income

The interest receipts and expenses of the rehabilitation trusts will be included in the consolidated financial statements.¹⁵⁷

No journal would be required, as the consolidation process will automatically add the interest income. Essentially, the mining right holder's and the rehabilitation trust's P/L and SFP will be added together, meaning the interest income will appear in the consolidated P/L.

(c) Adjustment of the rehabilitation trust's assets and liabilities

Upon consolidation, the mining right holder must bring the assets held by the rehabilitation trust into the group financial statements (SFP) to ensure that the mining group's financials reflect the rehabilitation trust's financial position as part of its financial position.¹⁵⁸

¹⁵⁶ Ibid.

¹⁵⁷ Ibid.

¹⁵⁸ Ibid.

An adjustment ensures that only the net rehabilitation liability is shown on the group financial statements, avoiding inflating the group assets and preventing contributions from being double-counted.¹⁵⁹

If the rehabilitation trust holds cash or investments worth R1,035,000, the mining right holder recognises a rehabilitation trust asset for the same amount. Therefore, to prevent duplication, the intercompany balances must be eliminated.

The rehabilitation trust's cash investments will be brought into the mining group's consolidated financial statements.¹⁶⁰

When the consolidation is done, all the mining company's assets and liabilities, including those held by the rehabilitation trust, are added together. Then, the SFP will show both the cash balances (of the Rehabilitation Trust) and the Rehabilitation Trust Asset (of the mining company). It will also show the Rehabilitation Trust's retained income reserves where it recognised the contribution receipts as income.

So, the consolidation journal that is needed is to eliminate the rehabilitation trust asset (of the mining company) and the retained income reserves of the rehabilitation trust:

	Dr	Cr
Retained Income Reserves (Rehabilitation Trust)	35000	
Rehabilitation Trust Asset (Mining Right Holder)		35000

The journal's effect is that the rehabilitation trust's cash assets are reflected in the consolidated SFP and the group's cash reserves.

4.3 The tax treatment of the rehabilitation trust and mining right-holder

4.3.1 Section 37A of the ITA

Section 37A(1) of the ITA provides for the deduction from a taxpayer's income of any cash paid by that taxpayer to a company or trust if "*the sole object of that company or trust is to*

¹⁵⁹ Ibid.

¹⁶⁰ Ibid.

apply its property solely for rehabilitation upon premature closure, decommissioning, and final closure, and post-closure coverage of any latent and residual environmental impacts on an area" that is covered in terms of certain rights, including a mining right.

For the mining right holder to qualify for the deduction, it must either:

1. Hold a permit or right for prospecting, exploration, mining, or production, as defined in the MPRDA or
2. Be engaged in these activities under such a permit, right, reservation, or permission.¹⁶¹

Further, section 37A(1)(d)(i) of the ITA lists several qualifying requirements that must be met before the deduction may be used.¹⁶²

Therefore, section 37A(1) of the ITA provides a tax benefit to taxpayers directly involved in the extractive industry and legally obliged to make financial provisions for decommissioning rehabilitation.

The receipts and accruals of an approved rehabilitation trust, as contemplated in section 37A to the ITA, are exempt in section 10(1)(c) of the ITA. The rehabilitation trust will, therefore, be exempt from South African income tax on the contributions received from the mining right holder and the interest receipts earned on those contributions. However, the qualifying requirements in section 37A of the ITA must be met to maintain its tax-exempt status.

Consequently, section 37A, read with section 10(1)(c) of the ITA is an income-based tax incentive. Income-based tax incentives are generally related to incentives that reduce the taxpayer's taxable income by providing for full or partial exemptions, tax deductions or the application of reduced tax rates.¹⁶³

¹⁶¹ Section 37A(1)(d) of the ITA.

¹⁶² "(a) *the sole object of that company or trust is to apply its property solely for rehabilitation upon premature closure, decommissioning and final closure, and post-closure coverage of any latent and residual environmental impacts on the area covered in terms of any permit, right, reservation or permission contemplated in paragraph (d) (i) (aa) to restore one or more areas to their natural or predetermined state, or to a land use which conforms to the generally accepted principle of sustainable development;*
 (b) *that company or trust holds assets solely for purposes contemplated in paragraph (a);*
 (c) *that company or trust makes distributions solely for purposes contemplated in paragraph (a), or subsection (3) or (4); and*
 (d) *that person –*
 (i) *(aa) holds a permit or right in respect of prospecting, exploration, mining or production, an old order right or OP26 right as defined in item 1 of Schedule II or any reservation or permission for or right to the use of the surface of land as contemplated in item 9 of Schedule II to the Mineral and Petroleum Resources Development Act; or*
(bb) is engaged in prospecting, exploration, mining or production in terms of any permit, right, reservation or permission as contemplated in item (aa); or
 (ii) *after approval by the Commissioner, paid any cash to that company or trust and that payment was not part of any transaction, operation or scheme designed solely or mainly for purposes of shifting the deduction contemplated in this subsection from another person to that person."*

¹⁶³ V Chand, K Romanovska 'The Impact of Pillar Two on Corporate Tax Incentives and Incentives Post Pillar Two – The Potential Rise of Tax Credits and Subsidies (2023) (Volume 6), No.9 *International Tax Studies* 29.

4.3.2 Tax treatment of the rehabilitation trust

Where the rehabilitation trust recognises the contributions received from the mining right holder as income, and the receipt thereof is exempt under section 10(1)(cP) of the ITA, a permanent difference may arise because of the difference in accounting and tax treatment.

A permanent difference will arise where an item is recognised as income for accounting purposes but not taxed or taxed differently than the regular corporate income tax regime.¹⁶⁴ The contributions will be recognised as income in the financial statements, but no tax will arise because they are tax-exempt in terms of section 10(1)(cP) of the ITA.

4.3.3 Tax treatment of the mining right holder

Under section 37A of the ITA, the mining right holder can deduct the contributions made to the rehabilitation trust from its taxable income.

The tax deduction will reduce the mining right holder's taxable income, providing immediate tax savings. This lower taxable income will result in a lower effective tax rate in the year the contribution was made.

Illustration of tax consequences :

Mining right holder	ZAR	Tax Savings
Contribution	15000	
Section 37A	(15000)	27% x 15,000 = R4050

Rehabilitation trust	ZAR	Tax Savings
Contribution	15000	
Interest Income	20000	
Income before tax	35000	
Section 37A read with section 10(1)(cP)	(35000)	35000 x 27% = 9450

¹⁶⁴ IFRS Foundation 'Income Taxes – Various Accounting Models' (May 2016), available at <https://www.ifrs.org/content/dam/ifrs/meetings/2016/may/iasb/income-taxes/ap19b-appendixa-various-accounting-models.pdf>, accessed 15 February 2025, p 2.

Taxable Income	Nil	
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4.4 Consolidation of the financial statements

The rehabilitation trust's interest income (R20,000) will be included in the accounting profit; however, it will not have a corresponding tax expense because it is tax-exempt in terms of section 10(1)(cP) of the ITA.

The rehabilitation trust's interest income must be included in the mining groups' accounting profit upon consolidation. However, the interest income will not form part of the consolidated taxed income. This creates a permanent difference because the income affects the accounting profit but will never be taxed.

Contributions to the Rehabilitation Trust are deductible and in the hands of the mining right holder. However, the rehabilitation trust's contribution receipts will not be included in the consolidated income as they are eliminated as an inter-company transaction.

Thus, at a consolidated level, the net effect is that the interest income of R20,000 has no income tax expense linked to it because it is exempt income under section 37A to the ITA. The contribution income of R15,000 is eliminated upon consolidation. Thus, its exempt nature in the hands of the rehabilitation trusts is not relevant at the consolidation level. The issue is that the mining company has a tax deduction for the contribution paid (R15,000) to the rehabilitation trust, which is not shown as an expense in the consolidated P/L.

Ultimately, the effective tax rate of the mining company will be lower due to the deduction for tax purposes of the contribution. This then carries forward into the consolidated effective tax rate, which is lower due to a) the tax deduction in the mining company for the contribution that does not appear as an expense in the consolidated PL and b) tax-exempt interest income earned in the trust which forms part of the consolidated PL.

A permanent difference will result in a lower effective tax rate for the group, as it lowers the proportion of accounting profit subject to tax based on IFRS. The effective tax rate is the actual tax expense as a percentage of the accounting profit, calculated by dividing the tax expense by the accounting profit.

4.4.1 An illustrative example of the financial statements and tax adjustments

In summary, and considering the examples above, the illustrative example below provides an exposition of the financial statements of the mining right holder and the rehabilitation trust, respectively. The purpose of the example is to show the reader how the journals discussed above will appear in the financial statements. In particular, it will show the effect of the tax

adjustments on the mining right holder's income before tax, ultimately rendering it an assessed loss.

Illustration of the financial statements and tax adjustments

Mining Right Holder		Rehabilitation Trust	
SFP		SFP	
Opening balance of the Rehabilitation Trust Asset	R1000,000	Opening balance of the fund	R1000,000
Increase in Rehabilitation Trust Asset (i.e. the contribution made and interest earned)	R35,000	Contribution received	R15,000
		Interest received	R20,000
Closing Balance of the Rehabilitation Trust Asset	R1,035,000	Closing Balance	R1,035,000
P/L			
Increase in Rehabilitation Trust Asset	35,000	Contribution received	15,000
Contribution to Rehabilitation Trust	(15,000)	Interest received	20,000
Income Before Tax	R20,000	Income Before Tax	R35,000
Tax Adjustments		Tax Adjustments	
Income Before Tax	R20,000	Income Before Tax	R35,000
Less: Increase in Rehabilitation Asset	(R35,000)	Less: Section 37A exemption	(R35,000)

include in Income Before Tax			
Assessed Loss	(R15,000)	Taxable Income	Rnil
Tax Payable	Rnil	Tax payable	Rnil
ETR	0%	ETR	0%

5 CHAPTER FIVE: A BRIEF OVERVIEW OF THE PILLAR TWO GMT FRAMEWORK

5.1 The Origin of Pillar Two

The Inclusive Framework (“IF”) undertook the BEPS Project to address the tax implications of, among other things, the recent increase in tax competition, which had been a core reason for base erosion and profit-shifting practices.¹⁶⁵ These practices relate to tax planning strategies that multinational enterprises (“MNEs”) use to exploit loopholes in tax rules to artificially shift profits to low—or no-tax locations to avoid paying tax.¹⁶⁶

BEPS Action 1 laid the groundwork for international cooperation between nations to address these concerns.¹⁶⁷ BEPS Action 1 primarily deals with the extensive range of tax challenges that have arisen due to the digitalisation of the economy.¹⁶⁸ As such, the two-pillar approach was first addressed in a policy note issued by the OECD in January 2019.¹⁶⁹ The policy note suggested a “consensus-based approach” based on two fundamental pillars: one addressing the allocation of taxing rights in the digital economy (Pillar One) and the other addressing the other BEPS issues (Pillar Two).¹⁷⁰ This approach advocated a multilateral agreement between members instead of directly enforceable provisions.¹⁷¹

A compromise was finally reached through various public consultations with stakeholders to achieve solutions to the concerns raised in a manner balanced to all stakeholders’ interests. The blueprints for Pillar One and Pillar Two were published in October 2020.¹⁷² These blueprints focused on finding a solution to applying current international tax rules in the context of the new digital global economy.¹⁷³

Pillar Two was a shift in the international tax regime. According to the 2019 OECD Secretariat Programme of Work, a key focus of Pillar Two was to create rules that would allow jurisdictions

¹⁶⁵ OECD ‘Base erosion and profit shifting (BEPS)’ available at <https://www.oecd.org/en/topics/base-erosion-and-profit-shifting-beps.html>, accessed on 11 February 2025.

¹⁶⁶ Ibid.

¹⁶⁷ Ibid.

¹⁶⁸ Deloitte *BEPS Action 1: Addressing the Tax Challenges of the Digital Economy* (Deloitte 2015) available at <https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dtl-tax-uk-beps-action-1.pdf>, accessed on 15 February 2025, p 1 – 2.

¹⁶⁹ F De Lillo ‘Introducing Pillar Two: Towards a Global Minimum Effective Tax Rate’ in A Perdelwitz & A Turina (eds) *Global Minimum taxation? An Analysis of the Global Anti-Base Erosion Initiative* (vol 4) 2021 3 – 4.

¹⁷⁰ OECD ‘Addressing the Tax Challenges of the Digitalisation of the Economy – Policy Note’ *OECD/G20 Inclusive Framework on BEPS* 23 January 2019, available at OECD/G20, Addressing the Tax Challenges of the Digitalisation of the Economy – Policy Note as Approved by the Inclusive Framework on BEPS on 23 January 2019 (OECD 2019), available at <https://www.oecd.org/tax/beps/policy-note-beps-inclusive-framework-addressing-tax-challenges-digitalisation.pdf>, accessed on 11 February 2025.

¹⁷¹ C Remeur ‘Understanding BEPS From tax avoidance to digital tax challenges’ *European Parliament* October 2019, available at [https://www.europarl.europa.eu/RegData/etudes/BRIE/2019/642258/EPRS_BRI\(2019\)642258_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2019/642258/EPRS_BRI(2019)642258_EN.pdf), accessed on 11 February 2025.

¹⁷² B Obuoforibo, A Perdelwitz & A Turina (eds) ‘Global Minimum Taxation? An Analysis of the Global Anti-Base Erosion Initiative’ (2020) *IBFD*, available at https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/collections/gmt/html/gmt_head.html, accessed on 15 February 2025.

¹⁷³ Ibid.

to claw back any taxes not claimed by the primary taxing jurisdictions if such payment of taxes is eradicated by a very low effective tax rate.¹⁷⁴

In October 2021, 135 G20/OECD IF¹⁷⁵ members of BEPS approved and committed to adopting Pillar Two to address the so-called “race to the bottom,” whereby countries shift their profits to low-tax jurisdictions. Pillar Two provides for imposing a global minimum effective tax rate of 15% for MNE Groups meeting the EUR 750 mil threshold (“**in-scope MNEs**”).¹⁷⁶

On 14 December 2021, the IF released the GloBE Rules. About two years later, the IF released further technical guidance (the “**GloBE Administrative Guidance**”) to assist governments with implementing the Global Minimum Tax under GloBE Pillar Two.

Pillar Two has since been widely debated as tax authorities, scholars, and industry practitioners seek to understand the GloBE Rules. Together with the GloBE Commentary, these rules intend to guide legislatures in implementing the GMT in their respective jurisdictions.¹⁷⁷

On 21 February 2024, the South African Treasury published a draft of the Global Minimum Tax Bill and a draft of the Global Minimum Tax Administration Bill for public comment. These Draft Bills set out the implementation of the GloBE Pillar Two in South Africa from 1 January 2024. They provide for the implementation of the Income Inclusion Rule (“**IIR**”) and a Qualifying Domestic Minimum Top-up Tax (“**QDMTT**”) as charging provisions for the imposition of a minimum effective tax rate.

The policy rationale behind Pillar Two

Pillar Two was created to address the BEPS issues not covered by Pillar One.¹⁷⁸ IF members were optimistic about the potential of BEPS Action 1. However, in public consultations, they still needed to be satisfied that it would be comprehensive enough to address profit shifting to the large extent it is currently applied globally.¹⁷⁹

Pillar Two has a dual role: firstly, serving as a means to “provide such a comprehensive multilateral solution to avoid the detrimental effect of uncoordinated, unilateral measures designed both to attract more tax base and to protect the existing tax base, with adverse consequences for all countries, large and small, developed and developing.”¹⁸⁰ Secondly, to

¹⁷⁴ Ibid.

¹⁷⁵ This includes South Africa.

¹⁷⁶ The subject to tax rule will not be addressed in this dissertation.

¹⁷⁷ G Perez-Navarro ‘What does Pillar Two’s Global Minimum Tax Mean for Tax Incentives?’ (2023) *Intertax* Vol 51 (Issue 2) p 100.

¹⁷⁸ UP Rule ‘Tax Challenges Arising from Digitalisation – Report on the Pillar Two Blueprint’ OECD (2020), available at <https://www.oecd.org/tax/beps/tax-challenges-arising-from-digitalisation-report-on-pillar-two-blueprint-abb4c3d1-en.htm>, accessed on 11 February 2025.

¹⁷⁹ Ibid.

¹⁸⁰ A P Dourado ‘The Global Anti-Base Erosion Proposal (GloBE) in Pillar II’ (2020) *Intertax* Vol 48 Issue 2, 152 – 156.

establish a basis for fair tax competition by preventing the “race to the bottom” mentioned previously.¹⁸¹ Pillar Two is therefore seen as a mechanism whereby international tax inequality can be addressed by ensuring global investment attractiveness disassociated from low effective tax rates.¹⁸² The rationale is that by implementing a global minimum tax rate, the marginal benefit of large international operating entities shifting their profits to low-tax jurisdictions is reduced or even nullified.¹⁸³ The incentive created with Pillar Two is to invest where the yield of return before the tax effect is considered the highest, resulting in a more economically stimulating investment motivation.¹⁸⁴

The OECD has also clarified that it seeks to address aggressive tax competition by implementing Pillar Two.¹⁸⁵ The GloBE Rules give each jurisdiction the power to decide how to implement them as part of its tax dispensation.¹⁸⁶ However, despite the OECD’s intention to create legislative freedom, Pillar Two influences how jurisdictions determine their tax rates, especially with added pressure to establish a rate equal to the global minimum rate of 15%.¹⁸⁷

5.2 The applicability of Pillar Two

The GloBE Rules apply to MNE Groups with consolidated revenue of €750 million or more in two of the four fiscal years immediately preceding the fiscal year being tested (the “**GloBE revenue threshold**”).¹⁸⁸

An MNE Group is any group with the required GloBE revenue threshold and at least one entity or permanent establishment outside the jurisdiction of its ultimate parent entity (“**UPE**”).¹⁸⁹

According to the GloBE Rules, a “group” constitutes a “collection of entities” connected to such an extent that its ownership or control of assets, liabilities, expenses, and cash flows are presented in the consolidated financial statements of the UPE (or excluded on materiality grounds) (“**Group**”).¹⁹⁰

Based on the GloBE Commentary, the MNE Group definition performs two key functions.¹⁹¹ It restricts GloBE Pillar Two to Groups with foreign subsidiaries and defines a required degree

¹⁸¹ Obuoforibo op cit note 172, p 3.

¹⁸² Ibid.

¹⁸³ Ibid.

¹⁸⁴ OECD "Tax Challenges Arising from Digitalisation – Economic Impact Assessment" (2020) *OECD Publishing*, available at https://www.oecd.org/content/dam/oecd/en/publications/reports/2020/10/tax-challenges-arising-from-digitalisation-economic-impact-assessment_814ce768/0e3cc2d4-en.pdf, accessed on 15 February 2025, p 143.

¹⁸⁵ Ibid 21.

¹⁸⁶ Dourado op cit note 180.

¹⁸⁷ L de Lima Carvalho ‘GloBE and the Supranational ‘Nudges’ Affecting Domestic Tax Policy’ (2019) *Tax Notes International* 95(5) 421-425.

¹⁸⁸ Article 1.1 to the GloBE Rules.

¹⁸⁹ Article 1.2 to the GloBE Rules.

¹⁹⁰ Article 1.2.2 to the GloBE Rules.

¹⁹¹ OECD GloBE Commentary para 17.

of shared ownership and control for two or more entities to form part of the same Group.¹⁹² The latter function is based on an accounting consolidation test discussed in Chapter 3 above. It hinges on whether the UPE must prepare consolidated financial statements for the group according to the applicable accounting standards, such as IFRS.¹⁹³

The MNE Group definition refers to the UPE as the core of implementing GloBE Pillar Two. The UPE is the top entity in an MNE Group responsible for consolidating the group's financial statements for financial reporting purposes.¹⁹⁴ Identifying the UPE is crucial because it determines which entity within the MNE Group is subject to the various reporting and tax obligations under GloBE Pillar Two.

The criteria for identifying the UPE is primarily based on financial accounting consolidation requirements. The entity considered the UPE must prepare consolidated financial statements following acceptable financial accounting standards.¹⁹⁵ Therefore, an MNE Group must present a degree of shared ownership and control over foreign subsidiaries within the Group.¹⁹⁶

The entities of which a Group consists can take any form of legal personality, not being a natural person or an arrangement such as a partnership or a trust (“**Entity**”).¹⁹⁷ The GloBE Rules, in particular, refer to so-called “constituent entities,” effectively being members of an MNE Group by way of being an Entity included in the Group or a permanent establishment of such an Entity. However, some Entities are expressly excluded from the application of the GloBE Rules, and as a result, their financial results will be excluded from the GloBE calculations.¹⁹⁸ However, their revenue will still be considered for the GloBE revenue threshold test (“**Excluded Entities**”).¹⁹⁹ These Excluded Entities include, among other things, governmental entities, international organisations, non-profit organisations, and pension funds. Income from such cross-border activities need not be subject to the minimum tax (subject to certain restrictions).²⁰⁰

¹⁹² Ibid.

¹⁹³ A Futter ‘A Proposal on How to Implement GloBE Pillar Two in South Africa’ (2024) *Bulletin for International Taxation* 165 166.

¹⁹⁴ Article 1.4 to the GloBE Rules defines an UPE as:

“(a) an Entity that:

i. owns directly or indirectly a Controlling Interest in any other Entity; and
ii. is not owned, with a Controlling Interest, directly or indirectly by another Entity; or

(b) the Main Entity of a Group that is within Article 1.2.3.”

¹⁹⁵ The definition to “acceptable financial accounting reporting standard” in Article 10 to the GloBE Rules expressly includes IFRS.

¹⁹⁶ Supra note 191.

¹⁹⁷ Article 10.1 to the GloBE Rules.

¹⁹⁸ OECD GloBE Commentary para 12.

¹⁹⁹ Article 1.5.1 to the GloBE Rules defines an “Excluded Entity” as an Entity that is –

“(a) a Governmental Entity;
(b) an International Organisation;
(c) a Non-profit Organisation;
(d) a Pension Fund;
(e) an Investment Fund that is an Ultimate Parent Entity; or
(f) a Real Estate Investment Vehicle that is an Ultimate Parent Entity.”

Certain Entities connected to an Excluded Entity will also be regarded as an Excluded Entity as per Article 1.5.2 to the GloBE Rules.

²⁰⁰ GloBE Commentary para 40.

A governmental entity is a so-called “sovereign entity” that would, in the normal course of business, not be liable for tax in the state it governs. According to the GloBE Rules, an Entity will be classified as a “governmental entity” when it complies with the following criteria²⁰¹ –

- (a) *“must be part of or wholly owned by a government (including any political subdivision or local authority thereof);*
- (b) *have the principal purpose of fulfilling a government function or managing or investing that government’s or jurisdiction’s assets and not carry on a trade or business;*
- (c) *be accountable to the government on its overall performance, and provide annual information reporting to the government, and*
- (d) *distribute any earnings to the government and vest its assets in the government upon dissolution.”*

In applying the definition above, a rehabilitation trust would not meet the requirements to be classified as a governmental entity as it is not partially, nor wholly owned by the government as required under subsection (a). The rehabilitation trust still remains owned by the mining right holder.

5.3 The Mechanics of the GloBE Rules

Pillar Two's primary purpose is to impose a global minimum effective tax rate of 15% on in-scope MNE Groups. The GloBE Rules guide how this tax will be calculated and imposed.

After an MNE Group with a GloBE revenue threshold has been identified together with its UPE and Constituent Entities, the next step is to determine the income or loss of each Constituent Entity by the GloBE Rules (the “**GloBE Income / Loss**”). A Constituent Entity’s financial accounting net income or loss will be adjusted according to the GloBE Rules to determine the GloBE Income / Loss for each Constituent Entity.²⁰² These adjustments are made to the net income or loss to eliminate several standard accounting tax differences where such adjustment is justified on policy grounds²⁰³. These adjustments can be broadly divided between permanent and temporary adjustments.²⁰⁴

After the determination of the GloBE Income / Loss of each Constituent Entity, the so-called “covered taxes” of each will be determined (“**Covered Taxes**”).²⁰⁵ Like the GloBE Income /

²⁰¹ Art 10.1 to the GloBE Rules (Defined Terms), p 57.

²⁰² Article 3.1.1 to the GloBE Rules.

²⁰³ Article 3.2 of the GloBE Rules.

²⁰⁴ Supra note 197 and Article 3.1 to 3.5 to the GloBE Rules.

²⁰⁵ Article 4.2 to the GloBE Rules state –

- “(a) Taxes recorded in the financial accounts of a Constituent Entity with respect to its income or profits or its share of the income or profits of a Constituent Entity in which it owns an Ownership Interest;*
- (b) Taxes on distributed profits, deemed profit distributions, and non-business expenses imposed under an Eligible Distribution Tax System;*

Loss determination, adjustments are made to the Covered Taxes of a Constituent Entity. These adjustments are made to accommodate specific timing differences, to allocate Covered taxes between Constituent Entities where required, and to recognise any adjustments after tax filing²⁰⁶ (“**Adjusted Covered Taxes**”).²⁰⁷

The effective tax rate for an MNE is calculated per jurisdiction in which it operates and is equal to the sum of the Adjusted Covered Taxes of each Constituent Entity located in that jurisdiction divided by the net GloBE Income of each Constituent Entity situated in that jurisdiction for the tested fiscal year (“**GloBE ETR**”). Where the GloBE ETR is less than the global minimum tax rate of 15 per cent, the difference is the Top-Up Tax percentage. The Top-Up Tax percentage is then multiplied by the excess profit to arrive at the Top-Up Tax liability amount for the MNE Group (“**Top-Up Tax Liability**”). Excess profits are the net of the GloBE Income per jurisdiction reduced by the GloBE concept of a “substance-based income exclusion” (“**SBIE**”).²⁰⁸ The SBIE aims to exclude any profits from the GloBE tax base that are not generally linked to BEPS.²⁰⁹ The SBIE consists of two categories of carve-outs:

- (a) Eligible payroll costs, which include certain payroll expenses such as salaries, wages, and bonuses; and
- (b) Eligible tangible assets include the value of assets indicative of the business's substantive activities, such as the property, plant, and equipment of the Entity in a jurisdiction.²¹⁰

The election of these two categories assumes that tangible assets and payroll are a good indicator of genuine economic activities.²¹¹ As discussed in Chapter Four above, a rehabilitation asset is not a tangible asset and, therefore, would not fall within the SBIE relief.

After a Top-Up Tax Liability has been calculated, one must also consider the charging provisions of the GloBE Rules. The GloBE rules provide that an MNE's parent or intermediary

(c) Taxes imposed in lieu of a generally applicable corporate income tax; and

(d) Taxes levied by reference to retained earnings and corporate equity, including a Tax on multiple components based on income and equity.”

Covered Taxes does not include any amount of:

“(a) Top-up Tax accrued by a Parent Entity under a Qualified IIR;

(b) Top-up Tax accrued by a Constituent Entity under a Qualified Domestic Minimum Top-Up Tax;

(c) Taxes attributable to an adjustment made by a Constituent Entity as a result of the application of a Qualified UTPR;

(d) A Disqualified Refundable Imputation Tax;

(e) Taxes paid by an insurance company in respect of returns to policyholders.”

²⁰⁶ Article 4.6 to the GloBE Rules.

²⁰⁷ Article 4.3, 4.4 to 4.5 of the GloBE Rules.

²⁰⁸ Article 5.3.1 to the GloBE Rules.

²⁰⁹ Article 5.3 deals with the SBIE which effectively reduces the excess profits of a Constituent Entity with 5% of the sum of the “eligible payroll costs” and the “eligible tangible assets” for each Constituent Entity, excluding constituent entities that are investment entities, in that country.

²¹⁰ Article 5.3.3 and 5.3.4 to the GloBE Rules.

²¹¹ L Hadnum ‘Takeaways from Yesterday’s OECD Report on Tax Incentives & Pillar Two’ (2022) *OECD Pillars in association with Orbitax*, available at <https://oecdpillars.com/takeaways-from-yesterday-oecd-report-on-tax-incentives-pillar-2/>, accessed on 11 February 2025.

country has the priority right to apply the top-up tax on undertaxed income using the IIR.²¹² The IIR allows the jurisdiction where the UPE is located to collect the Top-Up Taxes arising from implementing Pillar Two in all jurisdictions except those that provide for a QDMTT. Under the IIR, the GMT is paid at the UPE level in proportion to its ownership interest. Where the UPE jurisdiction does not provide for the application of the IIR, the intermediate parent entity may apply the IIR.²¹³

However, the QDMTT is prioritised over the IIR.²¹⁴ Hence, a source country with a QDMTT becomes the first to receive any top-up revenue from Entities in that country. Where a country is liable for paying Top-Up Taxes and its legislation makes provision for the QDMTT, no other jurisdiction may have the right to add additional Top-Up Taxes on the income earned in that jurisdiction.²¹⁵

Illustrative example 8:

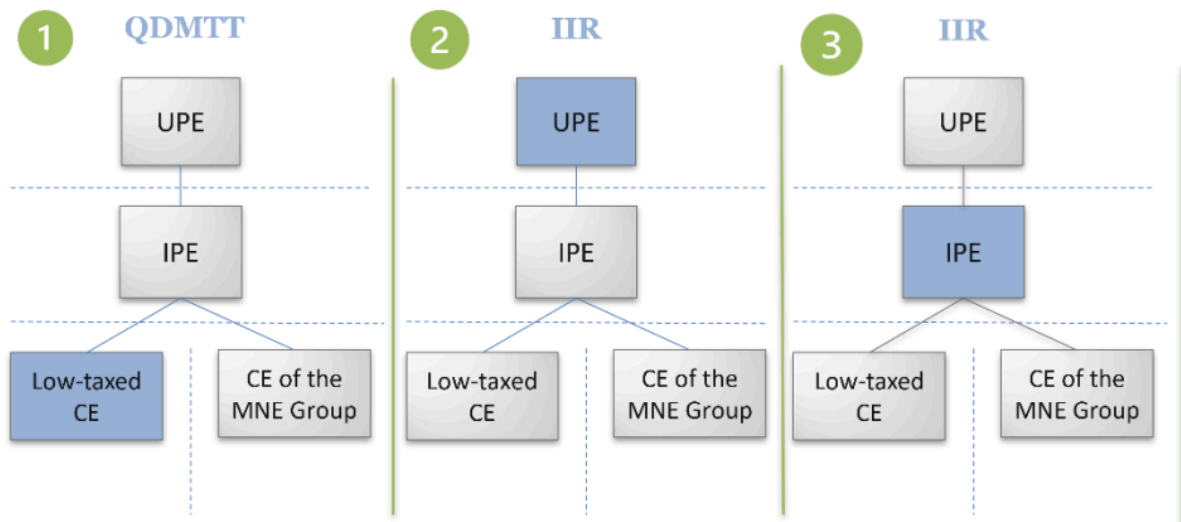


Figure 1.8 Agreed Rule Order (obtained from OECD Minimum Tax Implementation (Pillar Two) 2023).²¹⁶

As shown in the above diagram, the low-taxed jurisdiction has the primary right to collect top-up tax under the QDMTT (refer to column one). If the low-taxed jurisdiction does not have a QDMTT, the jurisdiction where the UPE is located can apply the IIR regarding the income of the low-taxed Constituent Entity (refer to column two). Suppose the UPE is situated in a

²¹² The intermediary country refers to the country where the intermediate parent entity is located, being a Constituent Entity other than the UPE, a PE or investment entity that owns an ownership interest in another Constituent Entity in the same MNE Group.

²¹³ OECD 'Minimum tax Implementation Handbook (Pillar Two)' OECD/ G20 Base Erosion and Profit Shifting Project (2023) available at <https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/global-minimum-tax/minimum-tax-implementation-handbook-pillar-two.pdf>, accessed on 11 February 2025 at para 47.

²¹⁴ Ibid para 14.

²¹⁵ Ibid.

²¹⁶ Ibid para 50.

jurisdiction that has not implemented a Qualified IIR (being an IIR consistent with the GloBE Rules). In that case, the top-up tax will be levied on the following entity in the ownership chain located in a jurisdiction with an IIR following a top-down approach (i.e. intermediate parent entity) (refer to column 3).²¹⁷

5.4 South African legislation imposing a GMT

The GMT Act takes an ambulatory approach, incorporating the GloBE Rules by reference subject to parliamentary oversight.²¹⁸ This would entail parliament reconsidering and approving any subsequent changes made to the GloBE Rules annually by the South African legislative process.

5.5 GloBE ETR calculation for rehabilitation trusts and mining groups in South Africa

As illustrated in Chapter Three, the difference in rehabilitation trusts' accounting and tax treatment could permanently affect the mining group's consolidated financial statements. This difference may result in a lower effective tax rate than the usual corporate income tax rate of 27% for the mining group.

Chapter Four discussed the calculation of the GloBE ETR with the other relevant components of GloBE Pillar Two. The impact of this calculation must be examined against the accounting and tax treatment of the rehabilitation trust and mining right holders. The intention is to determine whether mining right holders will be at risk of showing an ETR below 15% due to the tax treatment of a rehabilitation trust's contribution and income receipts and the deduction afforded to the mining right holder.

As discussed in Chapter Three, IFRS 10 requires the mining company to incorporate the rehabilitation trust's financial results and balance sheet position into its results. These results will be included in the consolidated financial statements of the reporting parent mining company.

From a GloBE Pillar Two context, the rehabilitation trust will be regarded as a Constituent Entity of the mining right holder due to the control of the mining right holder and the fact that its financial results form part of the consolidated financial statements of the mining group. Regarding the GloBE Rules, a Constituent Entity's financial results must be included in the GloBE Income of the reporting parent Entity. The receipts and accruals of the rehabilitation trust will be included in the GloBE Income of the reporting parent Entity. However, due to the tax deduction granted under section 37A read with section 10(1)(cP) to the ITA as discussed in

²¹⁷ Ibid para 50 and 51.

²¹⁸ Section 23 of the GMT Act.

Chapter Four above, no related tax expense will be included in its Covered Taxes for purposes of the ETR calculation.

Depending on the scale of the annual contributions made to the rehabilitation trust and the scale of the return (for example, the interest earned), the mining company may show a GloBE ETR lower than 15%. To illustrate this, it will be helpful to determine the percentage of the GloBE Income that the mining company can afford to spend on its contributions to the rehabilitation trust and the required return earned by the rehabilitation trust before its GloBE ETR drops below 15%.

For purposes of the illustrative examples below, the SBIE and capital allowances are not considered.

Illustrative example 9:

	Calculation	Amount
GloBE Income		R100,000
GloBE ETR threshold	15% x R100,000	R15,000
Implied South African taxable income	R15,000/27%	R55,556
Difference before the GloBE ETR is triggered (i.e. <15%)	R55,556 – R15,000;	R44,444
This means that the mining company can afford to make contributions and earn tax free interest up to 44.4% of its GloBE Income before the 15% ETR is breached.	$(R44,444/R100,000) \times 100$	44,44%

Illustrative example 10:

Building from illustrative example 14, however, the GloBE income is now changed to R105,000 for purposes of illustrating the calculation of a Top-Up Tax,

The GloBE Income will be calculated as follows:

	Amount	Reason
Mining operating income (before contribution, as the contribution is not deductible under GloBE)	R54,444	Pre-contribution income, no deduction for contributions under GloBE.
Rehabilitation Trust interest income	R50,556	Fully included in GloBE income as it reflects economic profit.
Total GloBE Income	R105,000	Consolidated income includes adjustments for Pillar Two rules.

The Covered Taxes will be calculated as follows:

	Amount	Reason
Tax on mining company operating income	27% x R54,444 = R14,700	27% of R54,444 local taxable income after deducting contribution.
Tax on Rehabilitation Trust interest income	Rnil	Exempt under local law, no tax paid.
Total Covered Taxes	R14,700	Consolidated tax reflects only mining company's liability.

The GloBE ETR will, therefore, be:

$$\frac{\text{Total Covered Taxes}}{\text{Total GloBE Income}} \times 100$$

$$= \frac{R14,700}{R105,000} \times 100$$

$$= 14\%$$

Resultantly, the Top-Up Tax will therefore be: (15%-14%) x R105,000 = R1,050

5.6 Conclusion

In conclusion, the rehabilitation trust's financial results must be included in calculating the South African GloBE Income and Covered Taxes of the mining group. However, because of section 37A and section 10(1)(cP) of the ITA the tax that would otherwise have been levied on the receipts and accruals of the rehabilitation trust will not be included as Covered Taxes resulting in a high risk that the mining group in South Africa will show a GloBE ETR of below 15% as a result.

6 CHAPTER SIX: AN INTERNATIONAL PERSPECTIVE

6.1 Australia and Canada

Australia and Canada are among the world's top mining countries due to their abundant natural resources, advanced mining industries, and favourable economic and political conditions.²¹⁹ Australia boasts vast reserves of minerals such as iron ore, coal, gold, and bauxite, which form the backbone of its mining industry.²²⁰ Additionally, the country invests heavily in advanced technology and sustainable mining practices, aligning with global efforts to reduce carbon emissions while fostering economic growth.²²¹ Canadian mining companies also have a significant international presence, particularly in Latin America and Africa.²²² Both countries balance environmental responsibility with economic development, cementing their roles as global leaders in mining.

In recent years, Australia and Canada have adopted legislation regarding the requirements for safe mine closure in conjunction with their mining and environmental laws.²²³ This chapter will examine the rehabilitation of mine laws in Australia and Canada.

6.2 Australia

6.2.1 Australian Mining Rehabilitation Legislation and Policy

In Australia, lawful mine closure requires the mining company to show that it has established criteria to meet the closure objectives presented in its decommissioning plans.²²⁴ There is no fixed list of criteria. However, it must include key performance indicators, trends, and estimations of the long-term impact of the mine's closure.²²⁵ In addition, mining companies operating in Australia must make financial provisions for closure to accumulate sufficient funds

²¹⁹ Canada and Australia: Driving Global Mining Excellence" (2023) *Mining Weekly*, available at <https://www.miningweekly.com/article/canada-and-australia-driving-global-mining-excellence-2023-07-14>, accessed on 15 February 2025.

²²⁰ Geoscience Australia "Australian Mineral Facts" Geoscience Australia, available at <https://www.ga.gov.au/education/minerals-energy/australian-mineral-facts>, accessed on 15 February 2025.

²²¹ Minetek "Australia's Mining Industry Trends in 2024 and Beyond" (2024) *Minetek*, available at <https://minetek.com/en-au/resource-hub/news/2024-mining-industry-trends/>, accessed 15 February 2025.

²²² CERLAC "Report on Canadian Mining: Social and Environmental Impacts" (May 2002), available at: https://www.miningwatch.ca/sites/default/files/CERLAC_mining_report.pdf, accessed on 15 February 2025, p 7.

²²³ A L Clark, J C Clark 'An international overview of legal frameworks for mine closure' 19 July 2021 *Eugene: Environmental Law Alliance Worldwide*; available at <http://www.elaw.org/node/3715>, accessed on 11 February 2025.

²²⁴ Department of Mines, Industry Regulation and Safety (Western Australia) "Mine Closure Plan Guidance How to Prepare in Accordance with Part 1 of the Statutory Guidelines for Mine Closure Plans" (2023), available at: <https://www.dmp.wa.gov.au/Documents/Environment/REC-EC-112D.pdf>, accessed on 15 February 2025, p 5.

²²⁵ *Ibid* p 15.

to rehabilitate the area and reduce the mine's lasting environmental and social impact.²²⁶

Also, Australia established the National Mining Rehabilitation Fund by enacting the Mining Rehabilitation Fund Act in 2012. This national fund serves as a means for the Australian government to secure the necessary funds to rehabilitate abandoned mines and recover the surrounding environment to a healthy and safe state.²²⁷ Mining right holders (tenement holders) contribute to the funds by paying levies, which are calculated based on the Mining Rehabilitation Fund Regulations of 2013.²²⁸ These national funds are colloquially referred to as ‘super funds’ in the mining industry, which exist in conjunction with the financial provision accounts held by mining companies.²²⁹

In addition, the Australian government requires the tenement holders to set aside rehabilitation funds in specific corporate accounts, which are explicitly ring-fenced to cover mine closure costs (known as environmental rehabilitation trusts).²³⁰ The environmental rehabilitation trust must be approved and recognised solely for rehabilitation purposes.

Tenement holders' contributions are deductible under Division 30 of the Income Tax Assessment Act, 1997 (“ITAA”). The environmental rehabilitation trust's income receipts are taxable at lower rates, unlike those of South Africa, where they are tax-exempt.²³¹

6.2.2 Pillar Two Impact

The effect of reduced tax rates on rehabilitation trusts under the OECD GloBE Pillar Two framework primarily may impact the Covered Taxes amount included in the jurisdiction's GloBE ETR calculation.²³² As discussed in Chapter Five, the Covered Taxes are the taxes paid on GloBE Income. If rehabilitation trusts are subject to a reduced rate, the taxes paid by the rehabilitation trust on its taxable income would be lower. Therefore, due to the tax expense payable being lowered, the Covered Taxes in the jurisdiction would also be lower as a result. Since Covered Taxes are the numerator in the GloBE ETR calculation, a lower Covered Tax amount would naturally lower the ETR.

²²⁶ C Miller ‘Financial assurance for mine closure and reclamation: A study prepared for the International Council on Mining and Metals’ 19 July 2021 *London: International Council on Mining and Metals*, available at <https://extractiveshub.org/>, accessed on 11 February 2025.

²²⁷ B White, G J Doole, D J Pannell, V Florec ‘Optimal environmental policy design for mine rehabilitation and pollution with a risk of non-compliance owing to firm insolvency’ (2012) 56 *Aust J Agric Res Econ.* 280–301.

²²⁸ Department of Energy, Mines, Industry Regulation and Safety ‘About the MRF’ available at https://www.dmp.wa.gov.au/Environment/What-is-the-MRD-19522.12px#:~:text=Money%20in%20the%20fund%20is,environmental%20and%20community%20safety%20community_ accessed on 11 February 2025.

²²⁹ Department of Minerals and Energy. Minerals and Petroleum Resources Development Act (1999), 448 Government Gazette No. 23922.

²³⁰ Department for Energy and Mining (South Australia) “Mine Rehabilitation and Closure” (2022), available at <https://www.energymining.sa.gov.au/industry/minerals-and-mining/mining/regulating-mining-activity/mineral-resources-regulation-reports/Annual-mineral-resources-regulation-report-1-July-2021-to-30-June-2022/mine-rehabilitation-and-closure>, accessed on 15 February 2025.

²³¹ PwC Australia - Corporate: Other Taxes available at <https://taxsummaries.pwc.com/australia/corporate/other-taxes>, accessed on 16 February 2025.

²³² Navarro op cit note 177.

Reduced tax rates for rehabilitation trusts may lower a jurisdiction's ETR under Pillar Two. A Top-up Tax may be triggered if the combined ETR falls below 15%, undermining the reduced rate's intended benefits and transferring tax revenue to other jurisdictions.

6.3 Canada

6.3.1 Canadian Mining Rehabilitation Legislation and Policy

The Canadian government²³³ and the provinces regulate the state's environmental and mining laws. Federal law, however, supersedes local municipal laws in conflict situations, much like our Constitution and national laws in South Africa.²³⁴

From a financial provisioning perspective, the Canadian *Mines Act* also requires mining right holders to accumulate funds for post-closure rehabilitation costs (mine reclamation trusts).²³⁵ The Chief Inspector of Mines must approve the vehicle used to collect these funds: "cash certified cheques, bank drafts, term deposits, government bonds and irrevocable standby letters of credit."²³⁶

Contributions to mine reclamation trusts are deductible under section 20(1)(ss) of the Income Tax Act, RSC 1985, c 1 (5th Supp) ("**Canadian ITA**"). However, Mining Reclamation Trusts are recognised under the Canadian ITA as so-called "Qualifying Environmental Trusts" ("**QETs**").²³⁷ The QET income tax rate equals the federal corporate tax rate minus the general rate reduction and the percentage deduction under subsection 124(1) of the Canadian ITA. Effectively, the income earned by the QET will be taxed at a rate lower than the general corporate tax rate of 26.5%.²³⁸

6.3.2 Pillar Two Impact

Canada would be similarly impacted under the OECD GloBE Pillar Two rules as Australia as they also provide for reduced tax rates.²³⁹ Thus, the rehabilitation trusts are taxed at a lower rate, decreasing Covered Taxes for GloBE purposes. The same principle as illustrated in Illustrative Example 16 would apply.

²³³ Being the federal government.

²³⁴ Z Faizuldayeva 'A comparative study of regulatory approaches to mine closure with a special emphasis on the current situation in the former Soviet Union' (2016) *SRK Consulting* available at http://dxi97tvbmhbca.cloudfront.net/upload/user/image/AComparativeStudyofRegulatoryApproachestoMineClosure_2016_020191128181753026.pdf accessed on 11 February 2025.

²³⁵ Section 248(1) of the Canadian Income Tax Act.

²³⁶ Faizuldayeva op cit note 265.

²³⁷ Section 211.6(1) of Part XII.4 of the Canadian ITA.

²³⁸ <https://laws-lois.justice.gc.ca/eng/acts/l-3.3/section-211.6.html?>

²³⁹ *Ibid.*

Reduced tax rates for rehabilitation vehicles in Canada can lower the jurisdiction's ETR under the GloBE framework, potentially triggering top-up taxes.²⁴⁰ These taxes could shift Canadian tax revenue to foreign jurisdictions, undermining the benefits of the reduced rates.

6.4 Conclusion

The abovementioned jurisdictions have many similarities and differences regarding mine rehabilitation. In Australia, mining companies must also present mining closure plans for approval and set aside funds for mine closure. However, Australia has the Mining Rehabilitation Fund as an extra aid for rehabilitation costs.²⁴¹ Canada similarly requires the approval of a mine closure plan and an impact management plan. In addition, Canada needs funds to be set aside²⁴², as equally imposed by both South Africa and Australia.²⁴³

Outside of the Pillar Two context, South Africa's Section 37A rehabilitation trust structure appears to be more favourable to mining companies than the systems in Australia and Canada because under Section 10(1)(cP), receipts and accruals in the trust are entirely exempt from tax.

Although contributions are deductible and withdrawals are tax-free for rehabilitation purposes in Australia and Canada, the income of the trust remains subject to tax (albeit at concessional or lower rates). Thus, some taxes remain attributable to income as opposed to the position in South Africa where none of the rehabilitation trust's income is taxable. Resultantly, the risk of showing a GloBE ETR of below 15% is lower in these countries than in South Africa.

However, reducing tax rates would also result in a lower GloBE ETR when considering Pillar Two. Reduced tax rates also generally create permanent differences when income or expenses are never fully taxed or deducted at the standard rate, as in Australia and Canada.

Thus, although other countries may not exempt the income and receipts of rehabilitation trusts, even the application of reduced tax rates may impact the GloBE ETR of the mining companies.

²⁴⁰ Ibid.

²⁴¹ Western Australia, Department of Mines and Petroleum 'The Mining Rehabilitation Fund – The First Two Years' (2015), available at https://www.dmp.wa.gov.au/Documents/Environment/MRF_The_First_Two_Years.pdf, accessed on 15 February 2025, p 2.

²⁴² Castrilli J. Report on the legislative, regulatory and policy framework. Respecting collaboration, liability and funding measures in relation to orphaned/abandoned, contaminated, and operating mines in Canada [homepage on the Internet]. Prepared for the National Orphaned/Abandoned Mines Initiative; 2007 [cited 2018 Dec 17]. Available from: http://www.abandoned-mines.org/pdfs/Jurisdictional_LegislativeReview.pdf

²⁴³ Mbalenhle Mpanza, Elhadi Adam, Raesa Moolla 'A critical review of the impact of South Africa's mine closure policy and the winding-up process of mining companies' (2021) 17(1) *J transdiscipl res S Afr*: 985 at 21.

7 CHAPTER SEVEN: REVIEWING TAX INCENTIVES IN THE AGE OF PILLAR TWO

7.1 Application of the OECD Criteria

To determine whether the “Top-Up Tax risk” identified in Chapter Four will undermine the rationale of the tax incentive provided for under section 37A read with section 10(1)(cP), it is helpful to consider the criteria discussed in Chapter Three above. This criterion can test whether the combined tax incentive remains effective and efficient despite the imposition of Pillar Two measures. In addition, it is also required to evaluate the potential behavioural responses by investors (or contributors in this case) and the possible unintended revenue losses, whether on a broader governmental level or within the company.²⁴⁴

7.1.1 Efficiency and Efficacy

As discussed in Chapter Four, sections 37A and 10(1)(cP) of the ITA is not a tax incentive provided for purposes of encouraging international investment to the mining sector, but rather a socio-economic and environmental tax incentive aimed at ensuring the constitutional right to health and wellbeing to the communities and promoting environmental sustainability and safety. Thus, the tax incentive encourages mining groups to use these vehicles for their mining closure financial provisioning.

Considering the implementation of Pillar Two measures through the introduction of the GMT Act in South Africa, the tax incentive will be less effective as mining companies could be less inclined to use this vehicle for their rehabilitation obligations if they have Top Up Tax liability.

Like efficacy, the tax incentive in section 37A of the ITA must remain efficient despite imposing Pillar Two measures. Efficiency relates to the cost of meeting the policy objective of the relevant tax incentive.²⁴⁵ This involves testing whether the policy objective can be met at a lower price in other ways.²⁴⁶ Some factors considered when evaluating the efficiency of section 37A in a Pillar Two context are:²⁴⁷

1. Whether the investment (or contribution) would not have been made if the incentive existed.
2. Whether the government costs and resultant revenue losses are low.
3. Whether the administration costs of the incentive are low.

When evaluating effectiveness and efficiency, a cost-benefit analysis regarding section 37A of the ITA must be performed, considering the imposition of Pillar Two measures. The comparison

²⁴⁴ Supra note 86 p 11.

²⁴⁵ Ibid p12

²⁴⁶ Ibid.

²⁴⁷ Ibid.

helps identify whether the envisaged benefits of section 37A and Pillar Two will still be more than the costs.²⁴⁸

As mentioned in Chapter Three, tax incentives are instruments to promote foreign direct investment and encourage companies to contribute to environmental sustainability and community upliftment.²⁴⁹

In the context of the discussions in Chapters Three and Four, it is evident that section 37A and section 10(1)(cP) of the ITA are structured as a tax incentive to motivate mining groups to use rehabilitation trusts to meet their financial provisioning obligations under NEMA. Therefore, considering the impact of implementing Pillar Two measures, the following cost-benefit analysis is drawn up in Table 3 below.

Table 3: Costs and benefits analysis of the tax incentives provided to rehabilitation trusts in a Pillar Two context

Costs	Benefits
<ul style="list-style-type: none"> - Immediate revenue loss - Administration costs - Potential Top-Up Tax 	<ul style="list-style-type: none"> - Increased control over the workings of a rehabilitation trusts due to strict requirements - Certainty regarding the security of the accumulated funds for purposes of rehabilitation - Environmental sustainability - Community safety

7.1.2 Potential behavioural responses to the use of rehabilitation trust in light of the implementation of Pillar Two measures in South Africa

The second inquiry involves determining the likelihood of mining groups changing their behaviour or view of the tax incentive provided in sections 37A and 10(1)(cP) to the ITA and using a rehabilitation trust as a rehabilitation vehicle.²⁵⁰ The impact of these behavioural responses must also be considered in light of the government's potential fiscal revenues and mining rehabilitation enforcement.

²⁴⁸ Ibid p 13.

²⁴⁹ Ibid p 14

²⁵⁰ Ibid.

All three factors, namely (1) the nature of the incentive, (2) the design of the incentive, and (3) the potential revenue impact on the government and taxpayers, must be considered in light of the impact of implement the Pillar Two measures.

The nature of incentives/ exemptionsAs discussed in Chapter Four, the nature of a tax incentive describes its fundamental characteristics and purpose. The focus is on the type or form of the incentive, leading to answering the question of what specific tax is being reduced, exempted, or deferred.²⁵¹

Different tax incentives exist, such as tax exemptions, reduced tax rates or deferred tax incentives. The tax incentive provided under section 37A and 10(1)(cP) of the ITA provides for an exemption of income and accruals of the rehabilitation trusts, ultimately lowering its taxable income. Section 37A of the ITA is an income-based tax incentive. Income-based tax incentives are prone to being impacted by the GloBE Framework.²⁵² As discussed in Chapter Four, the ETR is calculated based on a ‘common taxable base,’ being the GloBE income/loss.²⁵³ Thus, where an incentive lowers the taxable base, the ETR would naturally decrease, leading to an increased risk of a GloBE ETR below 15 percent.

The nominal tax rate starts with taxable income (as it results from applying tax rules) and is, therefore, not influenced by tax incentives other than rate reductions. Using the income recorded in the financial accounts, the GloBE Income / Loss ensures that all tax incentives granted by a jurisdiction are reflected in the ETR.

Thus, given the above, income-based tax incentives are less effective in encouraging or motivating mining groups to use rehabilitation trusts as their rehabilitation provisioning vehicle due to implementing a minimum ETR. The use of rehabilitation trusts, therefore, becomes inefficient from a tax perspective as it may result in Top-Up Taxes being payable, which is counterintuitive to the tax incentive provided under section 37A and 10(1)(cP) to the ITA²⁵⁴

Overall, the Pillar Two project makes it unappealing for countries to offer such income-based tax incentives to large MNEs as it will impact the ETR calculation.²⁵⁵

²⁵¹ Supra note 86, p 16.

²⁵² Ibid p 29.

²⁵³ N Bammens, D Bettens ‘The Potential Impact of Pillar Two on Tax Incentives’ (2023) Intertax Vol 51 (Issue 2) 155 159.

²⁵⁴ Supra note 86 p 7.

²⁵⁵ Ibid p 29.

7.1.2.1 The design of incentives/ exemptions

The design focuses on how the incentive is implemented and structured. It requires looking at the specific rules, mechanisms, and conditions under which the incentive operates to ensure its effectiveness and minimise misuse.

The tax incentive under sections 37A and 10(1)(cP) of the ITA is designed to interact with the financial provisioning provisions in NEMA. These sections do not operate in isolation but with other mining and environmental legislation, which sets out the requirements for creating valid rehabilitation trusts.

In this regard, it is essential to look back at Chapter Two, where the various allowable rehabilitation vehicles are listed. This illustrates that rehabilitation trusts are not the only means of financial provisioning for mining groups and that other vehicles, such as guarantees and insurance policies, may also be used. However, the key distinction between rehabilitation trusts and the other vehicles is that only rehabilitation trusts are afforded income tax exemptions in the ITA, rendering them more attractive to mining groups.

Thus, Pillar Two poses the risk that alternative options of rehabilitation funding may be selected. However, this would not prevent or demotivate mining groups from providing for their rehabilitation obligations at decommissioning; instead, it would force them to use other vehicles as prescribed by NEMA.

7.1.2.2 The Impact on Government Revenue

The tax incentive rehabilitation trusts are based on incentivising socio-economic and environmental benefits. Thus, despite the fiscal cost of revenue that could have been collected through contribution and interest receipts, the rationale of environmental and social sustainability is more important.²⁵⁶

However, due to the effect of GloBE Pillar Two on the overall tax position of mining groups with rehabilitation trusts, the efficacy of the tax incentive provided under section 37A and 10(1)(cP) of the ITA is foregone due to the Top-up Tax risk which may result under the GloBE Rules.²⁵⁷ In essence, mining companies would not be incentivised to use rehabilitation trusts as their rehabilitation vehicles of choice. This will tax the accruals and receipts of rehabilitation funds in other rehabilitation vehicles, ultimately increasing government revenue. However, despite the tax revenues foregone when section 37A of the ITA is used to exempt the income

²⁵⁶ Supra note 193 p 167.

²⁵⁷ Ibid.

and accruals of a rehabilitation trust, Pillar Two now presents the opportunity for the government to receive some tax revenue in the form of Top-Up Taxes being payable.

8 CHAPTER EIGHT: CONCLUSIONS AND RECOMMENDATION

8.1 Conclusions

Under NEMA, mining groups in South Africa with mining rights must make financial provisions for their rehabilitation costs at mine closure. One allowable rehabilitation vehicle is a rehabilitation trust. The rehabilitation trust is also the only rehabilitation vehicle granted a tax exemption for contributions and related interest receipts in terms of the ITA.

Pillar Two measures were introduced in South Africa through the publication of the GMT Legislation. Pillar Two provides for the jurisdictional calculation of an ETR based on GloBE Income / Loss. A Top-Up Tax liability will arise if the ETR is below a minimum of 15%.

This dissertation explores whether the imposition of Pillar Two measures in South Africa will render the use of rehabilitation trusts as a financial provisioning vehicle in terms of NEMA and the MPRDA less attractive due to the interaction between the tax incentive granted under section 37A and 10(1)(cP) of the ITA and the calculation of the ETR under the GloBE Rules.

By analysing the effect of the GloBE Rules through a hypothetical comparison of the effective tax rate of a fictitious mining group before and after the application of the GloBE Rules, it is found that the GloBE Rules would render section 37A and 10(1)(cP) to the ITA inefficient and ineffective in reaching the policy rationale of motivating rehabilitation and whether there would be any resultant behaviour changes from taxpayers to conclude as to what impact Pillar Two will have on financial provisioning for mining rehabilitation.

The key findings of this dissertation are set out as follows;

- (i) South Africa has sufficient legislation dealing with the rehabilitation of mines, particularly requiring mining right holders to make financial provisions for rehabilitating mines upon closure. Other countries, such as Australia and Canada, require financial provisioning to rehabilitate mines. The MPRDA provides for five allowable financial vehicles to accumulate rehabilitation funds. Only rehabilitation trusts are afforded a tax benefit in the ITA for deducting their contribution receipts and an exemption of their interest income. The rationale of the tax incentive is to align tax policy with environmental regulation.²⁵⁸ The tax incentive is provisional upon many strict requirements, and high penalties are imposed for transgression.
- (ii) Chapter Four discussed that IFRS requires consolidating the rehabilitation trusts' financial results and balance sheet position with the mining company when it prepares its consolidated financial statements. Upon consolidation, a permanent

²⁵⁸ Supra note 86 p 3.

- difference arises due to the tax deduction of the contributions and the tax exemption of the interest receipts in terms of section 37A (1) and section 10(1) (cP) of the ITA.
- (iii) The rehabilitation trust will be a Constituent Entity when applying the GloBE Rules to the mining group. Its financial results must be included in calculating the South African GloBE Income and Covered Taxes. The result is that the tax supposed to be levied on the receipts and accruals of the rehabilitation trust will not be included as Covered Taxes due to section 37A and section 10(1)(cP) to the ITA. There is a high risk that the mining group in South Africa will show a GloBE ETR of below 15% as a result.²⁵⁹
 - (iv) Chapter Six explored whether the combined tax incentive in section 37A and 10(1)(cP) to the ITA will remain effective and efficient despite implementing Pillar Two measures in South Africa. Effectiveness is measured against whether the policy objective is met. Section 37A and 10(1)(cP) of the ITA, which aims to ensure the communities' constitutional right to health and wellbeing and promote environmental sustainability and safety. Due to the implementation of Pillar Two measures and its specific method of calculations, the tax incentive provided will be rendered less effective when it results in the in-scope mining group showing a GloBE ETR of below 15% and ultimately liable for Top-Taxes. The efficiency of the tax incentive was measured against the cost of meeting its policy objective by considering whether there are other, less costly ways to reach the same objective.²⁶⁰ Due to NEMA providing for several other allowable financial provisioning vehicles, mining groups can meet their rehabilitation obligation without using rehabilitation trusts.
 - (v) In addition, it is also required to consider the potential behavioural responses by investors (or contributors in this case) and the possible unintended revenue losses, whether fiscal or within the company, that may result.²⁶¹ In this regard, when mining companies are faced with losing out on the tax benefit provided by the tax exemption in Section 37A of the ITA due to the risk of the imposition of Top-Up Taxes, they may decide to use other rehabilitation vehicles. This could increase government revenues as previously tax-exempt income and accruals in the hands of the rehabilitation trust could become taxable in a different rehabilitation vehicle.
 - (vi) Chapter Seven explored the tax incentives for rehabilitation vehicles in Australia and Canada. These countries use reduced tax rates for rehabilitation vehicles as tax incentives for rehabilitation compliance. Generally, reduced tax rates also create permanent differences because the lower rates typically apply indefinitely to the

²⁵⁹ Illustrative example 3 in chapter 4.

²⁶⁰ Supra note 86 p12.

²⁶¹ Ibid p 11.

trust's income, resulting in income never taxed at the standard corporate tax rate. This will lower the jurisdiction's ETR under the OECD GloBE Pillar Two framework, potentially triggering Top-up Taxes if the ETR falls below the 15% minimum. These international comparisons illustrated that any tax incentives resulting in a permanent difference may create a risk of lowering the GloBE ETR to below 15%.

As mentioned, tax incentives are not merely instruments to promote foreign direct investment but also to encourage companies to contribute to environmental sustainability and community upliftment.²⁶²

The findings suggest a real risk that implementing Pillar Two measures in South Africa will undermine the tax benefit granted under the ITA, ultimately penalising mining companies for complying with their statutory obligations of making provisions for rehabilitation at the closure of mines using rehabilitation trusts. Mining groups using rehabilitation trusts will potentially be liable to pay a top-up tax due to the impact of the incentive provided by section 37A and section 10(1)(cP) to the ITA in calculating the GloBE ETR.

In conclusion, this study underscores that implementing Pillar Two measures in South Africa makes using rehabilitation trusts as a financial provisioning vehicle less attractive due to the Top-Up Tax risk created by the tax incentive under section 37A and 10(1)(cP). Therefore, the tax incentive will lose efficiency and efficacy in motivating mining groups to use rehabilitation trusts as their financial provisioning vehicle.

8.2 Recommendations

8.2.1 Recommendation: Classifying rehabilitation trusts as an Excluded Entity

As discussed, above and in light of the discussion in Chapter Four, the ETR for an MNE Group is computed on a per-jurisdiction basis, being equal to the sum of the Adjusted Covered Taxes of each Constituent Entity located in that jurisdiction divided by the net GloBE Income of that MNE in the same jurisdiction for the fiscal year.

The GloBE Rules do not apply to certain Entities of an in-scope MNE Group, also defined as Excluded Entities. These exceptions include governmental entities.²⁶³

As defined in Chapter Four, a governmental entity is a so-called “sovereign entity” that would, in the normal course of business, not be liable for tax in the state it governs. The GloBE Rules provide a list of criteria which must all be met for an Entity to qualify as an Excluded Entity

²⁶² Supra note 86 p 14.

(Chapter Four). Given the purpose that the rehabilitation trust serves and which is reflected in its design, it does meet some of the qualifying requirements of an “Excluded Entity”, such as having the principal purpose of fulfilling a government function (i.e., the obligation to protect the environment); its remaining assets after fulfilling its function vests in the government or a similar vehicle (i.e., remaining assets will not benefit the contributor); the ultimate purpose of the vehicle is to promote social welfare (i.e., by restoring the assets of the South African nation); substantially all of the income from its activities is exempt from income tax in its jurisdiction of residence; and the assets of the vehicle must solely be applied for the rehabilitation of the environment.

Due to its unique features and targeted purpose, a rehabilitation trust does not fall within these definitions. This dissertation recommends that rehabilitation trusts be included as so-called Excluded Entity for the GloBE Model Rules and Pillar Two to prevent mining companies from being negatively affected.

8.2.2 Recommendation: Widen the scope of the SBIE to include rehabilitation assets

As briefly discussed in Chapter Five, the SBIE excludes profits that one would not generally link to profit shifting practices.²⁶⁴ The SBIE consists of two categories, one being “eligible tangible assets”, which includes assets that indicate substantive business activities.²⁶⁵

A rehabilitation asset, however, cannot be likened to a tangible asset. Although it is treated as an asset through accounting, the mining right holder cannot benefit economically from it.

Rehabilitation trusts are created for mining rehabilitation and environmental responsibility. They are not a method used to shift profits, as any profits shown by the rehabilitation trust are ring-fenced to be used for rehabilitation or relinquished to the state. Thus, this dissertation recommends including rehabilitation trusts in the SBIE, as they are not generally linked with BEPS practices.

8.3 Conclusion

The imposition of Pillar Two measures in South Africa could likely undermine the tax benefit granted under the ITA, ultimately penalising mining companies for complying with their statutory obligations to make provisions for rehabilitation at mine closures. Mining groups will, therefore, potentially be liable to pay a top-up tax due to the low effective tax rate, effectively

²⁶⁴ Article 5.3 deals with the SBIE which effectively reduces the excess profits of a Constituent Entity with 5% of the sum of the “eligible payroll costs” and the “eligible tangible assets” for each Constituent Entity, excluding constituent entities that are investment entities, in that country.

²⁶⁵ Article 5.3.3 and 5.3.4 to the GloBE Rules.

eradicating any incentive provided by section 37A and section 10(1)(cP) to the ITA for making such contributions to a rehabilitation trust.²⁶⁶

²⁶⁶ *Supra* note 86.

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