



Domestic Resource Mobilization in Mozambique's Extractive Sector For Climate Financing



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Table of Contents

Executive Summary	6
1. Introduction	8
1.1 Aims and Objectives of the Report	9
1.2 Methodology	9
2. Climate Vulnerability and the State of Climate Finance in Mozambique	11
2.1 Mozambique’s Climate Vulnerability	11
2.2 Mozambique’s Climate Agenda and Aspirations	13
2.3 Projected costs of mitigation, adaptation, and resilience building	15
2.4 Financial instruments for green transformation in Mozambique: challenges and opportunities.....	16
3. Domestic Resource Mobilization and the Extractive Industries in Mozambique.....	20
3.1 Overview of domestic resource mobilization in Mozambique.....	21
3.2 Domestic Resource Mobilization in the extractive sector in Mozambique.....	23
3.2.1 Fiscal revenues dynamics and trends in the extractive sector in Mozambique	24
3.2.2 Legal and institutional framework governing DRM in the extractive sector.....	25
3.2.3 Mozambique’s tax treaties and their impact on revenue collection.....	30
3.2.4 Illicit financial flows in the extractive industry.....	33
3.3 Can Domestic Revenue Mobilization (taxes) from the extractive sector meet the country’s climate finance needs?	34
3.4 The impact of the global climate agenda on DRM in the extractive sector in Mozambique (e.g. prospects for the coal, oil, and gas industries; EU CBAM- implications for the aluminum industry)	35
4. Conclusions and Recommendations.....	38

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Abbreviations

AT	Tax and Customs Authority
BEPS	Base Erosion and Profit Shifting
CBAM	Carbon Border Adjustment Mechanism
CIT	Corporate Income Tax
CONDES	National Council for Sustainable Development
CTA	Mozambique Private Sector Association
CTA	Mozambique Private Sector Association
DRM	Domestic Resource Mobilization
DTAs	Double Taxation Agreements
ENAMMC	National Strategy for Adaptation and Mitigation of Climate Change
EU	European Union
FUNAB	National Fund of Environment
GCF	Green Climate Fund
GDP	Gross Domestic Product
GEF	Global Environment Facility
IFFs	Illicit Financial Flows
INAMI	National Institute of Mines
INP	National Petroleum Institute
IPP	Petroleum Production Tax
KIIs	Key Informant Interviews
LDCF	Least Developed Countries Fund
LNG	Liquefied Natural Gas
MEF	Ministry of Economy and Finance
MIREME	Ministry of Mineral Resources and Energy
MTA	Ministry of Land and Environment
MZN	Mozambican Metical
NAPA	National Adaptation Programme of Action
NDA	National Designated Authority
NDC	Nationally Determined Contribution
PAL	Local Adaptation Plans
SCCF	Special Climate Change Fund
tCO₂eq	Tons of CO ₂ Equivalent
UNDP	United Nations Development Programme
UNFCCC	United Nations Framework Convention on Climate Change
USD	United States Dollar
UTIE	Extractive Industry Taxation Unit
VAT	Value Added Tax

Glossary

Adaptation Fund: Financial mechanism created to support climate change adaptation projects and programs in developing countries. It was established under the Kyoto Protocol of the United Nations Framework Convention on Climate Change (UNFCCC) and became fully operational in 2007.

Carbon Markets: Trading systems where carbon credits or allowances can be bought and sold to encourage emission reductions and investments in low-carbon technologies.

Climate Finance: Financial resources provided to support climate change mitigation, adaptation, and resilience-building efforts, often through international agreements and funds.

Climate Vulnerability: The susceptibility of a region or community to the adverse effects of climate change, often measured by its exposure to climate-related hazards and its ability to adapt.

Debt for Climate Swaps: A financial mechanism in which a developed country cancels a portion of a developing country's debt in exchange for funds to finance climate-related projects.

Domestic Resource Mobilization (DRM): The process by which a country raises revenue from its sources, including taxes and other income, to support its public expenditures and development initiatives.

Double Taxation Agreements (DTAs): International treaties signed between two countries to prevent double taxation of income and assets. These agreements specify which country has the primary right to tax specific types of income.

Exchange rate: The exchange rates between Mozambican Meticals (MZN) and US dollars (USD) used in this study are presented in the table below. The conversion from MZN to USD is done using the end-year average exchange rate during that financial year. (Source: National Institute of Statistics).

Green Bonds: Bonds issued to raise funds for projects that have positive environmental or climate impacts, such as renewable energy or clean transportation.

Green Climate Fund (GCF): financial mechanism established under the United Nations Framework Convention on Climate Change (UNFCCC) to assist developing countries in their efforts to combat climate change.

Global Environment Facility (GEF): multilateral financial mechanism that provides funding and support for environmental projects and initiatives on a global scale. It was established in 1991, as a financial mechanism under the United Nations Environment Programme (UNEP), with the aim of addressing pressing environmental issues and promoting sustainable development.

Illicit Financial Flows (IFFs): Money that is illegally earned, transferred, or utilized. These funds typically originate from three sources: commercial tax evasion, trade misinvoicing and abusive transfer pricing; criminal activities, including the drug trade, human trafficking, illegal arms dealing, and smuggling of contraband; and bribery and theft by corrupt government officials.

National Adaptation Programme of Action (NAPA): A document that outlines a country's immediate needs and strategies for adapting to climate change's adverse effects.

Nationally Determined Contribution (NDC): A country's plan submitted to the United Nations Framework Convention on Climate Change (UNFCCC) outlines its commitments to reduce greenhouse gas emissions and adapt to climate impacts.

Natural Disasters: Sudden and severe events, such as cyclones, floods, and droughts, caused or exacerbated by natural factors, leading to significant harm to people and property.

FY	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Average	29,5	29,9	30,7	38,3	62,6	63,6	60,3	62,6	69,6	63,83

List of figures and tables

Figure 1. Overview of Mozambique’s tax system.....	19
Figure 2. Trends in the fiscal contribution of EI megaprojects (2012-2021)	23
Figure 3. Map of global vulnerability to CBAM	34
Table 1. Key documents on climate change in Mozambique	12
Table 2. Summary of the specific tax and fiscal benefits regime for petroleum operations	25
Table 3. Revenue sources for petroleum operations.....	26
Table 4. Percentage of revenue destined for the State in the Production Sharing Agreement.....	26
Table 5. Summary of the specific tax and fiscal benefits regime for mining activities	27
Table 6. List of Mozambique’s tax treaties and the contents of key articles.....	29

Executive Summary



Mozambique is among the countries most vulnerable to the effects of climate change, with a significant increase in the frequency and intensity of extreme events, such as cyclones, tropical storms, floods, and droughts. In addition to the loss of human life, these events destroy public and private infrastructure, housing, and extensive areas of crops, causing frequent humanitarian crises. Like other low-income countries in the global south, despite contributing little to global carbon

emissions, Mozambique is among those most affected by the effects of climate change. The costs of adaptation, mitigation and building resilience are increasing in a context in which the country is still struggling to mobilize sufficient resources to provide essential services to improve the living conditions of its citizens.

At a global level, despite the various commitments of developed countries, the context is one of great

competition for access to the few resources available to finance measures and actions urgently needed to adapt and mitigate the effects of climate change. Countries are called to think about solutions within their borders, and the domestic mobilization of resources occupies an increasingly central role.

Informed by the increasing challenges posed by the effects of the climate crisis and the corresponding need to mobilize domestic resources to finance adequate responses in a context of heavy dependence on extractive industries, this report investigated and assessed the link between climate financing and DRM based on the extractive industries in the case of Mozambique. The following findings stand out:

- o Mozambique has developed a somewhat comprehensive legal and institutional framework for climate adaptation and mitigation, but the results on the ground remain limited. Limited preparedness and inadequate resources hinder the country's ability to effectively address climate crises, exacerbating the challenges in the context of weak socio-economic infrastructure and high poverty levels.

- o Mozambique faces substantial financial challenges, with the projected costs of adaptation, mitigation, and resilience building amounting to a significant portion of its GDP. The total investment demand from 2020 to 2025 for both adaptation and mitigation measures, as detailed in the country's NDC, including all cross-cutting actions, projects, and policies, is expected to amount to approximately USD 7.586 billion, equivalent to more than half of the country's annual GDP.

- o The state budget has yet to effectively incorporate climate change considerations, limiting its fiscal and climate transparency and affecting public spending efficiency. Furthermore, the use of various green financial instruments in the country, including debt-for-climate swaps, green bonds, and participation in carbon markets, is still incipient.

- o While Mozambique is mobilising some climate finance, it falls short of its climate needs, emphasizing the importance of domestic resource mobilization to address the growing costs of climate adaptation, mitigation, and resilience building.

- o Mozambique has shown a notable improvement in domestic resource mobilisation, with a tax-to-GDP ratio consistently above the African average. Still, persistent fiscal deficits and a history of accumulating unsustainable debt highlight the need for further enhancements in revenue collection.

- o Despite its significant contribution to the country's exports, the extractive sector's contribution to fiscal revenues remains relatively low, accounting for less than 10% of total fiscal revenues in 2021. Mozambique's tax treaty network with tax havens and Illicit Financial Flows, driven by practices such as transfer pricing, trade mispricing,

and tax base erosion, pose a significant challenge to the extractive sector's fiscal contribution.

- o While revenue from the extractive sector, particularly LNG projects, has the potential to contribute to climate finance needs, challenges lie in prioritising climate financing in the budget and ensuring transparent and effective revenue management from the sector.

In light of the above findings, the report recommends the following:

- ⇒ Strengthen advocacy efforts: There is a need to reinforce the role of the Mozambican government and civil society actors in the global advocacy for international financial architecture reform and the mobilization of climate finance for Mozambique and other African countries;

- ⇒ Mainstream climate considerations and disaster risk management considerations in the Budgeting process: Integrate climate change considerations into the National Development Strategy and the yearly national budgeting process. The public resources allocated ex-ante for emergency response and recovery have been significantly lower than the funds needed to cope with catastrophic events. The government should allocate a higher percentage of tax revenue to climate adaptation and mitigation efforts, as stipulated in Decree No. 53/2017;

- ⇒ Reform the legal and institutional framework governing DRM in the extractive industry to make it more efficient and progressive. These include:

- i. Revisit and renegotiate tax treaties, particularly those with the tax havens of Mauritius and UAE, to prevent aggressive tax planning and ensure that Mozambique receives its fair share of taxes from multinational corporations;
- ii. Equipping the UTIE with more financial and human resources to enhance the monitoring process in the mining industry, accurately determining production volumes, and assessing mineral quality to combat under-invoicing and tax evasion;
- iii. Strengthen efforts to combat IFFs in the extractive sector, mainly through measures targeting tax base erosion and profit shifting (BEPS) and transfer pricing abuses. Decree No. 70/2017, of December 6, must be reviewed to include more transparent and enforceable rules for transfer pricing.

- ⇒ Develop a National Climate Finance Taxonomy: Establish a clear and consistent methodology for tracking climate finance across ministries. This taxonomy will facilitate strategic decision-making and resource prioritisation;

- ⇒ Accelerate Paris Agreement Implementation: Expedite the establishment of frameworks under Article 6 of the Paris Agreement to access additional climate funding and support Mozambique's climate goals.

1 Introduction



This report has been informed by the growing impacts of the climate crisis and the need for domestic resource mobilization (DRM) to finance adequate responses, where traditionally, in Africa, there has been a heavy reliance on extractive industries. Mozambique has been heavily affected by the climate crisis, witnessing frequent and intense extreme weather events

such as cyclones, tropical storms, floods, and droughts. Concurrently, extractive industries have dominated the Mozambican economy. Aluminum, coal, natural gas, graphite, and other metals are among the main exports of the country. However, the link between climate financing and DRM based on the extractive industries in the case of Mozambique is yet to be assessed.

1.1 Aims and Objectives of the Report

This research has three key objectives:

- To establish the current state of play on Domestic Resource Mobilization in Mozambique’s extractive sector;
- To determine the extent to which the current International Financial System enables tax injustice and hinders effective DRM mobilization in Mozambique’s extractive sector;
- To assess the extent to which tax can be a tool for climate finance mobilization at national level.

1.2 Methodology

The research team adopted a qualitative approach to conduct the analysis, including a desk review and primary data collection, using key-informant interviews (KIIs). The desk review focused on secondary data reviewed from available reports, academic and professional literature and on existing national and international data covering the topics of the assessment. The KIIs were delivered in the form of semi-structured questionnaire designed to gather a wide range of information from differing profiles and perspectives from policy actors at the national level. Due to budget constraints, the study did not conduct field visits and interviews with community-level actors. However, five (5) KIIs covering the following actors were conducted: government, operators in the extractive industry, private sector, civil society organizations, and development partners. The study aimed at covering a wider range of actors, yet various government institutions were unavailable to provide an interview.

Below is the list of KIIs interviewed:

List of key informants

Acronyms	Institution
AT	Tax and Customs Authority
CTA	Mozambique Private Sector Association
MIREME	Ministry of Mineral Resources and Energy
OXFAM	Oxfam International
TEDI- FCDO	Taxing Efficiently for Developing Inclusively

The report is structured into four sections. The first section is the introduction whilst the second section provides an overview of the climate vulnerability in Mozambique, including trends and impacts of extreme events over the past years, Mozambique’s climate agenda and respective needs for financing mitigation, adaptation, and resilience across the country. The research analyses the extent to which conventional financial instruments such as debt for climate swaps, green bonds, carbon markets and carbon adjustment mechanisms can represent an alternative for climate financing in Mozambique. The third section examines the national scenario of DRM, followed by an in-depth assessment of DRM in the extractive sector in Mozambique and the extent to which it can serve as a basis for climate financing. This discussion is followed by an assessment of fiscal regimes and the governance framework for DRM in the extractive sector in Mozambique, including legislation, national institutional framework, and bilateral tax treaties. The impact of the global climate agenda and the risks of stranded assets on the extractive sector in Mozambique, particularly the future of the fossil fuel industries in Mozambique such as coal, oil and gas are assessed as well as the impact of the Carbon Border Adjustment Mechanism in the European Union are also assessed. The last section presents the conclusions and key recommendations.



2

Climate Vulnerability and the State of Climate Finance in Mozambique

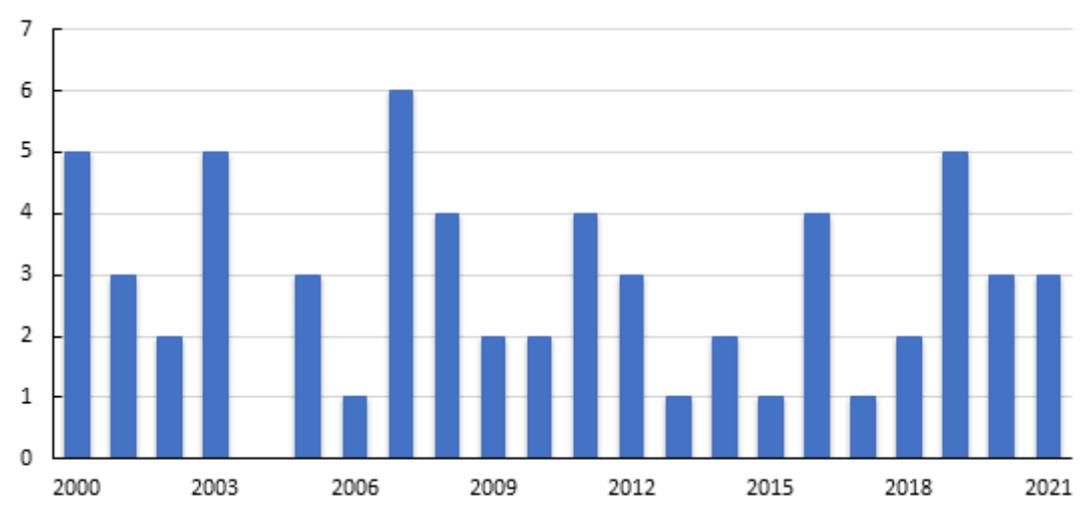


Mozambique's experience of climate shocks highlights the inequalities associated with the global climate crisis, where low-income countries are among the most affected by climate change while contributing the least to carbon emissions. Mozambique's coastline is in the Indian Ocean, known for seismic activities

and cyclones, and therefore highly vulnerable to the impacts of climate change.¹ The country has witnessed an increase in weather shocks, particularly extreme weather events such as tropical cyclones, which have resulted in significant economic and social costs outstripping the country's ability to respond effectively.

1. Matimbe, L. A. (2004). *Frequência de Ciclones Tropicais em Moçambique e a sua relação com a Precipitação* [Frequency of Tropical Cyclones in Mozambique and their relationship with Precipitation]. [Degree Thesis, Eduardo Mondlane University]. <http://monografias.uem.mz/bitstream/123456789/580/1/2004%20-%20Matimbe%2C%20lameque%20Arone.pdf>

Graph 1. Frequency of natural disasters in Mozambique (2000 - 2022)



Source: From the author based on data from the Emergency Events Database

2.1 Mozambique’s Climate Vulnerability

The country ranks 50th out of 181 countries assessed by the World Risk Index, with a high propensity to be affected by disasters and in a critical situation in terms of preparedness to deal with extreme natural disasters². It is estimated that, on average, the country is affected by a tropical cyclone or flood event every two years and a drought event every three years.³ This position is in line with the data on the frequency of disasters, illustrated by Graph 1, where the number of disasters with major social and economic implications is as high as 6 per year.⁴

Recent events in Mozambique show a concerning trend of extreme weather events, namely high-intensity tropical cyclones. Between 2019 and 2023 Mozambique was hit by 5 high-intensity cyclones:

- Between March and April 2019, Mozambique was hit by Cyclones Idai and Kenneth, which were the biggest cyclones ever to hit the country. Approximately 1.7 million people were affected, with damages and losses amounting to USD 3 billion, along with an estimated USD 3.4 billion of total cost for recovery and reconstruction



2. Ministry of Economy and Finance. (2022). Relatório de Riscos Fiscais para 2023 [Fiscal Risks Report for 2023]. <https://www.mef.gov.mz/index.php/todas-publicacoes/instrumentos-de-gestao-economica-e-social/relatorios-de-riscos-fiscais/1703-relatorio-de-riscos-fiscais-2023/file?force-download=1>
 3. Government of Mozambique. (2021). Update of the First Nationally Determined Contribution to the United Nations Framework Convention: Mozambique (2020-2025). https://unfccc.int/sites/default/files/NDC/2022-06/NDC_EN_Final.pdf
 4. Manguela, G. (2023, March 1). Cheias e inundações voltam a expor o despreparo do Governo na gestão do risco de desastres no país [Floods once again expose the government’s unpreparedness in disaster risk management in the country]. <https://cddmoz.org/wp-content/uploads/2020/07/Cheias-e-inundacoes-voltam-a-expor-o-despreparo-do-Governo-na-gestao-do-risco-de-desastres-no-pais.pdf>



- In December 2020, Mozambique was hit by Cyclone Chalane, which worsened the humanitarian situation of people affected by previous cyclones.⁵ Chalane hit Sofala and Manica Provinces, already heavily affected by Cyclone Idai, affecting 602 families and 3,010 people.⁶
- In January 2021, Mozambique was hit by Cyclone Eloise, which affected more than 262,000 people, displaced 16,000, and flooded more than 200,000 hectares of agricultural land.⁷
- In February 2023, Cyclone Freddy made landfall in central Mozambique in the Zambézia province, but it also had considerable impacts in other provinces such as Tete, Inhambane, Sofala, Manica, Zambézia, Gaza and Maputo. The negative effects included a toll of at least 160 lives lost, 700 people injured and affecting over one million individuals. In addition to human losses, numerous homes, schools, health facilities, bridges, and power poles were destroyed by the cyclone.⁸

These extreme weather events have resulted in cumulative negative impacts as they occur in succession allowing no adequate recovery period between them. This situation creates increasing pressure on the state's ability to respond adequately.

To address these challenges, Mozambique has developed a legal and institutional framework (detailed in the next section) which aims to reduce climate risks, promote resilience, and develop a low-carbon green economy. However, the results on the ground are still incipient. Limited preparedness and lack of adequate resources further inhibit the country's crisis adaptation and response capacity, in a context of weak socio-economic infrastructure, high poverty levels, heavy dependence on rain-fed agriculture and limited access to insurance magnify the impact of the shocks, further worsening the living conditions of the country's citizens.⁹ A recent poverty analysis carried out in Mozambique reveals that the occurrence of cyclones, floods, or droughts can result in a significant reduction of approximately 25-30 percent in per capita food consumption and that affected households also cut back on expenditures in basic non-food items.¹⁰

5. Voa Português. (2021, February 4). Eventos climáticos terão impacto no crescimento de Moçambique, prevê a Standard & Poor 's [Climate events will have an impact on Mozambique's growth, predicts Standard & Poor's]. [Weather events will impact Mozambique's growth, predicts Standard&Poor's \(voaportugues.com\)](https://voaportugues.com)

6. Protection Cluster. (2020). Mozambique: Tropical Storm Chalane Flash Update (As at 30 Dec 2020). <https://reliefweb.int/report/mozambique/mozambique-tropical-storm-chalane-flash-update-30-dec-2020>

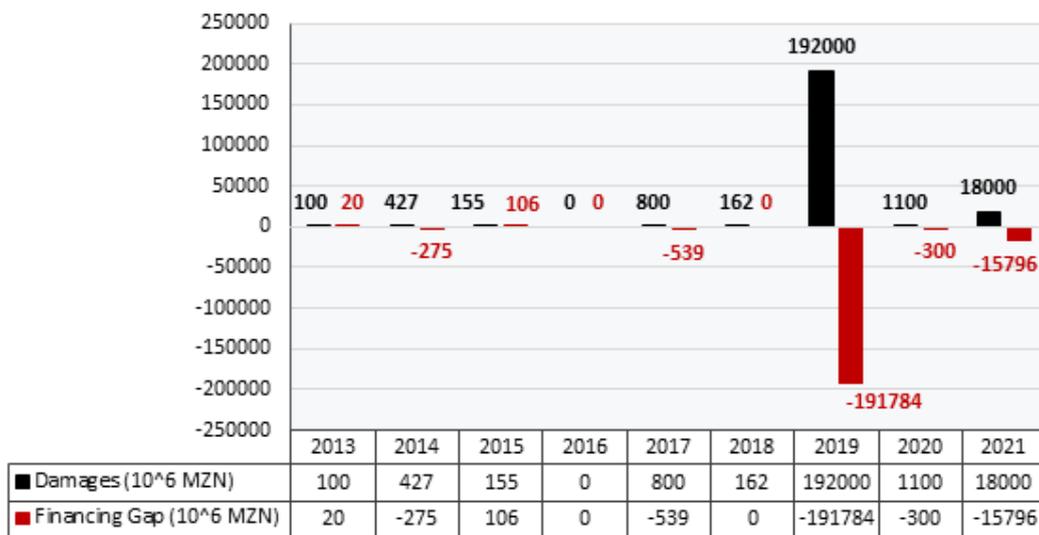
7. United Nations Population Fund. (2021). Cyclone Preparedness and Response. https://mozambique.unfpa.org/sites/default/files/pub-pdf/unfpa_fact_sheet_cyclone_preparedness_and_response_jan_2021_0.pdf

8. U.S. Embassy in Mozambique. (2023). Governo dos E.U.A. Presta Ajuda às Vítimas do Ciclone Freddy em Moçambique [U.S. Government Provides Aid to Cyclone Freddy Victims in Mozambique]. <https://www.deepl.com/translator#pt/en/Governo%20dos%20E.U.A.%20Presta%20Ajuda%20%C3%A0s%20V%C3%ADtimas%20do%20Ciclone%20Freddy%20em%20Mo%C3%A7ambique>

9. Bari, M., Medina, L., and Palacio, E. (n.d). Enhancing Resilience to Climate Change in Mozambique: Risks and Policy Options. <https://www.elibrary.imf.org/downloadpdf/journals/002/2018/066/article-A005-en.xml#:~:text=During%20the%20period%201992%2D2016,to%20cope%20with%20such%20events>.

10. Baez, J.E., Caruso, G. and Niu, C. Extreme Weather and Poverty Risk: Evidence from Multiple Shocks in Mozambique. *EconDisCliCha* 4, 103–127 (2020). <https://doi.org/10.1007/s41885-019-00049-9>

Graph 2. Damages vs Financing gap over the years (2023-2021)



Source: MEF (2023)¹¹

Decree No. 53/2017 of 14 October establishes that the government must channel 0.148% of Tax Revenue to the Contingency Plan for managing the risk of natural disasters¹². However, this instrument has been insufficient to provide the necessary resources for climate change mitigation and adaptation. Reflecting the ineffectiveness of the current model, the Government has annually reported huge differences between the resources allocated to the Annual Contingency Plans and the damage resulting from the occurrence of disasters (as illustrated in graph 2 above). For example, between 2013 and 2021, only MZN 4.1 billion (approximately USD 62.7 million) was allocated to the different Plans in a context where the damage resulting from climatic events in the same period amounted to MZN 212.7 billion (USD 3.2 billion), representing a deficit of more than MZN 208,6 billion (more than USD 3.1 billion).¹³

Overall, it can be said that the public resources allocated ex-ante for emergency response and recovery have systematically been significantly lower than the funds needed to cope with catastrophic events. These financial constraints and the resulting need to mobilize ex-post resources result in inefficient response efforts.¹⁴ This, in turn, leads to protracted and uncertain recovery processes, ultimately amplifying the adverse economic consequences of the shocks.



11. Ministry of Economy and Finance. (2022). Relatório de Riscos Fiscais Para 2023 [Fiscal Risks Report 2023]. <https://www.mef.gov.mz/index.php/todas-publicacoes/instrumentos-de-gestao-economica-e-social/relatorios-de-riscos-fiscais/1703-relatorio-de-riscos-fiscais-2023/file?force-download=1>

12. Government of Mozambique. (2020). Boletim da República. <https://faolex.fao.org/docs/pdf/moz197255.pdf>

13. Ministry of Economy and Finance. (2022). Relatório de Riscos Fiscais para 2023 [Fiscal Risks Report for 2023]. Disponível em <https://www.mef.gov.mz/index.php/todas-publicacoes/instrumentos-de-gestao-economica-e-social/relatorios-de-riscos-fiscais/1703-relatorio-de-riscos-fiscais-2023/file?force-download=1>

14. World Bank. (2019). Mozambique: Cyclone Idai & Kenneth Emergency Recovery and Resilience Project (P171040). <https://documents1.worldbank.org/curated/en/727131568020768626/pdf/Project-Information-Document-Mozambique-Cyclone-Idai-Kenneth-Emergency-Recovery-and-Resilience-Project-P171040.pdf>

2.2 Mozambique's Climate Agenda and Aspirations

(NDC) submitted to the United Nations Framework

Mozambique's climate agenda is reflected in the country's extensive legal and policy framework, which is supported by a robust institutional framework. The National Adaptation Programme of Action (NAPA) from 2007, the National Climate Change Adaptation and Mitigation Strategy for 2013-2025¹⁵, and the Nationally Determined Contribution

Convention on Climate Change (UNFCCC) in 2018 stand out as the key to the country's climate change policy framework. At the district level, the country is also developing Local Adaptation Plans (PAL) for 128 different areas, some of which are already being implemented with major funding hurdles.¹⁶

Table 1. Key documents on climate change in Mozambique

Key Documents	Scope
National Adaptation Programme of Action (NAPA)	Outlines the country's immediate needs, identified through a participatory assessment process, and determined to strengthen the national capacity to cope with the adverse effects of climate change
National Climate Change Adaptation and Mitigation Strategy (2013-2025)	Establishes action guidelines for resilience and disaster risk reduction in vulnerable communities and the national economy. It also seeks to promote development of low carbon emissions and a green economy through its integration into the sectoral and local planning process
Nationally Determined Contribution (NDC)	Climate action plan to cut emissions and adapt to climate impacts. The plan defines how to reach the targets for mitigating the greenhouse gas emissions that cause climate change and for adapting to climate impacts, and elaborate systems to monitor and verify progress so it stays on track.

Source: Mombauer, D., & Wijenayake, V. (2021)

The strategic actions presented in the adaptation component of Mozambique's NDC are part of the adaptation and climate risk reduction pillar of the National Climate Change Adaptation and Mitigation Strategy (ENAMMC). For the adaptation component, based on the country's adaptation and climate risk reduction pillar of the ENAMMC¹⁷, the Mozambican government has a set of strategic actions that cover various sectors, including climate risk reduction; water resources; agriculture, fisheries, food security, and nutrition; social protection; health; biodiversity; forests; and infrastructure, urban areas, settlements, and tourist and coastal zones. On the other hand, the contributions associated with the mitigation theme count on the implementation of actions, measures, projects, policies, and programs that contemplate the sectors of agro-livestock and sustainable land use, waste management, energy security, and sustainability of industries.

The existing policies are supported by an institutional framework centered around the National Council for Sustainable Development (CONDES)¹⁸, the Technical Council for Disaster Management, the Inter-Institutional Group on

Climate Change, the Ministry of Land and Environment, and the Ministry of Economy and Finance. Beyond this governmental framework, civil society organizations play a crucial role in implementing community-level adaptation and mitigation initiatives, empowering local communities in adaptation and mitigation, raising funds for climate projects, and serving as independent watchdogs for ENAMMC implementation.¹⁹

Mozambique's climate goals set out in the country's NDC delineates strategies for reducing greenhouse gas emissions and addressing climate change impacts in accordance with the Paris Agreement principles. Although Mozambique does not yet have a net-zero emissions target²⁰, the recent update of the country's NDC in 2021 describes ambitious goals to be achieved by 2025, including:²¹

- Achieve a reduction of GHG emissions by about 40 million tons of CO2 equivalent (tCO2eq);
- Increase the share of renewable energy in total energy consumption (not specified);
- Achieve a 40% reduction in the prevalence of

15. Ministry for the Coordination of Environmental Action. (2013). Estrat gia Nacional de Adapta o e Mitiga o de Mudan as Clim ticas 2013-2025 [National Strategy for Adaptation and Mitigation of Climate Change 2013-2025]. <https://faolex.fao.org/docs/pdf/moz185538.pdf>

16. Mombauer, D., & Wijenayake, V. (2021). Country Report: Entry Points for the Formulation of a National Adaptation Plan for Mozambique. Southern Voices on Adaptation.

17. This climate strategy is supported by several international cooperation initiatives and projects, involving organizations such as the European Union, the World Bank, the United Nations Development Program (UNDP), and the French Development Agency (AFD), among others.

18. CONDES, founded in 1997 and presided over by the Prime Minister, includes seventeen Ministries, academic institutions, civil society organizations, and private sector representatives. It oversees NDC implementation, report approval, and the coordination of climate policies and strategies.

19. Mombauer, D., & Wijenayake, V. (2021). Country Report: Entry Points for the Formulation of a National Adaptation Plan for Mozambique. Southern Voices on Adaptation.

20 BloombergNEF. Climate Scope. <https://www.global-climatescope.org/markets/mz/>

21. Government of Mozambique. (2021). Update of the First Nationally Determined Contribution to the United Nations Framework Convention: Mozambique (2020-2025). https://unfccc.int/sites/default/files/NDC/2022-06/NDC_EN_Final.pdf

- uncontrolled fires;
- Restoring 5,000 hectares of forests and mangroves.

The emission reductions proposed in Mozambique's mitigation contribution would represent a mitigation effort of about 1.2 tCO₂eq per capita by 2025. To achieve this target, the country has outlined dozens of adaptation, mitigation, and cross-cutting actions, measures, projects, and policies whose implementation is heavily reliant on international climate support.²²

2.3 Projected costs of mitigation, adaptation, and resilience building

Mozambique faces significant financial challenges in dealing with the effects of climate change and implementing adaptation and mitigation measures. The estimated costs for adaptation, mitigation, and building climate resilience are substantial and do not significantly match with the country's DRM efforts.

The total investment demand from 2020 to 2025 for both adaptation and mitigation measures, as detailed in the country's NDC, including all cross-cutting actions, projects, and policies, is expected to amount to approximately USD 7.586 billion, equivalent to more than half of the country's annual GDP.²³ The financing gap is more concerning if considered within the projected costs of building resilience, which are expected to absorb more than one third of the country's GDP till 2030.²⁴

While the projected costs of mitigation, adaptation, and resilience building are increasing, the state budget still fails to clearly make provisions to fund the country's NDC²⁵. The climate change dimension is yet to be mainstreamed into the planning and budgeting process. If this continues, Mozambique will be unable to benefit from its advantages in terms of increased fiscal and climate transparency, increasing the efficiency of public spending through the process of pre-assessment and approval of projects planned by the State before they are funded on social and economic impact, as well as on vulnerability considerations and other aspects of global climate change.

In sum, Mozambique sits at a complex intersection between high vulnerability to climate shocks and financial challenges to ensure climate adaptation, mitigation, and resilience building. There is an urgent need to design mechanisms

to address the challenges and ensure a more resilient and sustainable future for present and future generations. Global climate finance commitments as well as financial instruments such as debt for climate swaps, green bonds and carbon markets are presented as an alternative for ensuring financing for climate needs. The next sub-section explores the opportunities and limitations posed by these instruments for the case of Mozambique.

2.4 Financial instruments for green transformation in Mozambique: challenges and opportunities

The financial resources required to adequately respond to the challenges posed by climate change in Mozambique far outweigh the resources available. Within the context of sparse resources, climate finance is often presented as the alternative for developing countries to support the mobilization of resources for climate mitigation, adaptation, and resilience building. Global climate finance commitments as well as financial instruments such as debt for climate swaps, green bonds and carbon markets are among the main financial instruments presented as an alternative for funding climate needs.

Debt-for-Climate Swaps

Up to this date, there is record of only one debt-for-climate swap in Mozambique.²⁶ This particular debt-for-climate swap proposal, announced in June 2023, covers 2.4 million euros of Mozambique's outstanding debt to the Belgian State, which amounts to 5.6 million euros.²⁷ At the time of the agreement's announcement, Mozambique was making annual payments of 500,000 euros to the Belgian government as part of its debt obligations. However, under the proposed debt-for-climate swap, the payments would no longer be directed to the Belgian government but instead channeled to the Belgian development agency, Enabel. Enabel will then utilize these funds to finance climate change projects in the country, aligning debt relief with climate action and sustainable development initiatives within the country.

Although contributing to mobilize additional finance, even for heavily indebted nations like Mozambique, debt-for-climate swaps remain a rather restricted source of financing. This limitation arises not because they are completely reliant on the creditors and their political agendas but also from the fact that, when implemented,

22. *Ibid.*

23. Government of Mozambique. (2021). Update of the First Nationally Determined Contribution to the United Nations Framework Convention: Mozambique (2020-2025). https://unfccc.int/sites/default/files/NDC/2022-06/NDC_EN_Final.pdf

24. Oeconómico. (2023, March 28). Moçambique precisa de investir 1/3 do PIB até 2030 para se tornar resiliente às mudanças climáticas [Mozambique needs to invest 1/3 of GDP by 2030 to become resilient to climate change]. <https://www.oeconomico.com/mocambique-precisa-de-investir-de-1-3-do-pib-ate-2030-para-se-tornar-resiliente-as-mudancas-climaticas/>

25. Government of Mozambique. (2021). Update of the First Nationally Determined Contribution to the United Nations Framework Convention: Mozambique (2020-2025). https://unfccc.int/sites/default/files/NDC/2022-06/NDC_EN_Final.pdf

26. The information on the details of the agreement is scarce. The team's attempts to reach out to Enabel for additional clarifications did not yield any outcomes.

27. Belga News Agency. (2023, June 23). Belgium offers Mozambique 2.4m euro 'debt-for-climate swap'. <https://www.belganewsagency.eu/belgium-offers-mozambique-24-million-debt-for-climate-swap>

BOX

1

Debt-for-Climate Swaps

The Debt for Climate Swaps are a financial solution in which a donor country (a developed country) agrees to cancel a portion of a developing country's debt if the latter uses the funds to finance climate-related projects. Ideally, this mechanism would help alleviate external debt while also mobilizing financial resources to address climate change.

they typically provide minimal fiscal impact on participating countries.²⁸ Furthermore, there is mounting evidence that these instruments are not an efficient use of finance as a substantial portion of the money relieved through them does not get effectively allocated to climate-related projects.²⁹

It's crucial to recognize that while additional swap agreements can address a country's climate finance requirements, they may also have unfavorable repercussions on its standing in international markets. As highlighted in an analysis by the African Development Bank (AfDB)³⁰, particularly in the context of commercial debt, any form of renegotiation of the initial bond or loan terms, even in the name of biodiversity conservation, will inevitably have an adverse effect on the country's perceived creditworthiness. This could potentially lead to a downgrade in credit ratings and, consequently, an increase in the cost of future borrowing. Therefore, it can be asserted that while debt swaps serve as a valuable tool for countries already in default, those with ongoing market access might consider pursuing alternative methods to finance climate and environmental initiatives.

28. Camps Adrogué, B., & Plant, M. (2022, December 12). Debt-for-Climate Swaps Won't Solve the Climate or Debt Crises, but Can They Help? Center for Global Development. <https://www.cgdev.org/blog/debt-climate-swaps-wont-solve-climate-or-debt-crises-can-they-help>

29. African Natural Resources Management and Investment Centre. 2022. Debt for Nature Swaps – Feasibility and Policy Significance in Africa's Natural Resources Sector. African Development Bank. Abidjan, Côte d'Ivoire. <https://www.afdb.org/en/documents/debt-nature-swaps-feasibility-and-policy-significance-africas-natural-resources-sector>

30. *Ibidem*

BOX

2

Green Bonds for climate finance

Green bonds are an alternative source of financing for climate projects where bonds are issued by companies, governments, and financial institutions to fund green projects, for instance in renewable energy, energy efficiency, clean transportation, and water conservation¹. An example of a bond issue in Africa is the \$41.45 million Kenya bond issued in 2019. The bond was subscribed 2.4 times more than needed, indicating strong demand by investors.² Bond proceeds are being used to fund geothermal and wind power projects, which will help reduce Kenya's reliance on fossil fuels.

1. The World Bank. (2015, December 1). What Are Green Bonds? <https://www.worldbank.org/en/topic/bonds/brief/green-bonds>

2. Read more details on Kenya Green Bonds Programme Webpage – <https://www.greenbondskenya.co.ke/about>



Green Bonds

Despite enormous potential for green investments in renewable energy projects, sustainable agriculture and waste management, Mozambique has not yet established green bond commitments. Like in the major of other African countries, green bonds are still perceived as a foreign concept. In spite of green bonds' potential in terms of raising additional funds for environmentally aligned sustainable development projects in accelerating climate change mitigation and adaptation, the Mozambican private and public sectors have lagged behind other countries from the region (South Africa, Morocco, Nigeria, Seychelles, Namibia and Kenya) in the issuance of these innovative bonds.³¹

The benefits of this financial tool in terms of securing extra funding are not without their downsides. The first and perhaps most concerning for countries like Mozambique is the fact that represent a form of debt financing. After all, by their nature, green bonds are tradable financial instruments that allow the issuer of the bond to borrow funds with a promise to pay back the money (i.e., the principal), usually with interest, by a certain date. This represents a major deterrent for a government that is already struggling with high levels of indebtedness.

Given the country's high level of indebtedness, ideally, the private sector should be the one driving the use of this innovative financial instrument to raise money for environmentally beneficial purposes. However, Mozambique continues to grapple with unresolved challenges related to limited institutional capacity, the absence of essential regulatory measures, and the absence of compelling incentives to stimulate greater involvement from the private sector. The government has been working on policies and strategies to encourage the implementation of this financial instrument, including the establishment of a legal framework to attract investors, with no significant progress made thus far.³²

Carbon Markets

Mozambique is participating in the carbon markets through the Forest Carbon Partnership Facility (FCPF), a trust fund from the World Bank supporting countries in reducing emissions from deforestation and forest degradation, commonly known as REDD+. The FCPF pays Mozambique for reducing carbon emissions by tackling deforestation and

31. Marbuah, G. (2021). Scoping the green bond landscape in Africa. Stockholm Environment Institute. <http://www.ijstor.org/stable/resrep29540>

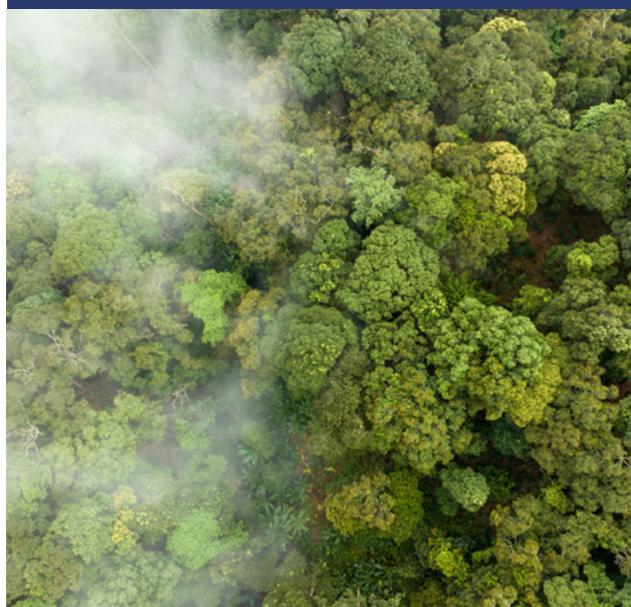
32. Open.Enabel. (2022, July 29). Mobilising climate finance for the implementation of Mozambique's Nationally Determined Contributions under the Paris Agreement. <https://open.enabel.be/en/MOZ/2081/1825/u/mobilising-climate-finance-for-the-implementation-of-mozambique-s-nationally-determined-contributions-under-the-paris-agreement.html>

BOX
3

Carbon Markets for climate finance

Carbon markets are trading systems in which carbon credits or allowances can be bought and sold. A carbon credit is a kind of tradable permit that equals one ton of carbon dioxide, or the equivalent amount of a different greenhouse gas reduced, sequestered, or avoided. ¹ They aim to encourage companies and countries to limit their emissions of greenhouse gases by putting a price on carbon. The price reflects the environmental and social costs of emitting carbon and creates an incentive to reduce emissions or invest in low-carbon technologies.

1. UNDP Climate Promise. (2022). What Are Carbon Markets and Why Are They Important? <https://climatepromise.undp.org/news-and-stories/what-are-carbon-markets-and-why-are-they-important>





forest degradation in the Zambézia Province.³³ Mozambique became the first country to receive payments from the FCPF in October 2021, when it received USD 6.4 million for reducing 1.28 million tons of carbon emissions since 2019. The payment is the first of four under the country's Emission Reductions Payment Agreement (ERPA) with the FCPF that could unlock up to USD50 million for reducing up to 10 million tons of CO₂ emissions in Mozambique's Zambézia Province by the end of 2024.³⁴

The payments reward efforts to reduce carbon emissions by adopting sustainable agriculture practices, monitoring the use of forest resources, or restoring degraded land. Local communities will receive a previously agreed-upon portion of the payments concerning their contribution to reducing deforestation. A benefit-sharing plan prepared with local actors and communities that have contributed to the results will ensure that they receive most of the benefits.³⁵

The country is also at the forefront of the list of the African Carbon Markets Initiative (ACMI) member countries and is currently in the process of formulating regulations for the sector. In addition to reducing deforestation and forest degradation emissions, Mozambique could participate in other types of carbon markets, such as those related to energy or industry sectors. For example, Mozambique has a large potential for renewable energy sources, such as hydro, solar, and wind power, which could reduce its dependence on fossil fuels and generate carbon credits.³⁶

However, there is a dark side to carbon markets that cancels out any potential benefits to local communities. Particularly worrying for Mozambique is the fact that, if not managed properly, carbon markets can further deteriorate the challenges on insecurity, land appropriation, and human rights violations, disproportionately affecting local communities. Indeed, investigations have shown that these dynamics have promoted the search for areas of high biodiversity with the aim of capturing carbon and subsequently selling carbon credits, which can jeopardize the population's subsistence. The set of projects has an adverse impact on rural livelihoods and triggers new forms and dynamics of poverty among communities and have also contributed to an increase in land competition in Mozambique, in response to the predatory introduction of resource extraction.³⁷

Overall, it can be said that while the country is already mobilizing some climate finance, the overall amount is not sufficient to meet Mozambique's climate needs. Mozambique's share in international financing commitments is not enough to cover the needs, and the use of financial instruments is incipient. Like many other countries from the global south that contribute very little with global carbon emissions but are the most affected by the effects of climate change, Mozambique is challenged to look for solutions within its borders to finance the increasingly high costs of adaptation, mitigation, and building resilience. More than ever, domestic resource mobilization should be at the top of the priorities of the Mozambican government.

33. World Bank. (2021). Mozambique Becomes First Country To Receive Emission Reductions Payments From Forest Carbon Partnership Facility. <https://www.worldbank.org/en/news/press-release/2021/10/15/mozambique-becomes-first-country-to-receive-emission-reductions-payments-from-forest-carbon-partnership-facility>

34. World Bank. (2021). Mozambique Becomes First Country To Receive Emission Reductions Payments From Forest Carbon Partnership Facility. <https://www.worldbank.org/en/news/press-release/2021/10/15/mozambique-becomes-first-country-to-receive-emission-reductions-payments-from-forest-carbon-partnership-facility>

35. World Bank. (2021). Mozambique Becomes First Country To Receive Emission Reductions Payments From Forest Carbon Partnership Facility. <https://www.worldbank.org/en/news/press-release/2021/10/15/mozambique-becomes-first-country-to-receive-emission-reductions-payments-from-forest-carbon-partnership-facility>

36. Observatory of Economic Complexity. (2021). Bilateral Product Trade Between Mozambique and All Countries - Carbon. <https://oec.world/en/profile/bilateral-product/carbon/reporter/moz>

37. BRUNA, N., Monjane, B e Samuel, E. (2021). Para Além do Gás e Carvão: Créditos de Carbono na Corrida Extractivista aos Recursos Naturais Em Moçambique. Destaque Rural No 135. Observatório do Meio Rural. Maputo, Moçambique.

Climate Finance in Mozambique: A typical case of a developing Country



While Mozambique may appear to be making commendable strides in mobilizing climate finance based on the sheer number of projects from different climate funds it has been undertaking, a closer examination reveals a stark reality that resonates with numerous developing countries. Mozambique faces a substantial gap between the resources mobilized and the comprehensive requirements to effectively address climate change.

Mozambique has USD 3.14 million approved from the Green Climate Fund (GCF)¹ for readiness support (which comprises adaptation planning, National Designated Authority (NDA) strengthening, strategic framework), with \$1.46 million already disbursed. The country also benefits from 7 GCF-funded projects worth \$30.6 million, addressing various issues such as green energy access, blue economy investments, coral reef protection, climate investment at the sub-national level, energy access support, and ecosystem-based adaptation for vulnerable coastal populations. The Ministry of Economy and Finance coordinates all GCF projects.²

Under the Global Environment Facility (GEF)³, Least Developed Countries Fund (LDCF), and Special Climate Change Fund (SCCF), Mozambique is involved in a total of 38 national, regional global projects, with a total financing of USD 300 million and most of the STAR GEF-8 allocation utilized for biodiversity and land degradation, to the detriment of climate change.⁴ Furthermore, the country, along with Madagascar, Malawi, and the Union of Comoros, is part of a USD 13 million regional project on urban climate resilience under the Adaptation Fund.⁵

The combined finance mobilized through the three climate funds – GCF, GEF, and the Adaptation Fund,

about USD 350 million, is roughly equivalent to a mere 5% of the country's projected needs. This underscores the challenges the country faces and other less-polluting developing nations significantly impacted by climate change. Like other African developing countries, Mozambique grapples with inadequate financial support from the international community, particularly from the global north, which bears primary responsibility for climate change. Accessing the much-needed funding is becoming increasingly challenging as developed countries have failed to honor their \$100 billion climate finance pledge made at the COP15 in 2009.

Countries are becoming increasingly competitive in pursuing additional financing, with Mozambique falling behind due to country-level challenges. The lack of clear definitions and consistent methodology to track climate finance across different ministries is the most concerning among the prevailing challenges. Climate finance in Mozambique would benefit from increased clarity and institutional coordination, as several entities are involved, including MEF, MTA, and “broker” institutions such as UNDP. Some progress has been made with establishing the National Fund of Environment (FUNAB) through Decree no. 26/2011 and ENAMMC to manage and coordinate climate funds, with current efforts focused on FUNAB's accreditation for accessing global climate funds.⁶

Moreover, a climate finance taxonomy would help to develop mobilization strategies and make informed decisions on which funding sources to prioritize.⁷ The country also needs to accelerate the pace of establishing the framework under Article 6 of the Paris Agreement, still in progress, to tap additional funding.

1. Green Climate Fund – <https://www.greenclimate.fund/#> (October 2023)

2. GCF (2023, October 21) – <https://www.greenclimate.fund/countries/mozambique#overview>

3 <https://www.thegef.org/> (October 2023)

4. GEF (2023, October 21) – <https://www.thegef.org/projects-operations/country-profiles/mozambique>

5. Adaptation Fund (2023, October 21) – <https://www.adaptation-fund.org/project/building-urban-climate-resilience-south-eastern-africa-madagascar-malawi-mozambique-union-comoros-2/>

6. Zagama, B., Kowalzig, J., Walsh, L., Hattle, A., Roy, C., & Dejgaard, H. P. (2023). Climate Finance Shadow Report 2023: Assessing the delivery of the \$100 billion commitment. Oxfam International. <https://policy-practice.oxfam.org/resources/climate-finance-shadow-report-2023-621500/>

7Open.Enabel. (2022, July 29). Mobilising climate finance for the implementation of Mozambique's Nationally Determined Contributions under the Paris Agreement. <https://open.enabel.be/en/MOZ/2081/1825/u/mobilising-climate-finance-for-the-implementation-of-mozambique-s-nationally-determined-contributions-under-the-paris-agreement.html>

3

Domestic Resource Mobilization & the Extractive Industries in Mozambique

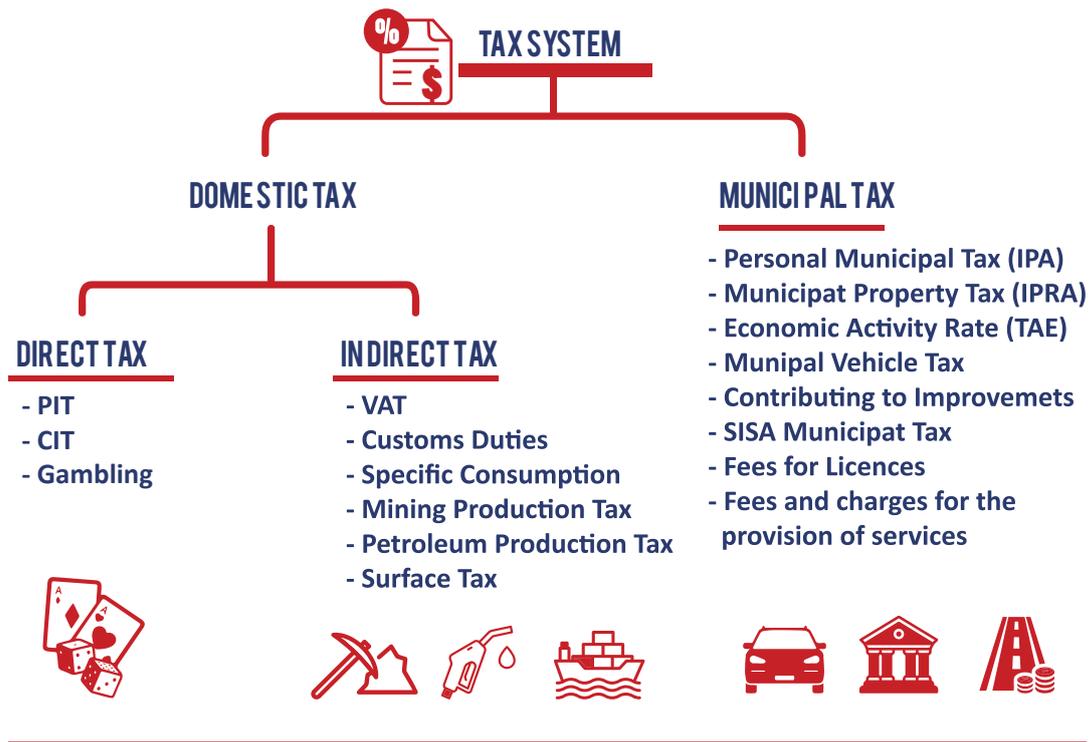


The Mozambican tax system is structured into two subsystems (national and municipal taxes) through which wealth, income, and consumption are taxed separately. In turn, these are classified as direct taxes (levied directly on income or wealth) and indirect taxes (levied on expenditure). The collection of these revenues, including natural resources-related revenues, is under the responsibility of the Mozambican Revenue Authority (known as *Autoridade Tributária de Moçambique – AT*),

operating under the official oversight of the Ministry of Economy and Finance (MEF). In addition, local governments such as municipalities also collect municipal taxes prescribed in the Municipal Tax System Law.³⁸ The local governments have financial autonomy in the management of the resources they collect (Article 276 of the Republic of Mozambique Constitution), while AT channels all of the collected revenue to the public treasury account (*Conta Única do Tesouro – CUT*).

38 Law 1/2008 of January 16 and Decree 63/2008 of December 30.

Figure 1. Overview of Mozambique's tax system



Source: adapted by authors from ITIE (2022)

3.1 Overview of domestic resource mobilization in Mozambique

Mozambique has witnessed a notable rise in its overall revenue collection over the last decade, despite facing various challenges including the insurgency in Cabo Delgado, the occurrence of natural disasters, the COVID-19 pandemic, among others.³⁹ Indeed, the analysis of the tax-to-GDP ratio reveals a gradual upward trend in the performance of the revenue authority over the past years. The total amount of taxes collected by the government as a percentage of the country's GDP averaged 25% in the last decade, significantly surpassing the prevailing average in Africa of 16%.⁴⁰ As illustrated by the graph below, the total revenues collected increased from 21% of GDP in 2012 to 26% in 2021 (tax and non-tax revenues). Notably, the tax-to-GDP ratio reached its pinnacle in 2019 at 29%, marking the highest point in the recent period, only to experience a rapid decline in 2020 due to the impact of the COVID-19 pandemic.

Despite having a relatively high tax to GDP ratio compared to other African countries, historically, the Mozambican State Budget has consistently grappled with budget deficits. This persistent shortage in public finances has compelled the Government to accumulate debt, both domestically (in the form of internal public debt) and internationally (through external public debt). In 2015, the situation took a more severe turn when an illegal debt of USD 2 billion, known as the "hidden debt scandal", was added to the General State Account. This event triggered a rapid escalation of public debt, propelling it to levels deemed unsustainable. Consequently, the country found itself positioned among the economies grappling with the most heightened levels of public debt.⁴¹

The hidden debt scandal triggered an unprecedented crisis in the State's accounts as development partners interrupted their budget assistance. This situation resulted in austerity measures, with public expenditure per person (USD per capita) decreasing by about 39% between 2014 and 2019.⁴² The Government's planning and budgeting process has unmistakably embraced the principle of

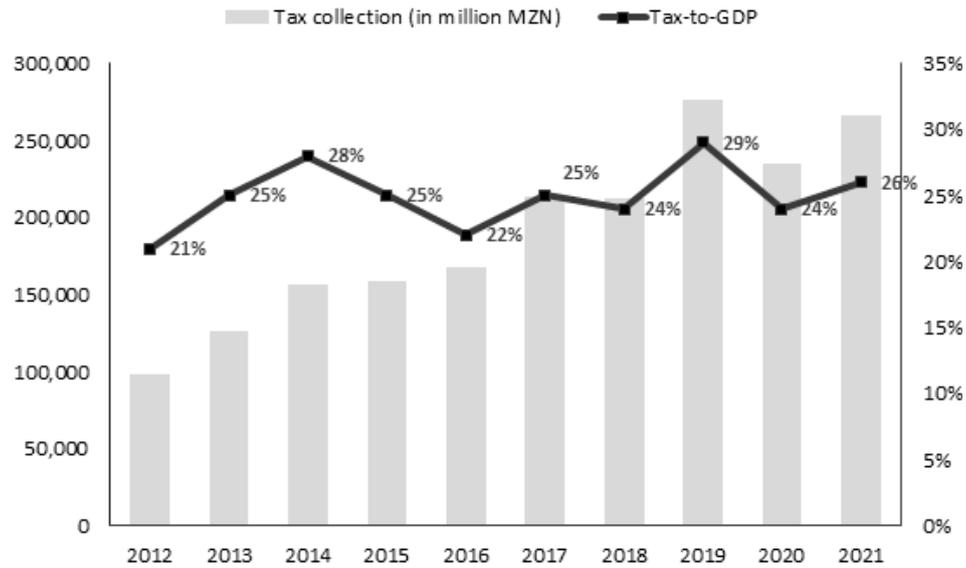
39. Ministry of Economy and Finance (2021). *Report of the Balance of Implementation of the Strategic Plan for Public Finance 2016 - 2019*. <https://www.mef.gov.mz/index.php/publicacoes/politicas/avaliacao-do-desempenho-da-gestao-de-financas-publicas/1215-relatorio-da-implementacao-pefp-2016-2019/archive>.

40. Organization for Economic Co-operation and Development. (2019). *Revenue Statistics in Africa 2019: African Union Commission, African Tax Administration Forum and OECD*. <https://www.oecd.org/tax/tax-policy/brochure-revenue-statistics-africa.pdf>

41. Machava, A. (2019, November 25). *What price are Mozambicans paying for the unsustainable public debt?*. http://eleicoes.cddmoz.org/wp-content/uploads/2019/12/What_price_are_mozambicans_paying_for_the_unsustainable_public-debt_.pdf

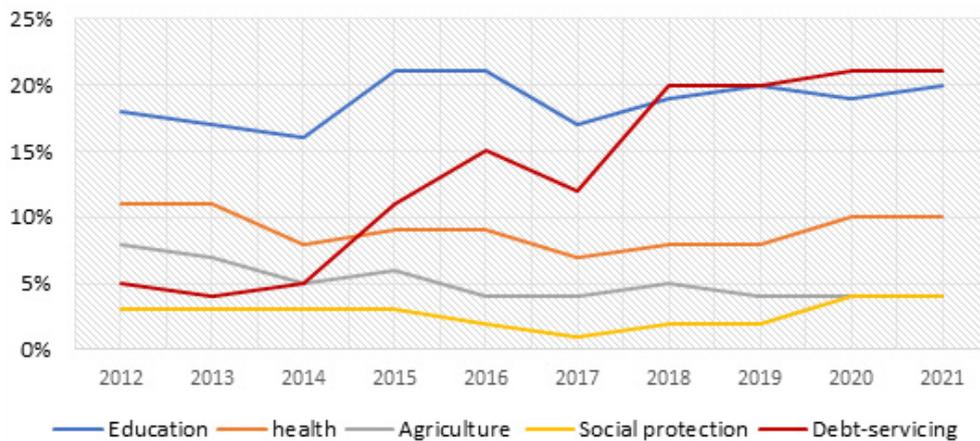
42. Center for Public Integrity. (2019). *Costs and Consequences of Hidden Debts for Mozambique*. <https://www.cmi.no/publications/file/8282-custos-e-consequencias-das-dividas-ocultas-para-mocambique.pdf>

Graph 3. Trends in Tax Collection (2012-2021)



Source: MEF (Several years)

Graph 4. Trends in the composition of government spending (2012-2021)



Source: MEF (Several years)

favoring debt reimbursement, MZN 1.2 trillion (USD18 bn)⁴³ – about 102% of GDP as of December 2021, over social expenditure as evidenced by the budgets that have been approved in recent years. Graph 3 below illustrates that the portion of the State Budget dedicated to servicing the debt has grown fourfold over the period between 2012 and 2021, while the expenditure on social sectors has almost remained stagnant.

The substantial repayments of debt, encompassing both capital and interest expenditures, have eroded the State’s fiscal space. Strikingly, despite a rise in population leading to heightened demand for state-provided services, the

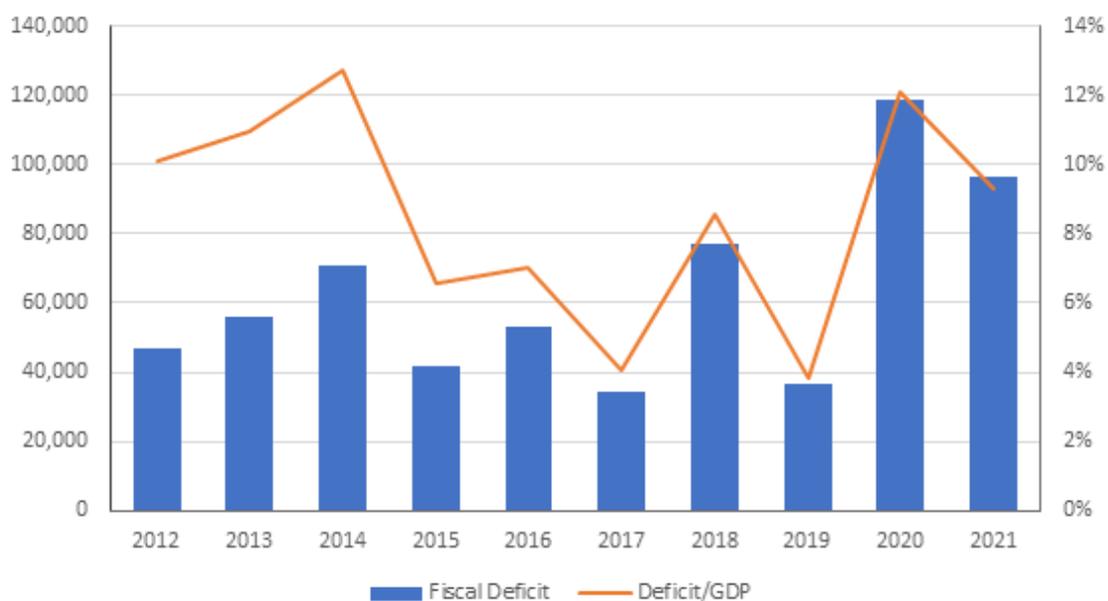
allocation of funds to critical sectors, for example education, healthcare, agriculture, and social protection has displayed minimal growth over the past decade.

Consequently, Mozambique’s tax system still has room for significant improvements not only in terms of revenue collection but also in terms of its fairness⁴⁴, including the revenue sufficiency, progressivity, redistribution, and tax incentives. In terms of revenue sufficiency, the persistent trend of fiscal deficits before development assistance highlights the insufficiency of the country’s fiscal resources to support its expenditure for public service delivery and overall development.

43. Ministry of Economy and Finance. (2021). Annual Debt Report: Fiscal Year 2020. <https://www.mef.gov.mz/index.php/todas-publicacoes/instrumentos-de-gestao-economica-e-social/gestao-da-divida-publica/1511-relatorio-anual-da-divida-publica-exercicio-fiscal-2020-1/file?force-download=1>

44. Sinoia, D., Manguela, G., & Langa, N. (2023). Fair and Efficient Taxation: A Way to Break the Natural Resource Curse in Mozambique? Center for Democracy and Development, Oxfam Novib, & Tax Justice Network Africa.

Graph 5. Trends in fiscal defecits (2012-2021)



Source: MEF (Several years)

In terms of progressivity, besides the heavy reliance on VAT at the disaggregated level, important challenges remain in relation to the size of Mozambique’s informal economy and efforts to expand the base of individuals, for example High Net worth Individuals and legal entities subject to the tax system.

The tax system in Mozambique also includes numerous tax incentives that are incorporated in both the CIT, VAT, and Customs Duties Code, and the separate Code of Fiscal Benefits. These incentives favor new and large foreign investors while placing existing and small businesses at a disadvantage. The numerous incentive instruments also reduce the tax base and create opportunities for tax evasion, avoidance, and tax fraud. The next sub-section develops this topic by looking into the specific tax regimes prevailing in the extractive industry in Mozambique.

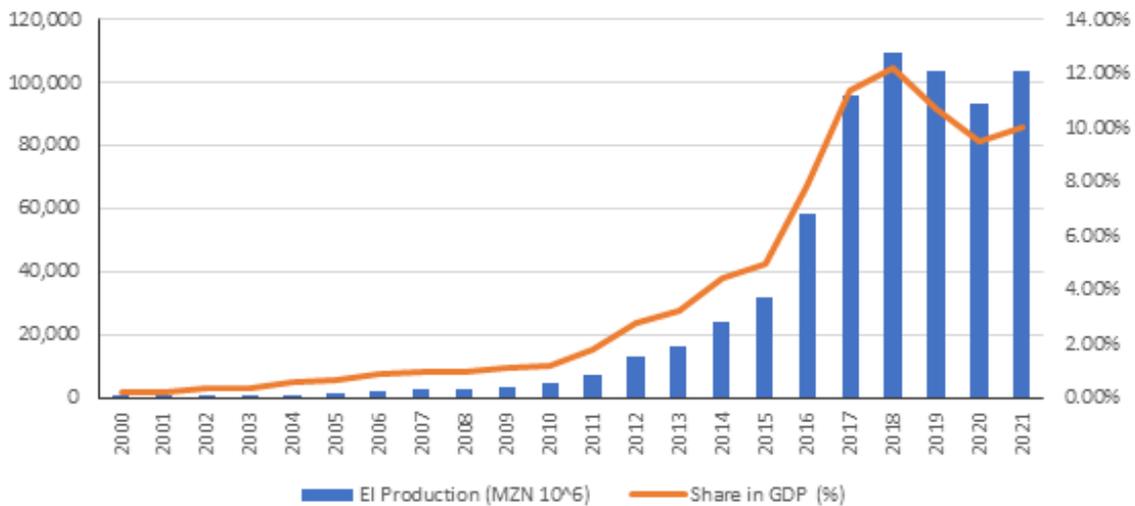
3.2 Domestic Resource Mobilization in the extractive sector in Mozambique

Mozambique’s extractive industry and potential is large and diverse, including significant deposits of coal, natural gas, graphite, iron ore, titanium, apatite, marble, bentonite, bauxite, kaolin, copper, gold, rubies, and tantalum⁴⁵. The country’s extractive sector witnessed a remarkable boom during the onset of what is now referred to as the “age of megaprojects” in the early 2000s. This era marked a significant surge in substantial investment initiatives spanning across both the manufacturing and extractive domains. Noteworthy among these developments was the initiation of major natural gas endeavors in 2004, with Sasol’s Pande and Temane projects situated in the Inhambane province. Subsequently, in 2007, the Kenmare Moma Mining Company introduced its heavy sands project in the Nampula province. Additionally, the Tete province witnessed a significant upswing with the introduction of coal projects by Rio Tinto and Vale in 2011.⁴⁶ Throughout the 2010s, the extractive sector has attracted a huge influx of investment in the significant reserves of Liquefied Natural Gas (LNG) in the Rovuma Basin.

45. Jamal, Z., & Sacur, D. (2022, September 29). Energy transition and the challenges that lie ahead for the Mozambican mining industry. <https://www.ibanet.org/energy-transition-mozambique-mining>

46. Deloitte and EITI (2018). Final Report, EITI Mozambique. Maputo: EITI Mozambique. <https://mireme.gov.mz/wp-content/uploads/2022/07/ITIE-Mocambique-8o-Relatorio.pdf>

Graph 6: Extractive Industry's Production (2000-2021)



Source: National Institute of Statistics (several years)

Despite contributing significantly to exports and economy growth, the fiscal revenues from the extractive sector represented less than

10%

Currently accounting for more than 10% of the country's GDP, the extractive sector contributes significantly to exports and consequently to economic growth in Mozambique, and its contribution to GDP is expected to reach 16% in 2030⁴⁷ as the LNG projects go online. In fact, presently and going forward, the top of the agenda of the government is directed towards transforming the anticipated revenues exceeding \$96 billion from the three LNG mega ventures into tangible benefits for the population.⁴⁸

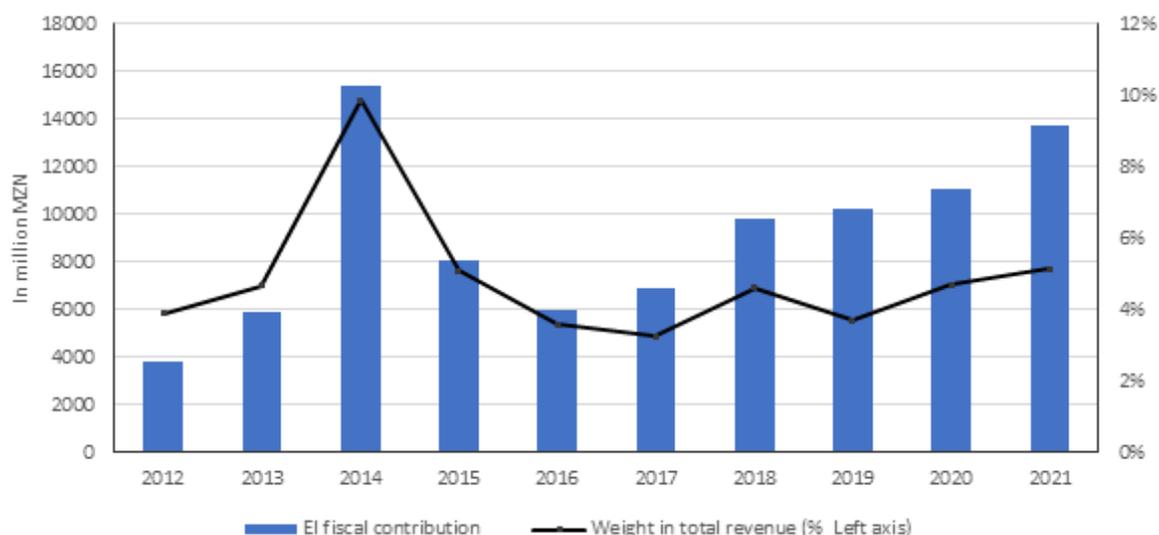
3.2.1 Fiscal revenues dynamics and trends in the extractive sector in Mozambique

Despite contributing significantly to exports and economy growth, the fiscal revenues from the extractive sector represented less than 10% of total fiscal revenues in 2021, as illustrated by the graph below. The peak of the sector's contribution in terms of revenue collections was reached in 2014, at the peak of commodity prices, amounting to MZN 18,1 billion meticaís (USD 589.3 million), before witnessing a deceleration, due to the repercussions of the fall in commodity prices that the country faced to MZN 10,7 billion (USD 279,3 million) in 2015. Since then, the revenue collection has been steadily increasing towards the 2014 peak. In 2021, the sector contributed MZN 13,7 billion (more than USD 209,8 million), equivalent to 5% of the total revenues. This contribution is expected to experience an abrupt increase in the coming years as the country reaps the \$96 billion windfall from the three Liquefied Natural Gas (LNG) megaprojects in the Rovuma Basin.

47. Further Africa. (June 16, 2023). Mozambique extractive industry's GDP contribution to be 16% by 2030 – Minister. <https://furtherafrica.com/2023/06/16/mozambique-extractive-industrys-gdp-contribution-to-be-16-by-2030-minister/>

48. Banco de Moçambique. (2020). Proposta do Modelo de Fundo Soberano para Moçambique. https://www5.open.ac.uk/technology/mozambique/sites/www.open.ac.uk.technology.mozambique/files/files/Proposta%20de%20modelo%20de%20fundo%20soberano_versao%20final.pdf

Figure 2. Trends in the fiscal contribution of EI megaprojects (2012-2021)



Source: AT Tax Statistics Reports (several years)

The revenues in the extractive industry come in the form of Corporate Income Tax (CIT), personal income tax, concession fees, earmarked revenue, royalties, fees in lieu of taxes, VAT, stamp duty, surface tax, dividends, and others. In terms of composition, corporate and personal income tax the most significant, accounting to more than 2/3 of the total fiscal contribution of the sector (as of 2021).⁴⁹

3.2.2 Legal and institutional framework governing DRM in the extractive sector

The extractive sector in Mozambique operates under a relatively robust legal and institutional framework, tailored to accommodate the distinct characteristics of both the mining and hydrocarbons sectors.⁵⁰ Within the mining sector, the cornerstone is the Mining Law ratified by Law No. 21/2014 on August 18, along with its corresponding regulations. These regulations set the framework for the allocation of concessions and licenses, while also delineating the parameters for overseeing, inspecting, and controlling mining operations throughout the country. In parallel, Resolution No. 89/2013, adopted on December 31, outlines fundamental principles and strategic initiatives for the effective management and sustainable utilization of mineral resources. As for the hydrocarbon sector, the legal and regulatory framework for the exploration, production, transportation, processing and commercialization of oil and natural gas is governed by the Petroleum Law of 2014 (Law 21/2014, of 18th August).



49. AT. (2022). Anuário Estatístico: Estatísticas Tributárias 2021 [Statistical Yearbook: Tax Statistics]. Autoridade Tributária. <https://www.at.gov.mz/por/Media/Files/Anuario-Estatistico-2021>

50. I2A Consultoria e Serviços. (2022). Independent Report of the Extractive Industry Transparency Initiative – Year: 2020. *Extractive Industries Transparency Initiative*. https://eiti.org/sites/default/files/2023-01/ITIE%20Moc%CC%A7ambique_10o%20Relato%CC%81rio_ENG_1.pdf

In terms of the institutional framework, the National Institute of Mines (INAMI) is the government agency responsible for regulating and supervising the exploitation of mineral resources in Mozambique. Meanwhile, the oversight of the oil and gas domain lies within the purview of the National Petroleum Institute (INP), which assumes responsibility for issuing exploration licenses, supervising the operations of oil companies, and actively fostering the growth of the oil and gas sector within the nation. Functioning at a strategic level, the Ministry of Mineral Resources and Energy (MIREME) emerges as the central authority responsible for shaping policy and orchestrating planning efforts pertinent to the extractive sector, underscoring its pivotal role in steering Mozambique's trajectory towards responsible resource management and comprehensive development.

As for the fiscal domain, the Extractive Industry Taxation Unit (UTIE) within the National Tax Authority, created in 2016, is responsible not only for collecting taxes from the extractive industry but also for undertaking risk analysis, inspections and specialized audits, among other functions.⁵¹

1) Oil and Gas Sector

The taxation of oil and gas operations in Mozambique is governed by the Specific Regime of Tax and Fiscal Benefits approved by the Law number 27/2014, of 23 September, which has been in force since 1 January 2015. Its regulation, approved by Decree 32/2015, of 31 December, came into force on the date of its publication.⁵² In 2017 the government introduced some amendments to the Specific Regime of Tax and Fiscal Benefits from Petroleum Operations, through the Law number 14/2017, of 28 December⁵³. According to this regime, petroleum operations are subject to both the general taxes that make up the Mozambican tax system and sector-specific taxes provided for in the regime.

Structured to ensure a steady influx of tax revenue for the government, provides for a combination of both production-based revenue-raising mechanisms and profit-based taxes. In tandem with conventional taxes outlined in the broader tax framework, petroleum operations have additional fiscal provisions. This encompasses the Petroleum Production Tax (IPP), complemented by specific income-tax rules and production-sharing mechanisms. As summarized in the table below, the existing petroleum contracts revolve around three main sources of state revenue: (1) royalties,

51. Diário Económico (September 15, 2021). AT cria Unidade de Tributação de Indústrias Extractivas para Aumentar Receitas do Sector [AT creates Extractive Industries Taxation Unit to Increase Sector Revenues]. <https://www.diarioeconomico.co.mz/2021/09/15/negocios/extractivas/at-cria-unidade-de-tributacao-de-industrias-extractivas-para-aumentar-as-receitas-do-sector/>

52. I2A Consultoria e Serviços. (2022). Independent Report of the Extractive Industry Transparency Initiative – Year: 2020. *Extractive Industries Transparency Initiative*. https://eiti.org/sites/default/files/2023-01/ITIE%20Moc%CC%A7ambique_10o%20Relato%CC%81rio_ENG_1.pdf

53. In 2017 the government introduced some amendments to the Specific Regime of Tax and Fiscal Benefits from Petroleum Operations, through Law no. 14/2017 of 28 December.

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5

A new paradigm for revenue-management and sharing in Mozambique

It is also worth noticing two important recent developments affecting the management of the resources derived from the extractive industry operations in Mozambique: the Sovereign Wealth Fund and the new regime of revenue-sharing with producing territories

The Sovereign Wealth Fund (SWF)

The country is currently working on the establishment of a Sovereign Wealth Fund as the elected mechanism to manage the expected revenues from the Rovuma Basin LNG exports. The first official proposal was published in October 2020 and is still being discussed, awaiting approval by the parliament. There is a national consensus that, in line with the proposed objectives, the instrument will help to accumulate savings while smoothing government spending and dissociating it from the short-term volatility of revenues from the exploitation of the resources, thereby avoiding the Dutch disease.

The proposal establishes during the first 15 years, 60% of the collected revenues will go to the State Budget and the remaining 40% to the sovereign wealth account (rules would change to a 50%/50% distribution after the sixteenth year of operation). According to the government, the development objective will be financed with 60% that is channeled to the State Budget, in line with the country's National Development Strategy (NDS), currently under revision.

Revenue-Sharing regime

Mozambique recently reviewed its regime of revenue-sharing with producing regions and those affected by the exploitation of natural resources in the extractive sector. After almost a decade of advocacy and contestation by civil society organizations and other relevant actors, the Mozambican government recently decided to review upward the percentage of revenues allocated to producing territories, from 2,75% to 10%, aiming to ensure that these resources have a direct impact on improving the lives of the populations in the producing regions, thus reducing the asymmetries.

which constitute a small and fixed value per ton of gas/oil produced; (2) corporate income tax, which is assessed based on annual profits; and (3) the most significant source of revenue, known as the “profit oil”, resulting from the state’s share of total production.⁵⁴ First, is deducted a fixed percentage for royalty payments from the gross production. The oil company recovers its incurred expenses, known as “cost oil,” up to a maximum limit of 60% of the petroleum produced after royalties each year. The remaining difference is then used to subtract other eligible costs, resulting in the “profit oil” shared between the state and the company.

Table 2. Summary of the specific tax and fiscal benefits regime for petroleum operations⁵⁵

Petroleum Production Tax (royalties)	Transfer taxes and capital gains																			
<p>Calculated (monthly) based on the value of the petroleum produced. IPP is usually paid in cash, but the government can require taxpayers to pay part or all of their tax in kind.</p> <p>The IPP rates are as follows:</p> <ul style="list-style-type: none"> • Crude Oil: 10% • Natural Gas: 6% <p>Note: A 50% reduction is foreseen in the law for mining products used in the development of local industry</p>	<p>The gains obtained by non-residents from the sale of petroleum rights in the national territory are taxable at a rate of 32%.</p>																			
	Production-sharing mechanism																			
	<p>The distribution of the “profit-oil” follows a decreasing scale (based on the R Factor) that strongly favors the company at the beginning.</p>																			
Income tax rules																				
<p>The CIT rate is the same as the general tax system (32%). But the regime provides for specific income tax rules.</p> <ul style="list-style-type: none"> o The tax profit must be ascertained for each concession agreement, i.e., on an individual basis o Each area of the concession agreement must obtain a NUIT o Specific non-deductible costs (article 22). Among others, the IPP is not deductible. o Specific amortization rates (article 23): 	<table border="1"> <thead> <tr> <th></th> <th>Government</th> <th>Multi Nationals</th> </tr> </thead> <tbody> <tr> <td>R < 1</td> <td>15</td> <td>85</td> </tr> <tr> <td>R 1 – 1.5</td> <td>25</td> <td>75</td> </tr> <tr> <td>R 1.5 – 2</td> <td>35</td> <td>65</td> </tr> <tr> <td>R 2 – 2.5</td> <td>50</td> <td>50</td> </tr> <tr> <td>R 2.5+</td> <td>60</td> <td>40</td> </tr> </tbody> </table>			Government	Multi Nationals	R < 1	15	85	R 1 – 1.5	25	75	R 1.5 – 2	35	65	R 2 – 2.5	50	50	R 2.5+	60	40
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	<p>With a maximum duration of 10 years, which may be extended until the term of the concession in exchange for a 2% annual increase in the production tax rate.</p>																			

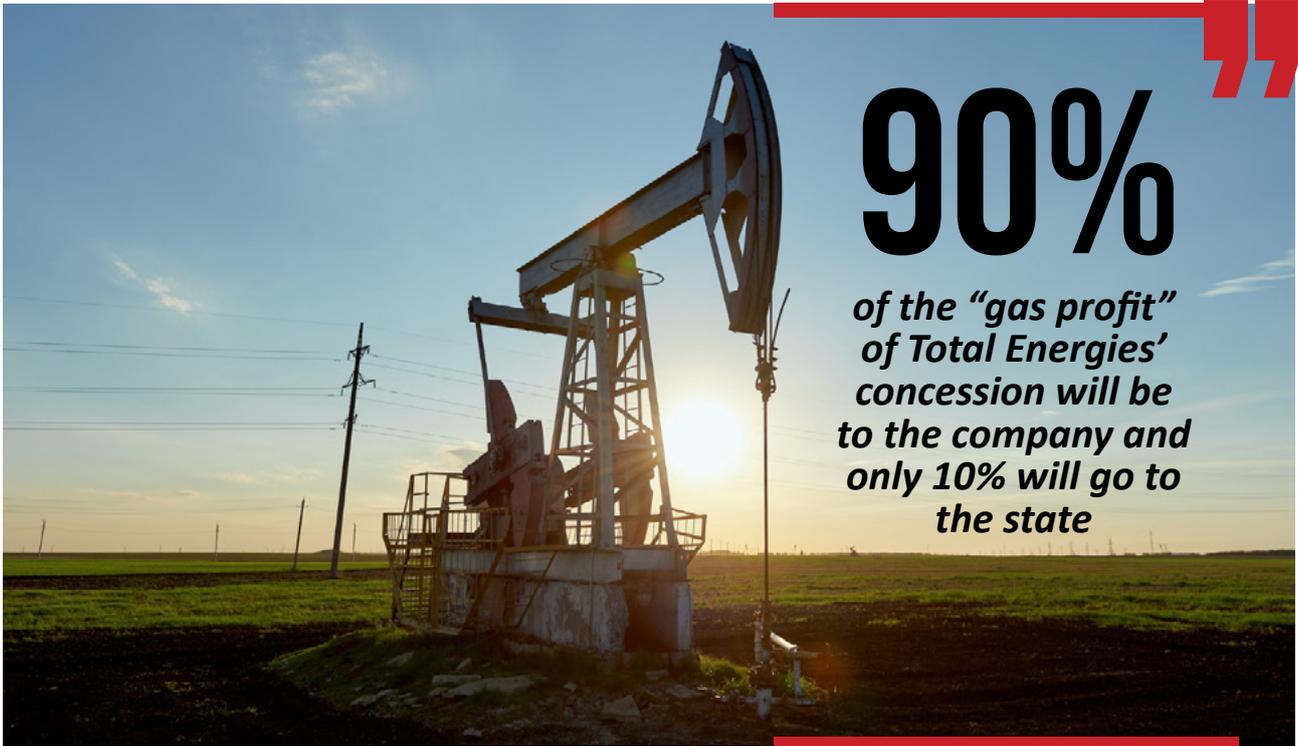
Source: Sinoia et al. (2023)⁵⁶

The current fiscal regime applied to the hydrocarbon sector is recognized as progressive, as it allows the government to collect more and more revenue over the production period of petroleum projects. However, a significant number of the contracts in the oil and gas sector were signed long before the approval of this regime and contain provisions that hinder revenue collection. This applies to royalties, CIT and production sharing agreements. For instance, in terms of royalties, while it is generally assumed that the royalty rate for natural gas production in Mozambique is 6%, as illustrated in the table below, the contracts signed before the entry into force of Law no. 12/2007 of 27 June benefit from reduced rates, some as

54. Other sources of state revenue include Production Bonuses and commitments from the companies regarding Institutional Support, Training, and Social Investment. I2A Consultoria e Serviços. (2023). Independent Report of the Extractive. Industry Transparency Initiative: Year 2020. <http://www.itie.org.mz/download/decimo-relatorio-itie-mocambique-english/?wpdmdl=3385&refresh=63fa77d20135b1677359058>

55. Sinoia, D., Manguela, G., & Langa, N. (2023). Fair and Efficient Taxation: A Way to Break the Natural Resource Curse in Mozambique? Center for Democracy and Development, Oxfam Novib, & Tax Justice Network Africa.

56. Sinoia, D., Manguela, G., & Langa, N. (2023). Fair and Efficient Taxation: A Way to Break the Natural Resource Curse in Mozambique? Center for Democracy and Development, Oxfam Novib, & Tax Justice Network Africa.



low as 2%, undermining the revenue collected from this source. In terms of CIT, generally the rate in Mozambique is fixed at 32%. However, in the case of oil operations, the government offered wasteful incentives starting in early 2007, including a reduction in the CIT rate to 24% for the first eight years of production. Given the wide range of deductions allowed, CIT has a limited impact on state revenue in the early years of production.⁵⁷ Regarding production sharing agreements, which rely on R factor, the first years of production benefit oil operators. For example, in the first years of production, 90% of the “gas profit” of Total Energies’ concession will be to the company and only 10% will go to the state. Only in the long term will the gas profit be divided equally, or a relatively larger portion will go to the state.

Table 3. Revenue sources for petroleum operations⁵⁸

Revenue source	Sasol	Total Energies	ENI	Statoil	Petronas
Royalty Rate	5%	2%	2%	2%	6%
Income Tax Rate	17,5% – 35%	24%–32%	24%–32%	24%–32%	32%

Source: Sinoia et al. (2023)

Table 4. Percentage of revenue destined for the State in the Production Sharing Agreement

R-Factor Scale	Total Energies	ENI	Statoil	Petronas
R < 1	10%	15%	10%	10%
R 1- 2	20%	25%	20%	25%
R 2-3	30%	35%	30%	50%
R 3-4	50%	45%	40%	60%
R 4+	60%	55%	50%	70%

Source: Sinoia et al. (2023)

This is why it is usually said that the fiscal regime governing the lion’s share of Mozambique’s riches in the oil and gas sector

⁵⁷ *Ibid.*

⁵⁸ The table is compiled considering the original operators and partners of the contracts.

is heavily backloaded: the state will receive its share of the overall revenue only much later in the production schedule.⁵⁹ All terms affecting the revenue-allocation schedule (royalties, cost recovery limits and R-factor scales) are heavily skewed in favor of the oil companies in the first years of operations.

2) Mining sector

The taxation of mining operations in Mozambique is governed by the Specific Tax Regime and Tax Benefits approved by Law nº 28/2014, of 23 September. This regime's provisions officially took effect on January 1, 2015, encompassing both individuals and legal entities engaged in mining activities within the national borders.⁶⁰ The regulation of this scheme was approved by Decree number 28/2015, of 28 December, which entered into force on 1 January 2016. These regulations repealed the previous instruments that determined the rules of taxation in the mining area, namely the Laws number 11 and 13/2007 and Decree number 5/2008. It should be noted that Law number 24/2014 has been updated by law number 15/2017, of 28 December, as previously indicated.

Table 5. Summary of the specific tax and fiscal benefits regime for mining activities

Tax on Mining Production (royalties)⁶¹	Transfer taxes and capital gains
Calculated (monthly) based on the value of the mineral extracted. The royalty rate varies across minerals: <ul style="list-style-type: none"> 1) Diamonds: 8% 2) Precious metals, precious and semi-precious stones, and heavy sand: 6% 3) sands and stone: 1.5% 4) Base minerals, coal, ornamental rocks, and other mineral products: 3% <p>Note: A 50% reduction is foreseen in the law for mining products used in the development of local industry.</p>	The transfer of mineral rights or licenses is subject to a 32% capital gains tax.
	Distinction between domestic and foreign parties
	There is not any distinction between the duties, royalties, and taxes payable by domestic parties and those payable by foreign parties.
	Specific income tax rules
Surface Tax	The CIT rate is the same as the general tax system (32%). But the regime provides for specific income tax rules.
Calculated in accordance with the fixed amount per hectare (ha) of land included in the mining title. The amount is payable annually in meticaís per hectare and ranges from 17,50 MT/ha to 210,00 MT/ha	Fiscal stability agreements
Windfall profits tax	With a maximum duration of 10 years, which may be extended until the term of the concession in exchange for a 2% annual increase in the production tax rate.
Mining concessions or mining certificates with a pre-corporate income tax net return in excess of 18% are subject to a windfall profits tax levied on the accumulated net cash flow. The statutory rate of the windfall profits tax is set at 20%.	

Source: Sinoia et al. (2023)

As in the hydrocarbon sector, mining entities operating in the country are also required to comply with both the general tax regime and the Specific Tax Regime and Tax Benefits for Mining Activities.⁶² While the general tax regime mainly provides for a profit-based tax (CIT payable at a rate of 32%), the special regime establishes the basis for a tax mix that favors production-based revenue-raising mechanisms. These include: the Tax on Mining Production (IPM), the Surface Tax (ISS)

59. Manguela, G. (2023, 19 February). *Condicionalismo de custos é um falso argumento que a TotalEnergies quer usar para atrasar a retoma do projecto Mozambique LNG*. Centro para Democracia e Desenvolvimento. https://cddmoz.org/wp-content/uploads/2020/07/Condicionalismo_de_custos_e_um_falso_argumento_que_a_TotalEnergies_quer_usar_para_atrasar_a_retoma_do_projecto_Mozambique_LNG1.pdf

60. I2A Consultoria e Serviços. (2022). Independent Report of the Extractive Industry Transparency Initiative – Year: 2020. *Extractive Industries Transparency Initiative*. https://eiti.org/sites/default/files/2023-01/ITIE%20Moc%CC%A7ambique_10o%20Relato%CC%81rio_ENG_1.pdf

61. The specific taxes for the mining sector are not deductible for the basis of the CIT

62. Law no. 28/2014 of 23 September, in force since January 2015.



and the Tax on Mining Resources Income. The combination of production-based revenue-raising mechanisms and profit-based taxes results in a regular flow of tax revenue for governments over the entire life of the projects in the mining industry, even at the early stages of a mine's life cycle, when there is no profit.

3.2.3 Mozambique's tax treaties and their impact on revenue collection

Mozambique has signed 10 tax treaties (see the table below), two of which (with Botswana and Ethiopia) are not yet ratified, and is presently negotiating additional tax treaties, including with the Netherlands and Turkey.⁶³ As is the case in other developing countries, Mozambique's tax treaty network is severely abused by multinationals in treaty shopping schemes. Some of its Double Taxation Agreements (DTAs) are very restrictive. Unsurprisingly, most of the country's foreign investment comes from well-known tax havens that enable multinational enterprises

to set up letterbox companies to take advantage of its tax treaties and avoid taxes in Mozambique.⁶⁴

As depicted in table 6, by opening letter box companies in tax havens with signed DTAs with Mozambique, multinationals, predominantly from the extractive sector, abuse the restrictive provisions in the agreements to avoid paying their fair share of taxes. Most of the provisions of the DTAs that the country has with the tax havens follow an outdated model from the OECD that favors the residence country for tax rights at the expense of the countries where the economic activity takes place. As outlined in the table below, reduced rates of withholding taxes (for dividends, interest, and royalties), no withholding taxes on service fees, unfavorable definitions of "permanent establishment", and capital gains tax avoidance through offshore indirect transfers are some of the main clauses of the DTAs that multinational companies use to lower their taxes.⁶⁵

63. <https://cddmoz.org/wp-content/uploads/2020/07/Acordos-de-Dupla-Tributacao-1-1.pdf>

64. *Ibid.*

65. Van Teeffelen, J., Sinoa, D., East, S., & Langa, N. (2023). How Mozambique's tax treaties enable tax avoidance. Centre for Research on Multinational Corporations and Center for Democracy and Development. <https://www.somo.nl/wp-content/uploads/2023/03/How-Mozambiques-tax-treaties-enable-tax-avoidance1.pdf>

Table 6. List of Mozambique’s tax treaties and the contents of key articles⁶⁶

Count		Maurit	United Emirat	Italy	South	Portug	Macac	India	Vietna	Botsw	Ethiop
Treaty article	Year ratified	1999	2005	2005	2009	2010	2011	2012	2012	Not yet ratified	Not yet ratified
5(3)(a)	Construction PE (months)	6	12	6	6	6	6	12	6	6	6
5(3)(b)	Service PE (months)	6	9	No	6	6	6	9	6	6	6
10	WHT on dividend	8% (15%) ²⁷	0%	15%	8% (15%) ²⁸	10%	10%	7.5%	10%	0% (12%) ²⁹	10%
11	WHT on interest	8%	0%	10%	8%	10%	10%	10%	10%	10%	10%
12	WHT on royalties	8%	0%	10%	5%	0%	10%	10%	10%	10%	10%
12a	WHT on technical service fees	No	No	No	No	No	No	No	10%	10%	15%
13(4)	Capital gains – immovable property	No	Yes	No	Yes	Yes	No	Yes	Yes	No	No
13(5)	Capital gains – movable property	No	No	No	No	Yes	No	Yes	No	No	Yes
29	General anti-abuse rule	No	No	No	No	No	No	PPT	No	No	PPT

Red indicates the treaty article is not in line with the UN model, in the case of WHT it means a reduction by more than half of Mozambique's statutory 20% WHT rate.

According to ICTD’s database⁶⁷, of the eight treaties in force in Mozambique, six are classified as very restrictive⁶⁸, namely: Macau, Mauritius, Portugal, South Africa, the United Arab Emirates, and Italy, in ascending order of the level of restriction. The treaties with these countries increase the vulnerability of the Mozambican tax system to aggressive tax planning and limit the country’s ability to protect tax rights in terms of protection against tax abuse and protection of its tax rights. According to the trends of FDI flows to the country in the last years, the tax havens of Mauritius, and the United Arab Emirates are the preferred ones for multinational companies when it comes to aggressive fiscal planning to avoid taxes through DTAs. These two countries are currently the largest foreign investors in Mozambique, with 70% of the country’s total foreign investment. These countries – also referred to as investment hubs or offshore financial centers⁶⁹, enable multinational corporations to easily set up letterbox companies and offer a large network of favorable tax treaties and other tax benefits (such as an absence of withholding taxes or corporate income tax).⁷⁰

A recent report by SOMO and CDD⁷¹ exposed concrete cases of multinational companies that avoid paying their fair share of taxes through the abusive application of tax treaties that Mozambique has entered into with the tax havens of Mauritius and the United Arab Emirates (UAE)⁷². These include five gas and mining companies – Total Energies, Eni, and Vale – which will be responsible for between USD 1.4bn and USD 2.1bn in Mozambican tax evasion. Similarly, companies in the mining sector – Gemfields’ Montepuez mine, Kenmare’s Moma mine, and the Nacala Logistics Corridor – use treaty shopping to avoid paying taxes to the Mozambican government, with these three operations accounting for an estimated \$ 116.7 million in lost Mozambican tax revenues in recent years.

Overall, it’s estimated that because of its tax treaties with tax havens Mauritius and the United Arab Emirates (UAE), in 2021, Mozambique lost \$ 315 million just in withholding taxes on interest payments and dividends⁷³. This is 7.4% of the country’s total tax revenue of that year, which could have been spent on basic social expenditures or even to finance the concretization of the country’s NDCs. There are no doubts: Mozambique tax treaty network is a major leak for tax revenue

66. Van Teeffelen, J., Sinoia, D., East, S., & Langa, N. (2023). How Mozambique’s tax treaties enable tax avoidance. Centre for Research on Multinational Corporations and Center for Democracy and Development. <https://www.somo.nl/wp-content/uploads/2023/03/How-Mozambiques-tax-treaties-enable-tax-avoidance1.pdf>

67. Hearson, Martin (2021). Tax Treaties Explorer [Online database], Brighton: International Centre for Tax and Development (ICTD). <https://www.treaties.tax>

68. Following the methodological approach developed by ActionAid in the Mistreated Reports (2016), the classification is based on a labelling system in which a score of 0.47 or below is considered “Very restrictive”. Read more: <https://actionaid.org/publications/2016/mistreated>

69. The UAE has been ranked as the 10th worst tax haven worldwide in the Tax Justice Network’s Corporate Tax Haven Index, while Mauritius ranks 15th.³⁰ The UAE has signed 137 tax treaties with countries across the globe.

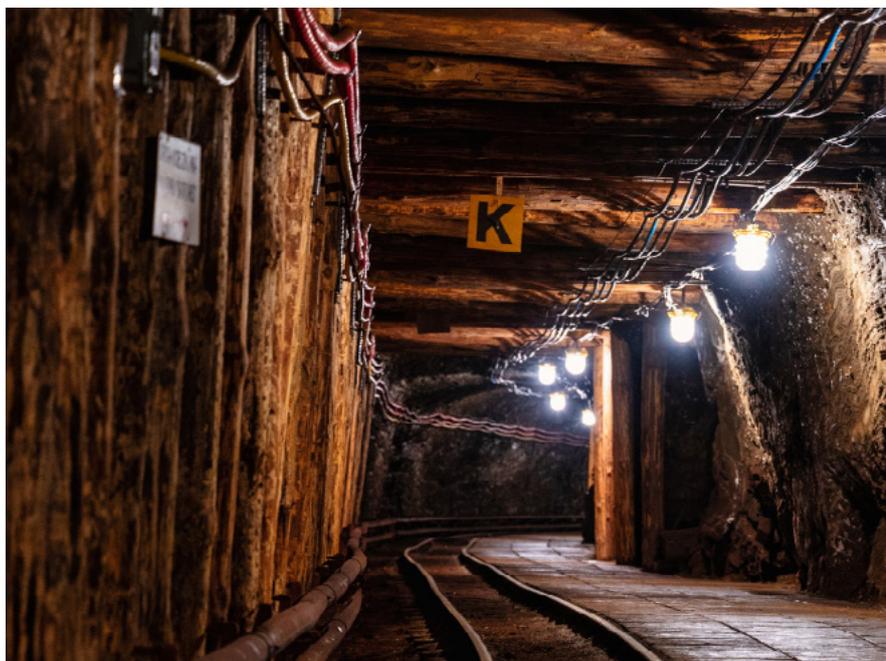
70. Abu Dhabi Global Market, “ADGM recognised as an attractive and tax efficient aircraft financing and leasing hub for the region”, 30 September 2017, accessed 16-01-2023, <https://www.adgm.com/media/announcements/adgm-recognised-as-an-attractive-and-tax-efficient-aircraft-financing-and-leasing-hub-for-the-region>.

71. SOMO and CDD. (2023). The treaty trap: tax avoidance in Mozambique’s extractive industries – The miners. Centre for Research on Multinational Corporations and Center for Democracy and Development. <https://www.somo.nl/wp-content/uploads/2023/07/The-treaty-trap-tax-avoidance-in-Mozambiques-extractive-industries-the-gas-companies.pdf>

72. CDD/SOMO DTA cases reports

73. Van Teeffelen, J., Sinoia, D., East, S., & Langa, N. (2023). How Mozambique’s tax treaties enable tax avoidance. Centre for Research on Multinational Corporations and Center for Democracy and Development. <https://www.somo.nl/wp-content/uploads/2023/03/How-Mozambiques-tax-treaties-enable-tax-avoidance1.pdf>

In 2021
Mozambique lost
\$315M
to withholding
taxes on interest
payments and
dividends



in the country. Fortunately, due to the advocacy work being led by CDD and its partners, there's already a national consensus, backed by political will, to move forward with the revision of the restrictive DTAs and unlock greater DRM in the extractive sector.

3.2.4 Illicit Financial Flows in the Extractive Industry

In Mozambique, as in many developing nations, the extractive industry's fiscal contribution also faces a formidable challenge in the form of Illicit Financial Flows (IFFs). These flows present a significant hurdle to Mozambique's development⁷⁴ by diverting critical resources that could otherwise catalyze sustainable economic growth, job creation, poverty reduction, addressing climate change, and other challenges the country faces.

Despite the lack of precise and updated data on the proportion of IFFs originating from Mozambique's extractive industry, the sector is often identified as fertile ground for such practices to flourish.⁷⁵ These practices are pursued through a range of channels, which including tax base erosion and profit shifting (BEPS) and abuse of transfer pricing. Tax Base Erosion and Profit Shifting (BEPS) and the abuse of transfer pricing are increasingly emerging as critical concerns within the extractive industry. These practices, while not inherently illegal, have profound implications for domestic resource mobilization, exacerbating the challenge of IFFs and the widening of the tax gap.

A. Tax Base Erosion and Profit Shifting (BEPS) & Abuse of Transfer Pricing

BEPS refers to a set of strategies employed by multinational corporations (MNCs) to exploit gaps in tax regulations and transfer pricing⁷⁶ norms, thereby shifting profits to jurisdictions with lower or no taxes. Capitalizing on the fact that the extractive industry involves high-value commodities and complex supply chains, the multinational companies employ BEPS strategies in tax avoidance schemes, leading to substantial revenue losses.

Tax Justice Network⁷⁷ reports that, overall, Mozambique loses up to USD144,3 million in taxes per year to international tax abuses, about 5% of tax revenues collected. Of the USD144 million, almost \$124 million is lost to multinational companies shifting their profits to tax havens in order to understate how much profit they have actually made in the country where they do business and consequently pay less tax than they should.

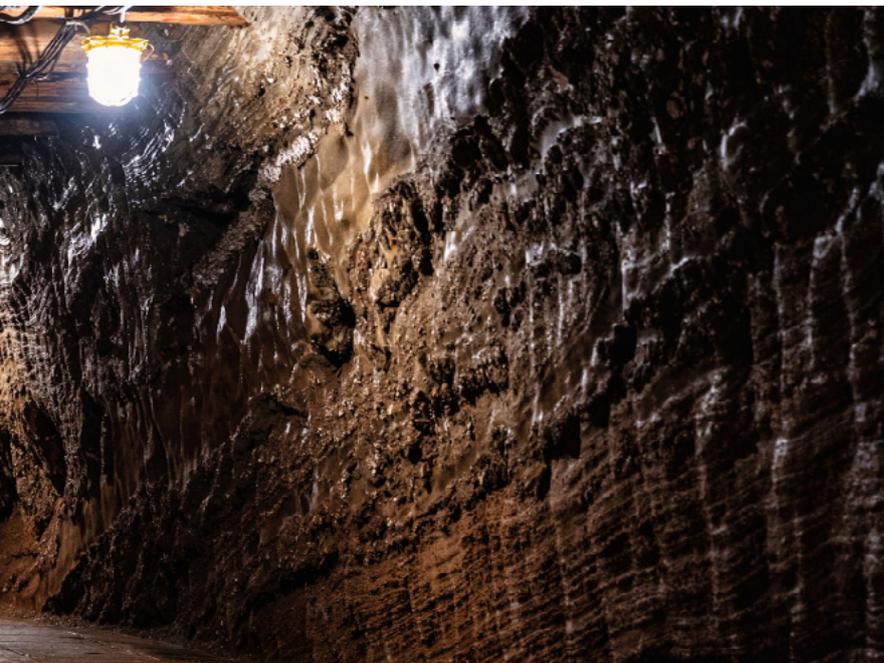
The revenue authority acknowledges the difficulty in controlling illicit financial flows (IFFs) arising from transfer pricing. Indeed, according to the information gathered from key informants, this issue represents the upcoming tax loophole that the government aims to tackle in the near future. More specifically, the focus is on reinforcing the existing legal framework on transfer pricing to make it operational. The current transfer pricing regime was approved by Decree No. 70/2017, of December 6, which regulates transfer pricing practiced in commercial and financial operations, involving related entities. However, due to the superficial nature of the legal instrument and

74. Kukutschka, R.M.B. (2018). Illicit financial flows in Mozambique. U4 Helpdesk Answer. <https://www.u4.no/publications/illicit-financial-flows-in-mozambique.pdf>

75. *bid*

76. Transfer pricing refers to the pricing of goods, services, or intangible assets transferred within a multinational corporation or between related entities.

77. Tax Justice Network Database – <https://taxjustice.net/country-profiles/mozambique/>



**Between 2004 & 2013
Mozambique lost an
average of**

\$240M

**each year in illicit financial
outflows related to trade
misinvoicing**

lack of clear rules, the revenue authority has been facing challenges to effectively enforce it. This legal deficiency has been capitalized by multinational companies, especially from the mining sector, to reduce the tax obligation.⁷⁸

B. Trade mispricing

Adulterated commercial invoicing stands out as a focal point in research concerning IFFs, capturing significant attention due to its widespread visibility. This category of practices revolves around the deliberate manipulation of trade invoices for both imports and exports, orchestrated with the intention to either mislead tax authorities or manipulate markets. The spectrum of motives behind such practices is broad, encompassing efforts to avoid payment of customs duties and domestic tariffs on traded commodities, as well as strategies aimed at channeling foreign exchange overseas.⁷⁹

The last GFI report⁸⁰ found that between 2004 and 2013, overall, Mozambique lost, on average, more than USD 240 million each year in illicit financial outflows related to trade misinvoicing⁸¹. The Mozambican government is

not oblivious to these illicit activities in the industry and is actively putting measures into effect to counteract the resulting revenue losses. As a recent development stemming from these endeavors, the Mozambican government has taken a groundbreaking step by imposing fines on 14 mining companies that failed to accurately declare the quality of the ores they extracted, a strategy employed to evade taxes.⁸² This imposition of fines aligns with a novel regulation within the mining sector (Ministerial Diploma no. 91/2023 dated 16 June - Reference Price Regulation), which focuses on documentary inspection of quality and quantity to determine the value of the mining products, allowing a reliable calculation of the price and the tax to be paid to the State.⁸³

While recent regulatory developments are a step towards ensuring an equitable distribution of taxes for the State, Mozambique still lacks a robust institutional framework for effective operationalization.⁸⁴ An immediate and crucial imperative lies in the investment towards enhancing the monitoring process, accurately determining production volumes, assessing mineral quality, and enhancing overall transparency within the process of valuing mining products. This comprehensive approach is indispensable

78. According to the tax authority, due to the structure of the projects in the hydrocarbon sector (involving multiple companies that provides a kind of checks and balances to the operations of the consortium), the challenge of transfer pricing is not a major concern in the gas industry.

79. TJNA. (n.d). Curbing Illicit Financial Flows and Tax Injustice in Africa. Tax Justice Network. <https://taxjusticeafrica.net/sites/default/files/publications/Curbing%20IFFs%20and%20Tax%20Injustice%20in%20Africa%20%28English%29.pdf?fbclid=IwAR168wZ1i93sr3ckogveA20oqn-4n087etTgUM4aVr6su58c9KxNIC8YMgA>

80. GFI (2015): Illicit Financial Flows from Developing Countries: 2004-2013, https://www.gfintegritty.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf

81 This estimates only covers misinvoicing of goods trade.

82. Diário Económico. (2023, July 26). Governo Multa 14 Mineradoras Por Falta de Declaração da Qualidade de Minérios [Government Fines 14 Mining Companies for Failing to Declare Ore Quality]. <https://www.diarioeconomico.co.mz/2023/07/26/oilgas/extractivas/governo-multa-14-mineradoras-por-falta-de-declaracao-da-qualidade-de-minerios/>

83. MEF. (2023, June 18). Nota de Imprensa [Press release]. Ministry of Economy and Finance. <https://www.mef.gov.mz/index.php/imprensa/anuncios-e-comunicados/1909-18062023-nota-de-imprensa-precos-de-referencia-mineiros/file>

84. Mate, R. (2023, July 11). Preço de Referência - Regulamento Insuficiente para Combater a Subfaturação no Sector Extractivo [Reference Price – Insufficient Regulation to Combat Under-invoicing in the Extractive Sector]. Center for Public Integrity. <https://www.cipmoz.org/pt/2023/07/11/preco-de-referencia-regulamento-insuficiente-para-combater-a-subfaturacao-no-sector-extractivo/>



**Mega projects from
the extractive sector
contribute more than**

200M

**to the state coffers
(more than 5% of the
total revenues)**

for combating under-invoicing, curbing tax evasion, and maximizing the advantages derived from the exploitation of mineral resources for greater DRM in the extractive sector.

3.3. Can Domestic Revenue Mobilization (taxes) from the extractive sector meet the country's climate finance needs?

As stated in previous subsections, the mega-projects from the extractive sector currently contribute more than USD 200 million to the state coffers, more than 5% of the total revenues. This represents only 0.0026% (yearly) of the approximately USD 7,586 billion that the country needs for its adaptation and mitigation actions until 2025. If this contribution will not change substantially, at least in the short in medium term⁸⁵, this implies that even if all revenues generated from the extractive sector, between 2020 and 2025, were allocated towards financing the country's NDCs, there would still be a substantial shortfall in funding.

The windfall of USD 90 billion that is expected from the LNG projects in the Rovuma Basin after the 2030s will certainly increase the currently restricted fiscal space, providing more room for Mozambique to expand the quality and quantity of its expenditure, even to meet the country's climate financing needs. However, at least two challenges

emerge. The first one is that climate financing is not yet the top priority of government spending. This stems from a combination of challenges, including the fact that the country is struggling with mounting debt that has been recurrently deviating resources from social sectors and the urgent need for investments to improve the lives of the more than 16 million Mozambicans who live below the poverty line. It's not surprising that the budget doesn't have clear lines to finance the achievement of the country's NDCs nor does it effectively integrate climate change in its financial decisions.⁸⁶

The second is related to the new paradigm of revenue-management from the extractive sector, particularly for the LNG revenues, in Mozambique. As discussed in Box 1, Mozambique is about to create a sovereign wealth fund to manage the revenues that are expected from the LNG projects in the Rovuma basin. According to the proposed Act, with pending approval from the parliament, the proposal establishes that during the first 15 years, 60% of the collected revenues will go to the State Budget and the remaining 40% to the sovereign wealth account (rules would change to a 50%/50% distribution after the sixteenth year of operation).

In these conditions, the eventual climate financing needs

85. According to government projections, greater inflows from the Rovuma Basin LNG are only expected after 2030s. Ministry of Economy and Finance. (2023). Medium-Term Fiscal Scenario. <https://www.mef.gov.mz/index.php/todas-publicacoes/instrumentos-de-gestao-economica-e-social/cenario-fiscal-de-medio-prazo-cfmp/cfmp-2024-2026/1912-cfmp-2024-2026/file?force-download=1>

86. Government of Mozambique. (2021). Update of the First Nationally Determined Contribution to the United Nations Framework Convention: Mozambique (2020-2025). https://unfccc.int/sites/default/files/NDC/2022-06/NDC_EN_Final.pdf

would be met by the 60% that will be channeled to the State Budget, in line with the country's National Development Strategy (NDS). This means that the strategy, currently in revision, should be the first document to clearly integrate the country's climate financing needs, which would then trickle down to the yearly state budgets. There is a need to mainstream climate considerations in the Budgeting process. To enable future monitoring of climate change expenditure and execution, the Mozambican government should develop a functional set of codes to be included in the national budget.

Overall, it can be said that DRM from the extractive industry, mainly after the 2030s, has indeed potential to contribute to the climate financing needs of the country. However, even if the challenges of the leaks in the form of IFFs and restrictive DTAs were addressed, considering the current composition of the public expenditure, climate finance needs rank, at best, in the third position, after the mounting debt and much-needed social expenditures to improve the lives of Mozambicans currently facing privation contexts.

3.4 The impact of the global climate agenda on DRM in the extractive sector in Mozambique (e.g. prospects for the coal, oil, and gas industries; EU CBAM - implications for the aluminum industry)

The global climate agenda is likely to exert significant influence on Mozambique's exports from the extractive sector. As the world intensifies efforts to combat climate change and transition towards more sustainable practices, several key dynamics are likely to impact the extractive sector and subsequently, Mozambique's revenue collection.

1) Climate-Related Trade Policies: The Case of EU's Carbon Border Adjustment Mechanism

The Carbon Border Adjustment Mechanism (CBAM) is a proposal by the European Union to impose a carbon tax on selected imports as part of the goal to become climate neutral by 2050 and reduce greenhouse gas emissions by 55% by 2030 compared to 1990 levels.⁸⁷ The CBAM is designed to avoid carbon leakage, which is the risk that EU producers will move their activities to countries with lower environmental standards, or that EU consumers will buy cheaper imports from these countries. It is to be applied to imports of selected carbon intensive imports such as cement, iron and steel, aluminum, fertilizers, electricity and hydrogen. The CBAM is set enter into force in its

transitional phase from October 1, 2023, and would be gradually implemented until 2035.

Mozambique stands out as one of the select nations exhibiting considerable vulnerability to the impacts of the CBAM, as depicted in the Figure below. Specifically, Mozambique is one of the countries that could be most affected by CBAM, as it is a major exporter of aluminum to the EU. Aluminum accounts for 25% of the country's export earnings, totaling USD1.4 billion annually. Aluminum is produced by the Mozal smelting plant, which is supplied by South African electricity⁸⁸. Due to South Africa's reliance on coal-based electricity supplies, Mozambique's aluminum exports could be subject to an annual CBAM fee in the order of €350 million per year, which could lead to a reduction of more than 60% of Mozambican exports to the EU and a 2.5% decrease in GDP.⁸⁹

In practice, not all USD1.91 billion are in jeopardy. It's expected that the implementation of CBAM will lead to unintended consequences such as the diversion of Africa's trade with Europe to other regions provided African countries negotiate adequate trade arrangements with other geographies such as China to promote their market access further. For instance, estimates indicate that Mozambique, which is essentially sensitive because of its aluminum exports to the EU, will only suffer costs equivalent to 0.07% of its GDP as the commodity exports are diverted toward other markets.⁹⁰ Key informants showed some

Aluminum accounts for 25% of the country's export earnings, totaling USD1.4 billion annually.



degree of understanding of the measure, but disregarded its potential implications. The prevailing perception is that the export diversification away from the European market will prevent major losses for the country.

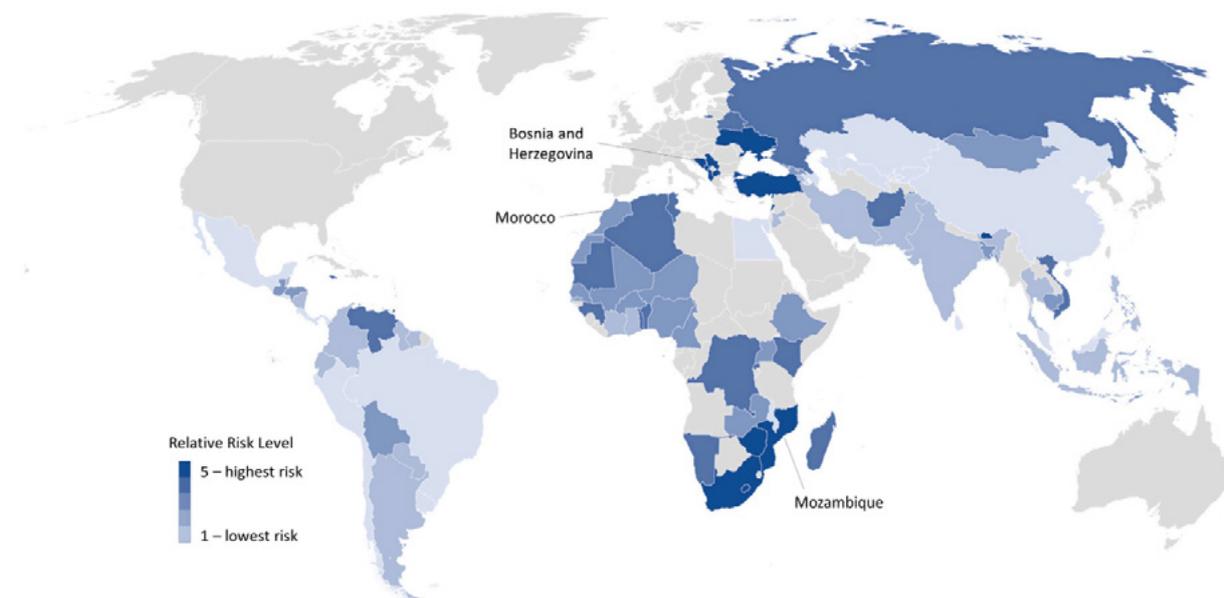
87. Maryla Maliszewska, Maksym Chepeliev, Carolyn Fischer, Euijin Jung (2023). How Developing Countries Can Measure Exposure to the EU's Carbon Border Adjustment Mechanism. <https://blogs.worldbank.org/trade/how-developing-countries-can-measure-exposure-eus-carbon-border-adjustment-mechanism>

88. <https://clubofmozambique.com/news/mozal-wants-to-use-power-generated-in-mozambique-aim-233285/>.

89. Elizabeth Khumalo. (2022). EU Carbon Border Adjustment Mechanism – Friend or foe for Mozambique Aluminium Exports. <https://furtherafrica.com/2022/11/11/eu-carbon-border-adjustment-mechanism-friend-or-foe-for-mozambique-aluminium-exports/>

90. African Climate Foundation and The London School of Economics and Political Science. (2023). Implications For African Countries of a Carbon Border Adjustment Mechanism in the EU. <https://www.lse.ac.uk/africa/assets/Documents/AFC-and-LSE-Report-Implications-for-Africa-of-a-CBAM-in-the-EU.pdf>

Figure 3. Map of global vulnerability to CBAM



Source: Eicke et al., 2021⁹¹

Mozambique’s risk level is fundamentally driven by a low statistical capacity to prove emissions – i.e., insufficient data or resources to effectively demonstrate or provide concrete evidence of the carbon content of its exports.⁹² The country’s carbon intensity of the total final energy consumption (TFEC) is 64% less carbon-intensive than the EU average⁹³. Thus, the country’s ability to adapt to an EU CBAM mostly depends on the ability to monitor, report, and verify the currently comparatively low emissions intensity of its products. Whether payments under a CBAM are based on benchmarking or embodied emissions, a lack of statistical capacity to prove its lower carbon intensity could have severe economic consequences.

2) Demand for Clean Technologies and Minerals: The case of Graphite

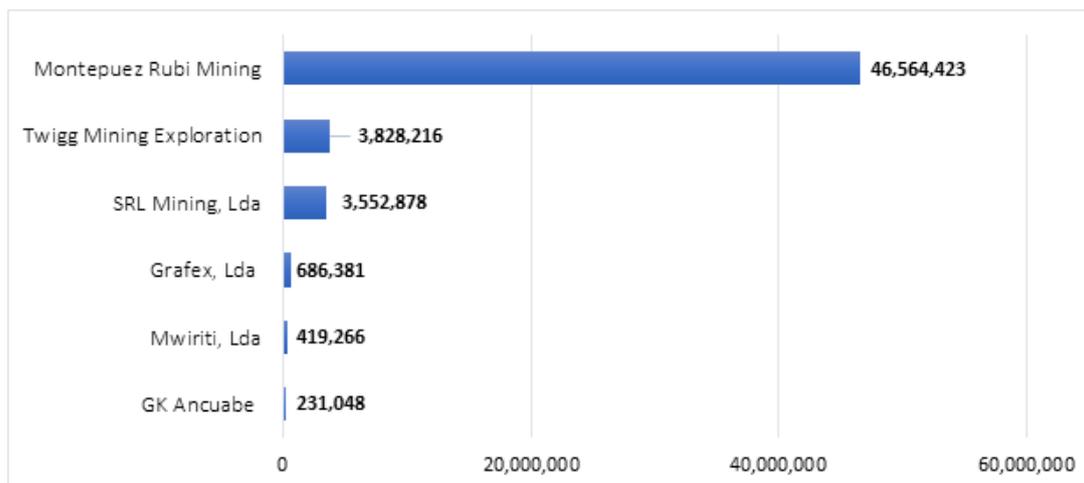
The global push towards renewable energy and electric mobility is increasing the demand for minerals like lithium, cobalt, and rare earth elements, which are vital for manufacturing batteries and clean energy technologies. According to the World Bank, the production of

transitional/green minerals is likely to increase by nearly 500% if investment in renewable energy and other green technologies is increased in order to meet the global net zero targets required to avoid the worst impacts of climate change.⁹⁴

Backed by its vast mineral resource wealth, Mozambique is prepared to capitalize on the emerging opportunities in the transitional minerals market. The nation, known for harboring the planet’s largest reserves of natural and high-quality graphite⁹⁵, has ascended to secure its position as the second-largest global producer of this increasingly indispensable mineral⁹⁶. With other relatively small players like Madagascar, Namibia, and Tanzania, Mozambique’s mining activities are positioning the continent as an emergent focus for graphite exploration at the global level. This is just the result of two projects: Germany-based Kropfmuhl, through its subsidiary *GK Ancuabe Graphite Mine Sociedade Anônima*, and Sydney-based Syrah Resources, also through a Mozambican subsidiary known as Twigg Mining & Exploration Lda.

91. GFI (2015): Illicit Financial Flows from Developing Countries: 2004-2013, https://www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final-1.pdf
 92. Eicke, L., Weko, S., Apergi, M., & Marian, A. (2021). Pulling up the carbon ladder? Decarbonization, dependence, and third-country risks from the European carbon border adjustment mechanism. *Energy Research & Social Science*, 80, 102240. <https://doi.org/10.1016/j.erss.2021.102240>
 93. *Ibid.*
 94. *Africa’s mineral resources are critical for the green energy transition- SAIIA* <https://saiia.org.za/research/africas-mineral-resources-are-critical-for-the-green-energy-transition/>
 95. U.S. Geological Survey, 2022, Mineral commodity summaries 2022: U.S. Geological Survey, 202 p., <https://doi.org/10.3133/mcs2022>.
 96. Mining Technology. (2023, June 28). Graphite production in Mozambique and major projects. <https://www.mining-technology.com/data-insights/graphite-in-mozambique/#catfish>

Graph 7. Main fiscal contributors from Cabo Delgado’s extractive industry (2022) – in US dollars



Source: Provincial Government of Cabo Delgado⁹⁷

Most of the country’s graphite is found in Cabo Delgado, one of the country’s northernmost provinces. Mining companies, predominantly listed in Australia, have eagerly ventured into the region to capitalize on the abundant and valuable deposits in Mozambique. Triton Minerals, Mustang Resources, Battery Minerals, and Syrah Resources are some of the main companies and all are listed on the Australian Stock Exchange. Leveraging on the reserves of this province, in 2022, Mozambique was estimated to be the world’s second-ranked producer of graphite, accounting for more than 13% (170,000 tons) of the world’s production, according to U.S. Geological Survey statistics⁹⁸. The production is exports-oriented, most notably to Germany, China, and India, as shown in the graph below based on the last update (for 2021⁹⁹) provided by the Observatory of Economic Complexity (OEC).

As it was established in previous sections, notwithstanding the challenges in terms of the prevailing tax leaks, Mozambique’s fiscal system applied to mining operations¹⁰⁰ provides for a combination of production-based and profit-based revenue-raising mechanisms that results in a regular flow of tax revenue for the government over the entire life of the projects in the mining industry, even at the early

stages of a mine’s life cycle where there’s no profit.¹⁰¹ With the existing legal and institutional framework, in less than decade of operations, the graphite mining operations in Cabo Delgado have channeled millions of dollars to the Mozambican governments in taxes. In fact, during 2022, the graphite projects were in the list of main fiscal contributors from Cabo Delgado’s extractive industry, as illustrated by the graph above.

In summary, it goes without saying that the global climate agenda will impact Mozambique’s extractive sector significantly. The EU’s Carbon Border Adjustment Mechanism (CBAM) presents a notable challenge, particularly for Mozambique’s aluminium exports to the EU. This could result in a substantial annual CBAM fee, potentially reducing exports by over 60% and impacting GDP. However, diversifying exports to other regions could mitigate losses. Mozambique’s ability to adapt to CBAM depends on its statistical capacity to prove lower emissions intensity. On a positive note, the demand for minerals like graphite is crucial for clean energy technologies, offers opportunities for increased tax collection and DRM since Mozambique is an emerging major global producer.

97. The information was shared in a session of the Development Observatory on April 2023

98. U.S. Geological Survey, 2023, Mineral commodity summaries 2023: U.S. Geological Survey, 210 p., <https://doi.org/10.3133/mcs2023>.

99. For the sake of consistency, this data should pertain to the year 2022. However, the authors were unable to obtain disaggregated and comprehensive database on Mozambique’s exports of graphite.

100. Specific Tax Regime and Tax Benefits for Mining Activities – Law nº 28/2014 of 23 September, amended by Law No. 15/2017 of 28 December.

101. Sinoia, D., Manguela, G., & Langa, N. (2023). Fair and Efficient Taxation: A Way to Break the Natural Resource Curse in Mozambique? Center for Democracy and Development, Oxfam Novib, & Tax Justice Network Africa.

4 Conclusions & Recommendations

This report examined the nexus between Mozambique's climate finance needs, and the opportunities and challenges for DRM through taxing Mozambique's extractive sector. The climate shocks experienced by Mozambique highlight the inequalities associated with the global climate crisis, where low-income countries are among the most affected by climate change while contributing the least to carbon emissions. The report shows the need for continued global advocacy for the materialization of the climate finance commitments made by rich countries.

The report finds that Mozambique faces severe climate challenges due to its vulnerability to natural disasters. The increased frequency of tropical cyclones, floods, storms, and droughts has caused devastating effects for the population, including the loss of lives, destruction of infrastructure and debilitation of basic service provision. Mozambique's climate agenda, as outlined in its Nationally Determined Contribution (NDC), aims to address these challenges, greenhouse gas emissions and build resilience. However, the country faces substantial financial constraints to realizing this. While the projected costs of mitigation, adaptation, and resilience building are mounting, the state budget still fails to clearly make provisions to fund the country's NDC. Also worth noting is that the climate change dimension is yet to be mainstreamed into the planning and budgeting process. Moreover, the financial instruments popularly understood as the way forward for climate financing are sub-optimal for Mozambique's needs and, currently, do not represent a broad and sustainable base for climate financing in Mozambique.

This report assessed the extent to which DRM, particularly in the extractive sector, could serve as a source of climate financing in Mozambique. Indeed, given the size and value of extractive resources in Mozambique today and in the near future, the extractive sector stands as a potentially important source to meet the country's climate financing needs. Yet, currently, the extractive sector contributes more than USD 200 million to the state coffers, only 0.0026% (yearly) of the approximately USD 7,586 billion that the country needs for its adaptation and mitigation actions until 2025. Presently, and at least in the short and medium term, the potential contribution of tax revenue from the extractive sector to support Mozambique's climate goals is very limited. Although the taxes from sector have increased over the years following the improvements in the legal and institutional framework – allowing for a regular flow of resources from a combination of production-based revenue-raising mechanisms and profit-based taxes to the state coffers over the entire life of the projects in the mining industry, the process is still constrained by the prevailing tax leakages through IFFs. These revenue leaks have been facilitated through unfavorable DTAs terms (especially those with Mauritius and UAE) that multinational corporations continuously exploit to avoid paying their fair share of tax and illicit financial outflows through BEPs and transfer pricing.

The report also highlighted the efforts underway to address the revenue leaks in the extractive industry. As a result of advocacy by CSOs, there is already a movement in the country to revise DTAs, preventing multinational corporations from exploiting them for tax avoidance. Additionally, the government is actively working on measures to combat IFFs, including enhancing transfer pricing regulations and imposing fines on mining companies engaging in trade misinvoicing. While progress is being made, there remains a need for a robust institutional framework to tackle these challenges and ensure equitable revenue distribution effectively.

The reforms being undertaken by the government are not the only factors that will determine the course of DRM from the extractive sector in Mozambique. The global climate agenda is set to impact Mozambique's extractive sector significantly. For instance, CBAM could affect Mozambique,

the country may reap

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*windfall from its
LNG projects in the
Rovuma Basin*

a major aluminum exporter to the EU, potentially leading to substantial annual fees and a significant economic impact in the worst-case scenario or prompt greater diversification of the country's export markets to mitigate some losses. On the flip side, Mozambique is also well-positioned to benefit from the growing demand for minerals like graphite, essential for renewable energy and electric mobility. With vast graphite reserves, the country has become the world's second-largest producer, attracting mining companies and contributing substantial tax revenue that could be channeled towards climate financing for adaptation and resilience.

It's expected that, in the long term (more specifically after the 2030s), the industry will be an important source of finance as the country may reap USD 90 billion windfall from its LNG projects in the Rovuma Basin. However, the extractive revenues will not be earmarked for climate financing expenditures. The mounting debt and much-needed economic social expenditures to improve the lives of Mozambicans currently facing privation are the most likely to benefit. This is particularly true considering the current and projected composition of the government expenditures, at least in the short and long term, and the fact that the national budget doesn't have clear lines to finance the achievement of the country's NDCs nor does it effectively integrate climate change into its financial decisions. (is a further conclusion that Global north countries in the form of the EU / CBAM have, once again, designed a neutral policy / blunt instrument that continues a pattern of penalizing low income countries who most need a more nuanced response to enable a meaningful equitable response to the climate crisis.

Recommendations



- ⇒ **Strengthen advocacy efforts:** reinforce the role of the Mozambican government and civil society actors in the global advocacy for global climate finance mobilization for African countries;



- ⇒ **Develop a National Climate Finance Taxonomy:** Establish a clear and consistent methodology for tracking climate finance across ministries. This taxonomy will facilitate strategic decision-making and resource prioritization;

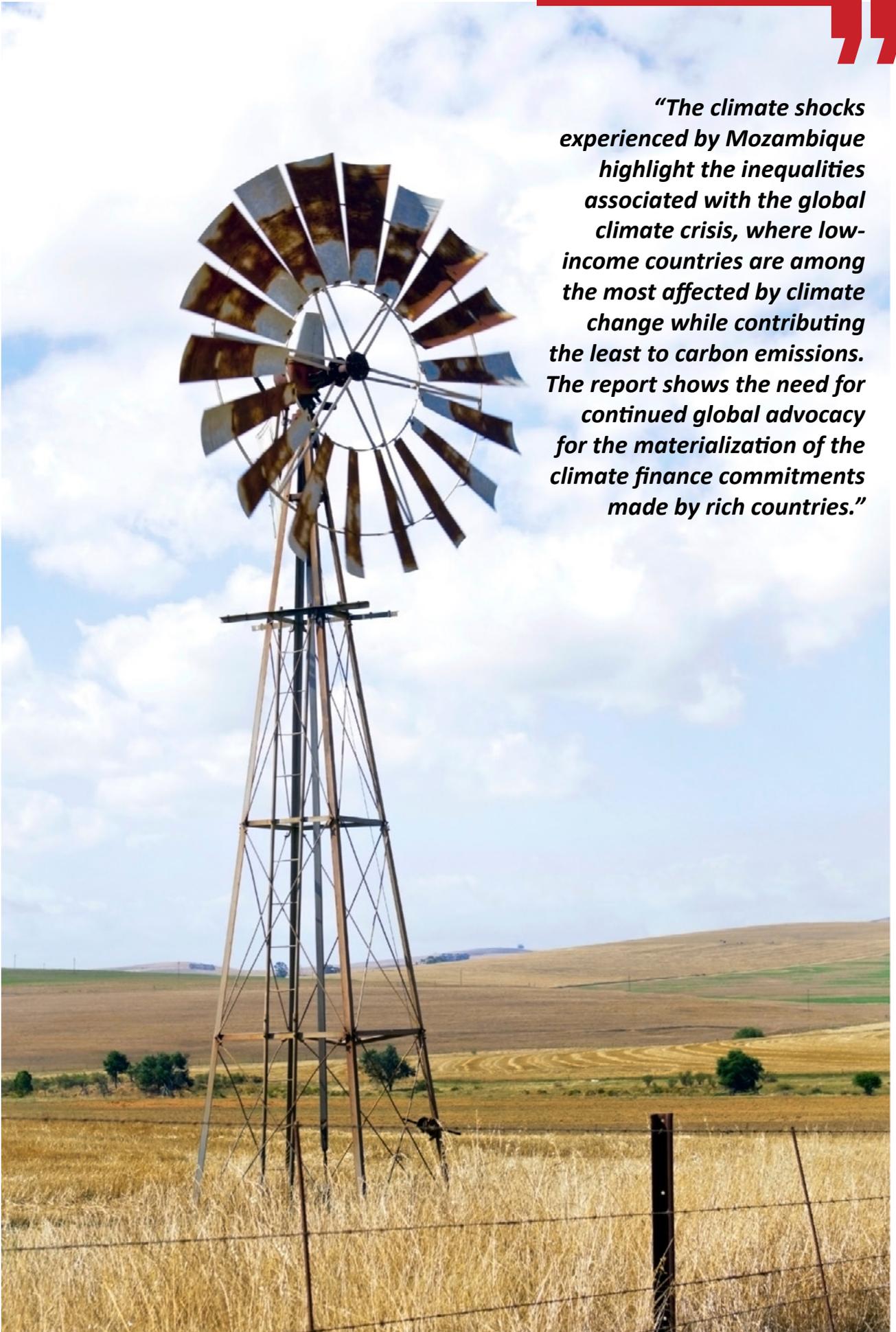


- ⇒ **Mainstream climate considerations and disaster risk management considerations in the Budgeting process:** Integrate climate change considerations into the National Development Strategy and the yearly national budgeting process. The public resources allocated ex-ante for emergency response and recovery have systematically been significantly lower than the funds needed to cope with catastrophic events. The government should allocate a higher percentage of tax revenue to climate adaptation and mitigation efforts, as stipulated in Decree No. 53/2017;

- ⇒ **Accelerate Paris Agreement Implementation:** Expedite the establishment of frameworks under Article 6 of the Paris Agreement to access additional climate funding and support Mozambique's climate goals;



- ⇒ **Reform the legal and institutional framework governing DRM in the extractive industry to make it more efficient and progressive.** These include:
- Revisit and renegotiate tax treaties, particularly those with the tax havens of Mauritius and UAE, to prevent aggressive tax planning and ensure that Mozambique receives its fair share of taxes from multinational corporations;
 - Equipping the UTIE with more financial and human resources to enhance the monitoring process in the mining industry, accurately determining production volumes, and assessing mineral quality to combat under-invoicing and tax evasion;
 - Strengthen efforts to combat IFFs in the extractive sector, particularly through measures targeting tax base erosion and profit shifting (BEPS) and transfer pricing abuses. Decree No. 70/2017, of December 6, must be reviewed to include clearer and enforceable rules for transfer pricing.



“The climate shocks experienced by Mozambique highlight the inequalities associated with the global climate crisis, where low-income countries are among the most affected by climate change while contributing the least to carbon emissions. The report shows the need for continued global advocacy for the materialization of the climate finance commitments made by rich countries.”



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