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Draft regulations for exploitation of mineral resources in the Area

Report of the Chair on the outcome of the third meeting of the open-ended working group of the Council in respect of the development and negotiation of the financial terms of a contract under article 13, paragraph 1, of annex III to the United Nations Convention on the Law of the Sea and section 8 of the annex to the Agreement relating to the Implementation of Part XI of the United Nations Convention on the Law of the Sea of 10 December 1982

I. Introduction and background

1. During the second part of the twenty-fifth session of the International Seabed Authority, the Council welcomed the progress made by the open-ended working group in advancing discussions on an appropriate system and rates of payment to the Authority for minerals recovered from the Area during exploitation, but recognized that further work still needed to be done in order to develop clear recommendations. It therefore requested the working group to convene a third meeting immediately prior to the next meeting of the Council, in February 2020.

2. During the second meeting, the working group had reviewed three options for the payment mechanism and associated rates of payment, namely:

(a) A fixed-rate ad valorem-only royalty mechanism;

(b) A two-stage ad valorem-only royalty mechanism;

(c) A combined ad valorem royalty and profit-based system.

3. In preparation for the third meeting of the working group, the secretariat was requested to further refine the model to include a progressive ad valorem royalty system. It was also agreed that, to the extent possible, the third meeting would begin work on other mineral resources than polymetallic nodules.

* ISBA/26/C/L.1.

4. The third meeting of the working group was held on 13 and 14 February 2020, prior to the first part of the twenty-sixth session, and was open to all stakeholders. However, it may be noted that most developing States were absent for that particular meeting. On 13 February, the agenda for the meeting was adopted with no amendment.[1]

II. Review of options

5. With a view to assisting in the creation of a review of the options for the payment mechanism, Richard Roth and Randolph Kirchain from the Massachusetts Institute of Technology made a presentation on the refined model, which included a progressive ad valorem royalty mechanism.

6. The Chair invited delegations to focus on the consideration of the four options in the model with a view to narrowing down the number of options under consideration and recommending one or two options to the Council, noting that the possible refinement of the assumptions used for the model would be considered at a later stage.

7. Participants expressed their thanks for a clear and comprehensive presentation by the Massachusetts Institute of Technology. Some delegations expressed the view that the four options should be further considered. Several delegations expressed support for both a two-stage fixed ad valorem mechanism and a two-stage progressive ad valorem mechanism around which to pursue discussion. Noting the complexity and administrative costs associated with a profit-based system, some delegations did not find it appropriate to continue the consideration of a profit element in the model. Those that favoured an ad valorem mechanism, either fixed or progressive, noted that it would meet the requirements of the United Nations Convention on the Law of the Sea and the Part XI Agreement, including for the system of payments to be fair to both contractors and the Authority. It was also noted that it would be simpler to implement, leading to lower administrative and compliance monitoring and auditing costs, and would be more transparent, making compliance monitoring easier. A suggestion was made, however, that maximum and minimum rates should be included in such a system. For the various options, the need to bear in mind the staffing requirements and monitoring costs for the Authority was highlighted. The goal of maximizing revenue to the Authority seemed to be widely accepted, while at the same time understanding that it was not the Authority's role to engage in risk-sharing ventures, but instead to administer the common heritage of mankind, in accordance with article 157 of the Convention.

8. Comments were made regarding some aspects and assumptions of the model, and the need for further details was highlighted. In particular, it was noted that the model did not adequately take into account external aspects, including environmental aspects, and that some of the fundamental assumptions of the model needed to be reviewed, in particular with regard to nodule abundance and collector number, width and speed. Comments were also expressed about linking royalties to metal prices, and suggestions were made about exploring other values, including the volume and weight of production, sponsoring States' fees and corporate income tax. Some delegations

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[1] To assist participants in the discussions of the third meeting, the following documents were prepared and made available on the website of the Authority: the provisional agenda, the indicative programme of work, a revised financial model, a briefing note from the Chair of the open-ended working group and presentations on the financial payment system by Richard Roth and Randolph Kirchain. By way of further background, reference was made to the briefing note prepared by the Chair for the second meeting of the working group and to the report by the Massachusetts Institute of Technology (https://ran-s3.s3.amazonaws.com/isa.org.jm/s3fs-public/files/documents/paysysmodel-3jun.pdf).

suggested that concrete price forecasts should be used for modelling purposes. The need was also stressed for a more precise definition of the calculation method to assess the value of a given production volume and its respective percentage. Concerns were also expressed with the underlying method of fine-tuning the rates of the payment regime to ensure post-tax profits were high enough to motivate investment in deep-sea mining.

9. With regard to the policy objective of the Convention and the Part XI Agreement,[2] and without prejudice to the future financial model to be adopted, several delegations recognized the benefit in establishing an updated comparative analysis of seabed mining and land-based mining before a next meeting. This could include the identification of:

(a) The royalty rates;

(b) The taxable base in those jurisdictions representing the bulk of production for the same or similar minerals and/or ores, e.g., manganese, copper, cobalt and nickel;

(c) Any environmental levies;

(d) Any administrative fees.

10. This work could identify the average royalty rate(s) and methodology to determine a taxable base, that would neither advantage nor disadvantage Authority contractors in relation to land-based producers. It could also consider the corporate income tax regimes of those major land-based producer jurisdictions, compared with those of sponsoring States and other States that would be involved in the entire value chain of Authority contractors.

III. Environmental aspects of the model

11. With regard to the environmental aspects of the model, some delegations expressed the need to revisit the 1 per cent benchmark for contractors to pay as contributions to an environmental compensation fund. The Secretary-General informed the working group that the secretariat had issued calls for proposals for consultancies to undertake studies on an environmental compensation fund and an environmental performance guarantee. It was noted that consideration of aspects of the fund not related to the financial model was beyond the current scope of the working group.

12. The working group agreed to revert to the consideration of the environmental aspects of the financial model once further information was available.

IV. Other mineral resources: economic modelling and timing

13. To assist discussions on the consideration of financial models for other mineral resources, Mr. Roth made a second presentation on the applicability of the model for polymetallic nodules to the other mineral resources in the Area, namely, polymetallic sulphides and cobalt-rich ferromanganese crusts. This was based on the assumption that the cash-flow value structure currently used for nodules could readily be adapted to other minerals, bearing in mind however that the specific costs and revenues associated with the retrieval of different resources may vary. A number of delegations shared the view that the development of a payment regime for other minerals was premature, including in the light of technological challenges and the fact that a true estimate could only be obtained using accurate geological information and there was

[2] Part XI Agreement, annex, section 8, item (1)(b).

still limited knowledge concerning the composition and metal concentration of the other two minerals, in particular polymetallic sulphides.

14. The working group agreed that the focus of its work should be on polymetallic nodules, at this stage, pending further studies on the other types of resources.

V. Recommendations

15. The open-ended working group recommended that the Council:

(a) Convene a fourth meeting of the working group, preferably before the second part of the session of the Council, in order to further advance work on the payment mechanism for polymetallic nodules as a priority;

(b) Invite all stakeholders to submit comments to the secretariat, by 23 March 2020, for the purpose of further refining the assumptions of the model;

(c) While recognizing that the working group did not fully endorse nor discard any of the options, request the secretariat to prepare a report in order to refine further the two-stage fixed ad valorem royalty mechanism and the two-stage progressive ad valorem royalty mechanism, including taking into account any comments submitted pursuant to paragraph 15 (b) above, and other information as appropriate, for consideration at the following meeting of the working group;

(d) Request the secretariat to prepare a comparative study, as reflected in paragraph 9 above;

(e) Request the secretariat to make the documentation that is to be considered at a next meeting of the working group available on the Authority's website at least 14 days before the first day of the next meeting.