

**TEMPLATE FOR SUBMISSION OF TEXTUAL PROPOSALS DURING THE 28TH SESSION:
COUNCIL - PART III**

Please fill out one form for each textual proposal which your delegation(s) wish(es) to amend, add or delete and send to council@isa.org.jm.

1. Name of Working Group:

Open Ended Working Group on the Financial Terms of Contracts

2. Name(s) of Delegation(s) making the proposal:

Canada (intersessional coordinator for payment system/rates review text)

3. Please indicate the relevant provision to which the textual proposal refers.

DR 81 (Review of system of payments)

4. Kindly provide the proposed amendments to the regulation or standard or guideline in the text box below, using the “track changes” function in Microsoft Word. Please only reproduce the parts of the text that are being amended or deleted.

1. The system of payments adopted under these regulations and pursuant to paragraph 1 (c) of section 8 of the annex to the Agreement shall be reviewed by the Council five years from the first date of commencement of Commercial Production in the Area and at intervals thereafter in accordance with relevant Standards as determined by the Council, taking into account the level of maturity and development of Exploitation activities in the Area.
2. The Council, based on the recommendations of the Commission and following a review under paragraph 1, and in consultation with Contractors, may revise decide to adjust the existing system of payments or introduce a new ~~the~~ system of payments, ~~in the light of changing circumstances and following any review under paragraph 1 above, save that any revision shall only apply to existing exploitation contracts by agreement between the Authority and the Contractor taking into account the level of maturity and development of~~ Exploitation activities in the Area, as well as the principles under Article 13 of Annex III to the Convention and Section 8 of the Agreement.
3. Without limiting the scope of any review by the Council, a review under this regulation may include an adjustment to an existing system of payments, or an introduction of a new system of payments, and may consider changes to all applicable Rules Regulations and Procedures (RRPs).
4. A review of the system of payments shall consider all Resource Categories unless otherwise decided by the Council.

5. A change to the system of payments shall only apply by agreement between the Authority and the Contractor for Contract Areas that have already commenced Commercial Production.

5. Please indicate the rational for the proposal. [150-word limit]

A review of the system of payments (DR 81) should be aligned with the review of the rates of payments (DR 82). Section 8, paragraph 1(c) of the Annex to the Implementation Agreement provides that any change to the system of payments may only apply to existing contracts at the election of the contractor and this shall be implemented by agreement between the Authority and the contractor. However, such agreement is not a pre-requisite for the application of a change in the rates of payment (DR 82). The need to make a clear distinction between the two provides a strong rationale to avoid merging text under DR 81 and 82 into a single regulation.

Specific elements to be included in the review process, including timelines, processes, and methodologies are proposed for inclusion in Standards will ensure greater transparency and predictability of the process from initiation to completion. Draft Standards are included as an appendix to this submission. A compliance and enforcement function (Regulation 103) will also be important.

Draft Text for Relevant Standards

Review of the system of payments and the rates of payments (Regulation 81 and 82)

Introduction and Guiding Principles

1. The purpose of the review of the system of payments and the rates of payments is to ensure that the financial needs and objectives of the Authority are being fulfilled. The review process shall be governed by the provisions of the Convention, the Agreement, relevant international standards, and Good Industry Practice in extractives sector taxation. Specifically, Section 8 of the Annex to the Agreement sets out the following principles:

- a. 'The system of payments to the Authority shall be fair both to the contractor and to the Authority and shall provide adequate means of determining compliance by the contractor with such system;¹
- b. 'The rates of payments under the system shall be within the range of those prevailing in respect of land-based mining of the same or similar minerals in order to avoid giving deep seabed miners an artificial competitive advantage or imposing on them a competitive disadvantage;²
- c. 'The system should not be complicated and should not impose major administrative costs on the Authority or on a contractor. Consideration should be given to the adoption of a royalty system or a combination of a royalty and profit-sharing system. If alternative systems are decided upon, the contractor has the right to choose the system applicable to its contract. Any subsequent change in choice between alternative systems, however, shall be made by agreement between the Authority and the contractor;³

Additionally, Article 13 of Annex III to the Convention sets out the following guiding objectives for the Authority:

- a. 'to ensure optimum revenues for the Authority from the proceeds of commercial production,⁴
- b. 'to attract investments and technology to the exploration and exploitation of the Area,⁵ and
- c. to ensure equality of financial treatment and comparable financial obligations for contractors'.⁶

Any recommendation to adopt a new or revised system of payment or changes in the rates of payments must clearly demonstrate that the change will result in a payment

¹ Paragraph 1(a), Section 8 of the Annex to the Implementation Agreement

² Paragraph 1(b), Section 8 of the Annex to the Implementation Agreement

³ Paragraphs 1(c), Section 8 of the Annex to the Implementation Agreement

⁴ Convention, Annex III, Article 13.1(a).

⁵ Convention, Annex III, Article 13.1(b).

⁶ Convention, Annex III, Article 13.1(c).

regime that is significantly better at meeting the principles set forth under Article 13 of Annex III to the Convention and Section 8 of the Agreement.

Review Process

2. The Council shall regularly review both the system of payments and the rates of payments following the Commencement of Commercial Production in the Area.
3. The Council shall establish and regularly update a schedule for the review of the system of payments and the rates of payments following the commencement of Commercial Production in the Area.
4. The Secretary General shall ensure that the schedule referenced in paragraph 3 above is made publicly available.
5. Any review of the system of payments and rates of payments conducted pursuant to this Standard shall be completed within 12 months, unless otherwise decided by the Council.
6. The Council shall initiate the first review of the system of payments and the rates of payment on the five-year anniversary of the start of the first royalty period [i.e., January 1st or July 1st] corresponding to the first instance of commencement of Commercial Production in the Area. An illustrative example for a scenario is included in Figure 1 below.

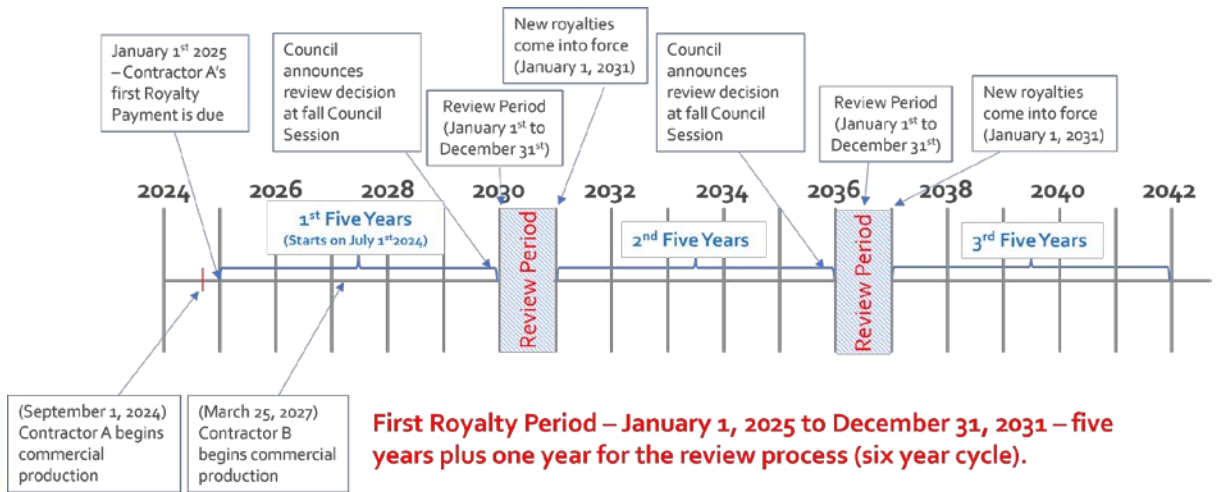


Figure 1: Example of a scenario with two Contractors entering Commercial Production at different times.

7. Subsequent reviews of the system of payments and rates of payments shall be initiated on a regular basis every five years following the conclusion of the 12 month period allocated for the previous review under paragraph 5.
8. Based on the review schedule, the Council shall ensure that adequate funds are allocated from the Authority's budget to undertake an effective and thorough review of the system of payments and rates of payments.

9. The Council shall task the Commission with preparing terms of reference for a review. The Council shall review and approve the terms of reference for the review at a Council meeting prior to the official scheduled initiation of the review process.

10. During a review, there should be a presumption that rates of payment and system of payments should not change unless there is evidence that rates currently in force have been set too high or too low, or that the system of payments is not performing as anticipated. Furthermore, any proposed change to the rates of payments and system of payments shall be material in nature and not an administrative nuisance [e.g., change in rate of less than [#] percentage point should not be recommended].

11. The Commission will be responsible for:

- Undertaking the review
- Engaging third-party experts
- Ensuring consultations with relevant stakeholders, including Contractors, Sponsoring States, Member States eligible for a seat on Group C of the Council, the Enterprise, and the Economic Planning Commission (once established).
- Providing the Council with recommendations, in accordance with the established timeframe set out in paragraph 7, on whether any adjustments are warranted along with a supporting rationale.

12. The Council shall consider the recommendations of the Commission and shall decide whether:

- to adjust the rates of payments and what the magnitude shall be for such adjustments; and
- to adjust the existing system of payments or introduce a new system of payments.

13. Should the Council decide to adjust the rates of payments or the system of payments, such adjustment shall:

- take effect from the beginning of the first royalty period following the Council's decision under paragraph 12 [i.e., January 1st or July 1st];
- apply to all future Contract Areas and all Contract Areas where the first five years of Commercial Production have elapsed by the time that the adjustment takes effect.

The establishment of Standards for the review of the financial terms of exploitation contracts will enable the Authority to simplify the text of the regulations and move rates, deadlines, timelines, and technical considerations, etc. into a set of Standards that can be easily updated.

The establishment of Standards will ensure that there is a consistent, rigorous, transparent, and timely approach to the process by which the Authority will review the system of payments and the rates of payments.

The establishment of a defined review process will also ensure that the Authority can fulfil its mandate to organize and control all mineral-resources-related activities in the Area for the benefit of humankind as a whole.

Also, any review of the system of payments and rates of payments should consider the rates of payments across all financial mechanisms established by the Authority (e.g., potential additional tax, profit share mechanism, financial incentives, etc.) and be aligned with the review of the system of payments and rates of payments.

Finally, the establishment of a transparent review process by the Authority will ensure that member States and Contractors have confidence in the Authority's ability to manage the financial system of the Area for the benefit of humankind as a whole.