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Council of

Alaska Producers

Comments on HFIN hearing on HB4005 (Mining Taxation), May 27, 2016

May 27, 2016

Representative Steve Thompson, Co-Chair
Representative Mark Neuman, Co-Chair
House Finance Committee
Alaska State Legislature
State Capitol
Juneau, AK 99801

Dear Representative Thompson and Representative Neuman:

The Council of Alaska Producers (CAP) is writing to provide comments on HB4005, "An Act relating to the mining license tax; relating to the exploration incentive credit; relating to mining license application, renewal, and fees; and providing for an effective date."

CAP is a non-profit trade association formed in 1992 and serves as a spokesperson for the large metal mines and major metal developmental projects in the state. Bringing together mining companies with interest in Alaska, the Council represents and informs members on legislative and regulatory issues, supports and advances the mining industry, educates members, the media, and the general public on mining related issues, and promotes economic opportunity and environmentally sound mining practices.

As businesses that have had to make tough decisions to optimize operations, cutting budgets and positions over the past four years of declining mineral prices, CAP appreciates the depth of the State's fiscal challenge.

CAP's position has been consistent. To achieve fiscal sustainability and a stable investment climate, we support strategic reductions in the cost of government, use of the Permanent Fund earnings, followed by broad based revenue measures to fill the remaining gap.

The goal of Alaska's mineral tax policy should be to attract investment and encourage a robust, responsible mining industry that contributes to Alaska's economic diversity by providing: a) good jobs, b) procurement and contract opportunities for local businesses, c) state and local government revenue, and d) revenue sharing to Alaska Native Corporations.

Investors in Alaska's mining industry look for fiscal stability. Increasing the Alaska Mining License Tax (AMLT) rate, decreasing incentives, and failing to provide clarity on local taxation creates greater uncertainty and deters investment.

Increasing the Mining License Tax

HB4005 proposes to raise the top tax rate for mines from 7% to 9% of net income resulting in a 29% increase in taxes for the large metal mines in Alaska. This amount is significant for the individual mines, however it is insignificant relative to the fiscal crisis that the Legislature is trying to solve. The fiscal note for this bill indicates that revenue will increase by approximately $5.6 million per year in FY18 while we are facing a deficit of approximately $3.5 billion.

The mining industry is facing commodity prices that are at four year lows, rising operational costs, and margins that are continuing to shrink. Mines invest significant capital and exploration money each year in their existing operations in order to extend their life and increasing the tax burden will minimize the money available for these efforts. Increasing the tax rate in HB4005 as proposed will have the effect of shortening the lives of the existing mines as the return on capital and exploration investments will be lessened and investment in the state becomes far less attractive.

When compared to the two largest mining states in the nation, Nevada and Arizona, Alaska already has the highest tax on mining as well as the highest corporate income tax rate. In order for Alaska to be competitive, attract mining dollars and ultimately generate more state revenue, we should be looking at incentives, not increased taxes.

Removing Incentives

The State of Alaska provides only two tax incentives to attract the development of new mines in Alaska and HB4005 proposes to significantly reduce both of them. The first incentive is the exemption from Alaska Mining License Tax for the first 3.5 years of operation and this bill proposes to limit that to two years. It takes a significant amount of exploration, development and construction expenditures to bring a new mine into production, and it can take up to 20 years for cumulative net cash flow to become positive. Having the tax exemption in the first 3.5 years is critical and shortening it to two years may stop a project from going into production.

The second incentive is the Exploration Incentive Credit Program which allows a maximum of $20 million of pre-operational costs to be deducted from AMLT and the state royalty. HB2005 proposes elimination of the option to apply the mining exploration tax credit to the royalty payment for a new mine on state land. While the maximum exploration credit for a new mine is only $20 million, it still could make a difference in the first years of production when a new mine is saddled with huge capital costs.

Failure to Provide Clarity on Local Taxation

For some time, a significant source of fiscal uncertainty has been the potential for municipalities to target the mining industry for special severance taxes. The Alaska Minerals Commission has consistently recommended that the Legislature address this.

In 2005, the Commission stated "...the mining industry does expect to pay its fair share of municipal government costs...it should do so by an equitable, broad based tax such as a property tax, not an industry specific tax such as a severance tax."

In 2013, the Commission also stated: "Allowing local governments to impose potentially onerous severance taxes inappropriately shifts control of development decisions away from the state. This precludes the state from fulfilling its mandate to manage state-owned resources in a way that maximizes benefits to all Alaskans."

CAP encourages you to consider amending the bill to protect state sovereignty by reserving the ability to levy mining special taxes to the Legislature. An amendment should:

1. Eliminate the ability for a municipality to levy or collect a tax on metal mines (just as Title 43 does for oil and gas production); and

2. Implement revenue sharing of the Alaska Mining License Tax with the municipality that hosts a metal mine.

Mines and municipalities will still have the ability to enter into payment in-lieu of taxes (PILT) agreements if a broad based tax such as a property tax is not available. Such an amendment should not impact the ability of municipalities to place severance taxes on coal, sand, gravel, rock, dimension stone or any other bulk commodity that they may currently tax.

If the State is going to increase the hurdles for investment in Alaska mining by raising the Alaska Mining License Tax, then it should provide some improved certainty by addressing this longstanding source of economic unpredictability.

In conclusion, CAP sees a growing disconnect between Alaska's potential for mineral development and the reality of declining investments in exploration/expansions. Alaska must compete on a global market for mining investment dollars and HB4005 will only serve to drive those dollars elsewhere.

Given these circumstances, we urge you to look closely at whether this bill helps diversify the economy, encourage investment, and grow the net revenue coming to the state. If it does not, then it must be set aside.

Thank you for the opportunity to provide these comments. Please keep in mind the many communities, hundreds of local businesses, and thousands of Alaska miners and their families who depend on a healthy mining industry.

Sincerely,

Michael Satre
President

cc: Members of the House Finance Committee