



MEMORANDUM

DATE: October 17, 2007
TO: Mike Black, Deputy Commissioner
THRU: Steve Van Sant, State Assessor
FROM: Ron Brown, Assistant State Assessor
RE: Review of Alaska and National Mining Taxation

Attached is a copy of the information collected in regards to mining taxation in Alaska and other States. The primary source of data for this report came from InfoMine USA, which contained data on 31 of the 50 states including Alaska.

There are three major taxes applicable to mines in the State of Alaska, these are;

- Corporate Income Tax
- Royalties
- Mining License Tax

The most significant issue noted in the review is that unlike other states, the Alaskan tax structure is almost solely based upon the calculation of net income in its treatment of mines. Due to this dependence on net income the significance of this single calculation cannot be overstated. However, due to allowed deductions for Mineral Incentive Credits, other taxes, percentage based depletion allowances and other issues, the net income calculation may be a questionable measure.

Currently, HB 156 is pending in the legislature. This bill appears to address several of the issues mentioned in this report and is a good source of additional information and comment.

Analysis of Mining Taxation of All 50 States

ANALYSIS OF STATE MINING TAXATATION

Data was obtained on Mining Taxation from 31 of the 50 states from InfoMine USA, Inc. A basic review of the tax structure across the country is provided below. A presentation of the individual programs for each state is available in excel format.

Income Tax:

23 of the states levy an income tax with an average tax rate of 6.32% and a median rate of 6.6%. Alaska levies a progressive income tax of between 1% and 9.4%. The actual rate depends upon the net income of the corporation's Alaskan operations. All taxes paid in the State of Alaska are deductible for income tax purposes.

Six of the remaining states levy a tax that is very similar to the income tax, but is sufficiently different that it should not be included in this category. Only two states (Washington and Wyoming) do not levy any type of tax that is based primarily on income.

Alaska Corporate Rate Schedule (AS 43.20.011)

Alaska Taxable Income	Tax	Marginal Rate*
\$ 0 - \$10,000	\$0	1%
\$10,000 - \$20,000	\$100	2%
\$20,000 - \$30,000	\$300	3%
\$30,000 - \$40,000	\$600	4%
\$40,000 - \$50,000	\$1,000	5%
\$50,000 - \$60,000	\$1,500	6%
\$60,000 - \$70,000	\$2,100	7%
\$70,000 - \$80,000	\$2,800	8%
\$80,000 - \$90,000	\$3,600	9%
\$90,000 or More	\$4,500	9.4%

* The marginal rate is the rate applied to income above the minimum income level set by the schedule. For example, a corporation with an income of \$15,000 would pay \$100, plus 2% of the \$5,000 of income over \$10,000 (\$100) for a total tax bill of \$200.

Sales Tax:

27 of the states levy a sales tax with an average tax rate of 6.16% and a median rate of 6.0%. Alaska does not levy a state sales tax, however some local municipalities can levy sales taxes. The actual rate depends upon the physical location of the mining operation. Local sales tax rates in Alaska vary from 1% to 7% in areas where a sales tax is levied.

Three of the four remaining states levy a tax that is very similar to the sales tax, but is sufficiently different that it should not be included in this category. Only one state, Oregon, does not levy a tax that is based upon sales.

It should be noted that sales taxes would only apply to assets purchased by and for the mine from inside a borough/city that levies a sales tax. Sales of the ore, ore concentrate or refined products from the mine will *typically* not be sold from the mine and therefore would not pay a sales tax. However, locally utilized materials gravel, sand etc., could be subject to such a tax.

Property Tax:

27 of the states levy a state property tax. The remaining four states, including Alaska, have property taxes but they are administered on the local level. The actual rate depends upon the physical location of the mining operation and the means of valuation (fractional versus full value) so any comparison of tax rates would be highly questionable. Property tax rates for local governments in Alaska vary from 0.5% in Whittier to 1.9% for the North Slope Borough.

Resources in Place:

The value of natural resources in place (reserves) is not part of the valuation for property tax purposes in Alaska. This is also the case for nine of the remaining 27 states where information is available. However there are a wide range of ad valorem valuation methodologies across the country such as income analysis, valuation by gross product or operating status. Under some of these valuation methods, at least some of the value for mineral reserves would be incorporated in the final value. The reports on 10 of the 27 states did not contain references to the inclusion of values for resources in place.

Royalties:

Royalties for the extraction of State Owned minerals is addressed only in Alaska. Alaska has a royalty structure based upon 3% of net income, except for coal which is 5% to 12% of gross value depending upon the lease type. Three other states have information related to the income or property tax implications of royalties paid to private entities.

Mining License Tax:

Alaska has a Mining License Tax that is based upon Net Income. The tax is progressive from 0% to 7% depending upon the level of Net Income. All new mining operations are exempt from the mining license tax for the first 3-1/2 years.

Alaska Mining License Tax Rates

Net Income	Tax
\$0 - \$40,000	\$0
\$40,001 - \$50,000	3% of net income
\$50,001 - \$100,000	\$1,500 + 5% of net income over \$50,000
\$100,001 and more	\$4,000 + 7% of net income over \$100,000

Severance Tax:

Alaska levies no severance tax on the State level. Two municipal governments do levy severance taxes; Denali Borough (Coal and Gravel) and Kodiak Island Borough which

taxes the gross production value of severed natural resources at the borough-wide mill levy.

Fourteen of the other 30 States with available data levy various severance taxes that range from a dollar rate per ton to a percentage of “Gross Value”, “Sale Price”, “Production Value” or some other method. These values are defined in the particular tax law and are not standardized terms.

Minerals Exploration Incentive Credits:

The State of Alaska offers a maximum \$20 million dollar credit for the expenses of exploration activities for mineral resources. These tax credits can be applied against future corporate income taxes, Mining License Taxes or state royalty payments.

The expenses applicable to these credits include; geochemical and geophysical surveys, exploration drilling, underground exploration, surface trenching and bulk sampling, aerial photographs, logging, sample analysis, metallurgical work etc. Qualifying expenses must be approved by DNR.

The expenses, once approved, can be expended over a 15 year period. However, the credits are limited to a maximum of 50% of the income, license or royalty taxes/payments in a given year. Since the maximum marginal tax rate for the corporate income tax is 9.4%, this could allow a tax free status for almost \$213 million dollars of net income and/or a reduction in royalties to the State of up to 20 million dollars.

Commonalities:

There are very few commonalities between the tax policies of mining operations across the country. Each State has approached the taxation of mines differently due to the myriad of differences in the type and scale of mines present within the states and due to the general tax structure used throughout each economy.

Basis of Valuation:

However, it was noted that the Alaskan tax structure has one major commonality. There are three major taxes that mines are subject to on the state level; income taxes, royalties and the Mining License Tax. All three of these taxes, with the exception of coal royalties, are based upon the net income of the mine. Royalties paid to the state and the Mining License Taxes are deductible when calculating net income. Net income also allows a depletion allowance in making this calculation.

Note that by inflating expenses and/or exporting revenue, the tax impacts for all three categories could be drastically minimized. This is not to say or allege that such practices occur or that there is evidence of such. It is only meant to point out that the entire basis of all three tax modes are based upon the result of one accounting calculation.

With the exception of Oregon, the other states utilize tax policies that are based upon values other than net income, or have taxes based upon more than one valuation. For example, Georgia’s Corporate “Corporate Net Worth Tax” is based upon a percentage of the net worth of the corporation. Montana’s “Metal Mines License Tax” is based upon a

percentage of the gross value of mine production. Wisconsin's "Net Proceeds Occupation Tax on Mining of Metallic Minerals" is based upon the net proceeds of the mine.

Treatment of the Ore Value:

As well, with the combination of the major taxes applicable to mines in Alaska, it is difficult to see where the actual value of the ore extracted is exposed to any substantial type of taxation by or payment made to the State. No State property tax is levied and the local property tax is precluded from placing any value on "resources in place". No State sales tax is levied on the sales of ore/ore concentrates or refined products.

The "Minerals Exploration Credit Program" is applicable to any royalties, income or Mining License taxes charged by the State. This program can "write-off" taxes or royalties by up to 20 million dollars over a 15 year period.

The corporate income tax allows the application of a "depletion allowance" as proscribed by the State tax code. This allowance, by the percentage method, allows a producer to reduce Gross Income by 10% for coal mines, and a 15% reduction to Gross Income for metals mines.

The Mining License Tax allows for an exclusion of the tax for the first 3 1/2 years of a new mining operation. This raises the question as to what constitutes a "new mining operation". Is an extension into a new vein of a pre-existing mine a "new mining operation"?

Again, since the royalties, income and Mining License taxes are based upon net income, any costs associated with obtaining the mineral rights are expensed from the income statement prior to the calculation of net income. Indeed it would appear that using the current percentage depletion allowance, the cost of these resources is being expensed at far above the actual cost.

Just as an example, let's imagine a mine that is operating at breakeven. Since net income is zero, there would be no income tax, no mining license tax and no royalty payment to the State for the ore processed by the mine. Yet, at the same time, the mine has extracted a considerable amount of State-owned, non-renewable resources.

Summation:

Looking at the current taxation/royalty structure, the intent appears to have been to attract large-scale mining and exploration to develop Alaskan resource deposits. Given the relatively low prices for gold, silver, zinc and lead at the time, it appears that an "incentive-based" structure was written to promote the development of these resources and the requisite infrastructure to profitably extract them.

In the past three years there has been a tremendous increase in the value of precious and base metal prices. The prices of such commodities have double, tripled and in some cases

more than quadrupled during this time. It would appear that the need for such an “incentive-based” structure does not apply to the current market situation.

As well, as is supported by the attached information, there would appear to be a significant difference in treatment between the mining industry and petroleum industries. Since the petroleum industry has become a huge component of the Alaskan economy and the primary source of governmental revenue, the treatment of this industry has been revisited and reviewed, multiple times over the years.

Conversely, the taxation and royalty treatment of the mining industry has changed very little since Statehood. This has created a situation where the public demands upon two industries, both engaged in the for-profit extraction of non-renewable, public resources are treated in substantially different manners.

Pending Legislation:

Currently, the legislature is considering HB 156 which addresses many of the issues raised in this report. Currently the bill is in the House Ways and Means Committee.

Notable changes in this proposed legislation are:

- increases in tax rates and income levels
- changes the Mining License Tax exemption to a deferral
- removes the deduction of the Mining License Tax from the State Corporate Income Tax
- uses the Net Smelter Return rather than net income for setting royalties
- mandates Cost Depletion rather than Percentage Depletion for calculating net income
- increases in mineral lease rents

While the bill does not address all of the issues presented in this report, it does address many of them. Copies of the bill, sponsor statement, available data and testimony in the past hearings on HB 156 are provided.

Mining Tax Laws Across the United States

Source: InfoMine USA

Notes

* L = Local, S = State, B = Both, N = None

STATE	INCOME	INCOME RATES	PROPERTY	PROP L/S/B*	RESERVES	ROYALTIES	SEVERANCE	SEVERANCE RATES	Sig. Other Tax
ALABAMA	Y	6.5%	YES	B	?	NO	Coal, Iron & Other	Various	No
ALASKA	Y	1% to 9.4% (Prog)	YES	L	No	YES	Local Only	Denali and Kodiak Only	Mining License Tax
ARIZONA	Y	6.968%	YES	B	Yes	NO	Metals	% of Prod. Value	No
ARKANSAS	Y	1% TO 6.5% (Prog) plus 3% surcharge	YES	B	If actively mined.	YES	Various	Various	No
CALIFORNIA	Y	8.84% with AMT	YES	B	Yes	NO	No	N/A	Numerous Fees
COLORADO	Y	4.63%	YES	B	?	NO	Various	Various	No
GEORGIA	Y	6.00%	YES	B	?	NO	No	N/A	Corporate Net Worth
IDAHO	Y	7.60%	YES	B	?	YES	No	N/A	Mining License Tax
ILLINOIS	Y	4.80%	YES	B	Yes	NO	No	N/A	Personal Prop. Tax
INDIANA	Y	8.50%	YES	B	Yes	NO	No	N/A	No
KENTUCKY	Y	4% TO 6% (Prog) with AMT	YES	B	?	NO	% of Gross Value	N/A	No
MAINE	Y	3.5% to 8.93% (Prog)	YES	B	?	NO	No	N/A	Mining Excise Tax
MICHIGAN	Y	See Single Business Tax	YES	B	?	NO	No	N/A	Single Bus & Low Grd Ore
MINNESOTA	Y	See Occupation Tax	YES	B	Iron Ore	NO	Taconite	Several	Several
MISSOURI	Y	6.25%	YES	B	?	NO	No	N/A	Corp Franchise Tax
MONTANA	Y	6.75%	YES	B	No	NO	Various	N/A	Coal Gross & Metal Mines
NEVADA	N	See Proceeds of Minerals Tax	YES	B	Yes	NO	No	N/A	Proceeds of Minerals
NEW MEXICO	Y	4.8% TO 7.6%	YES	B	No	NO	Various	N/A	Gross Rec. & Resource Excise
NORTH CAROLINA	Y	6.90%	YES	B	Yes	NO	No	N/A	Franchise & Pipe Nat Gas
NORTH DAKOTA	Y	2.6% TO 7.0% (Prog)	YES	B	Yes	NO	Coal	\$0.395 per ton	Coal Conv. Facility Tax
OREGON	Y	6.60%	YES	B	No	NO	No	N/A	No
PENNSYLVANIA	Y	9.99%	YES	B	?	NO	No	N/A	Cap. Stock & Franchise Tax
SOUTH CAROLINA	N	5.00%	YES	B	No	NO	No	N/A	Corp. License Tax
SOUTH DAKOTA	N	See Severance Taxes	YES	L	Yes	NO	Various	Various	Conservation Tax
TENNESSEE	Y	See Excise & Franchise Tax	YES	B	No	NO	Various	Various	Corp Excise & Corp Franch
UTAH	Y	See Corp Franchise Tax	YES	B	No	NO	Various	% of Proceeds	Corp Franchise Tax
VIRGINIA	Y	6.00%	YES	L	?	NO	No	N/A	Reclamation Tax
WASHINGTON	N/A	N/A	YES	B	Yes	NO	No	N/A	Business & Occup. Tax
WEST VIRGINIA	N	8.75%	YES	L	?	NO	No	% of Gross Value	Business Franchise Tax
WISCONSIN	Y	7.90%	YES	B	Yes	NO	No	N/A	Occ. Tax and Net Proc. Metal
WYOMING	N/A	YES	L	No	No	NO	Various	Various	Wyoming

Alaskan Mining Taxation Analysis and Data

MINING COMPANY TAXATION IN ALASKA

INCOME TAXES

→ 1% to 9.4% Progressive Rates

EXPLORATION INCENTIVE CREDIT

→ Allows up to \$20 Million in credits for each mine developed.

SALES TAXES

→ 0% to 7% depending upon location, sales of mine products are usually not taxable.

PROPERTY TAXES

→ Subject to same property taxes as are other properties in the same Borough/City. Ore Reserves are not assessable.

ROYALTIES

→ 3% of Net Income, except coal which is more, 5% to 12% of Gross Value.

MINING LICENSE TAX

→ 0% to 7% of Net Income Progressive Rates

Table 24. Revenues paid to the state of Alaska and municipalities by Alaska's mineral Industry, 1999 - 2006

ITEM	2000	2001	2002	2003	2004	2005	2006
State mineral rents and royalties ^a							
State claim rentals	\$1,975,376	\$1,736,522	\$1,908,228	\$2,129,440	\$2,657,939	\$3,308,752	\$3,460,803
Production royalties	\$6,175	\$1,933	\$23,447	\$270,734	\$162,637	\$124,338	\$171,220
Annual labor	\$79,907	\$103,274	\$124,741	\$224,519	\$226,191	\$332,439	\$155,007
Subtotal	\$2,061,458	\$1,841,729	\$2,056,416	\$2,624,693	\$3,046,767	\$3,765,529	\$3,787,030
State coal rents and royalties							
Rents	\$233,249	\$198,545	\$256,927	\$237,912	\$236,532	\$257,112	\$337,764
Royalties	\$1,482,803	\$1,168,043	\$860,633	\$1,064,208	\$1,239,257	\$1,476,250	\$1,473,948
Bonus	\$372,000	\$0	\$0	\$0	\$0	\$129,880	\$10
Offshore Prospecting Permits	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Subtotal	\$2,088,052	\$1,366,588	\$1,117,560	\$1,302,120	\$1,475,789	\$1,863,242	\$1,811,722
State material Sales							
Mental Health	\$33,928	\$118,545	\$151,993	\$134,512	\$76,267	\$129,409	\$89,634
Division of Land	\$449,343	\$1,515,769	\$1,595,708	\$542,311	\$467,360	\$944,905	\$1,582,769
SPCO	\$41,395	\$12,894	\$24,725	\$208,309	\$112,047	\$46,877	\$118,904
Subtotal	\$524,666	\$1,647,208	\$1,772,426	\$885,132	\$655,674	\$1,121,191	\$1,791,307
State mining miscellaneous fees							
Filing fees	\$5,400	\$3,000	\$3,000	\$4,700	\$1,300	\$8,465	\$965
Penalty fees	\$0	\$0	\$450	\$0	\$26,110	\$20,280	\$46,249
Explore incentive app filing fee	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Bond pool payment	\$50,100	\$53,866	\$45,208	\$44,878	\$35,426	\$32,331	\$36,721
Surface coal mining app fee	\$1,830	\$3,700	\$2,530	\$1,005	\$3,116	\$3,150	\$10,897
APMA mining fees	\$18,550	\$13,175	\$11,975	\$15,113	\$14,550	\$17,131	\$17,475
Subtotal	\$75,880	\$73,741	\$63,163	\$65,696	\$80,502	\$81,357	\$112,307
Total Rents, Royalties & Fees	\$4,750,056	\$4,929,266	\$5,009,565	\$4,877,641	\$5,258,732	\$6,831,319	\$7,502,366
State corporate income tax ^b	\$285,815	\$50,266	-\$221,936	\$406,064	\$2,104,144	\$23,641,883	\$71,299,684
Mining License Tax ^{c - e}	\$1,857,134	\$466,430	\$351,387	\$3,224,684	\$10,317,238	\$18,637,996	\$79,141,526
State Total	\$6,893,005	\$5,445,962	\$5,139,016	\$8,508,389	\$17,680,114	\$49,111,198	\$157,943,576
Payments to Municipalities	\$9,196,500	\$9,763,220	\$9,703,208	\$10,510,048	\$10,999,663	\$11,975,892	\$14,388,329
TOTAL	\$16,089,505	\$15,209,182	\$14,842,224	\$19,018,437	\$28,679,777	\$61,087,090	\$172,331,905

Notes:

^aIncludes upland lease and offshore lease rentals.^bPreliminary data for 2006.

►only subchapter C corporations pay income tax.

►this report may not reflect 100% of the returns received in a year.

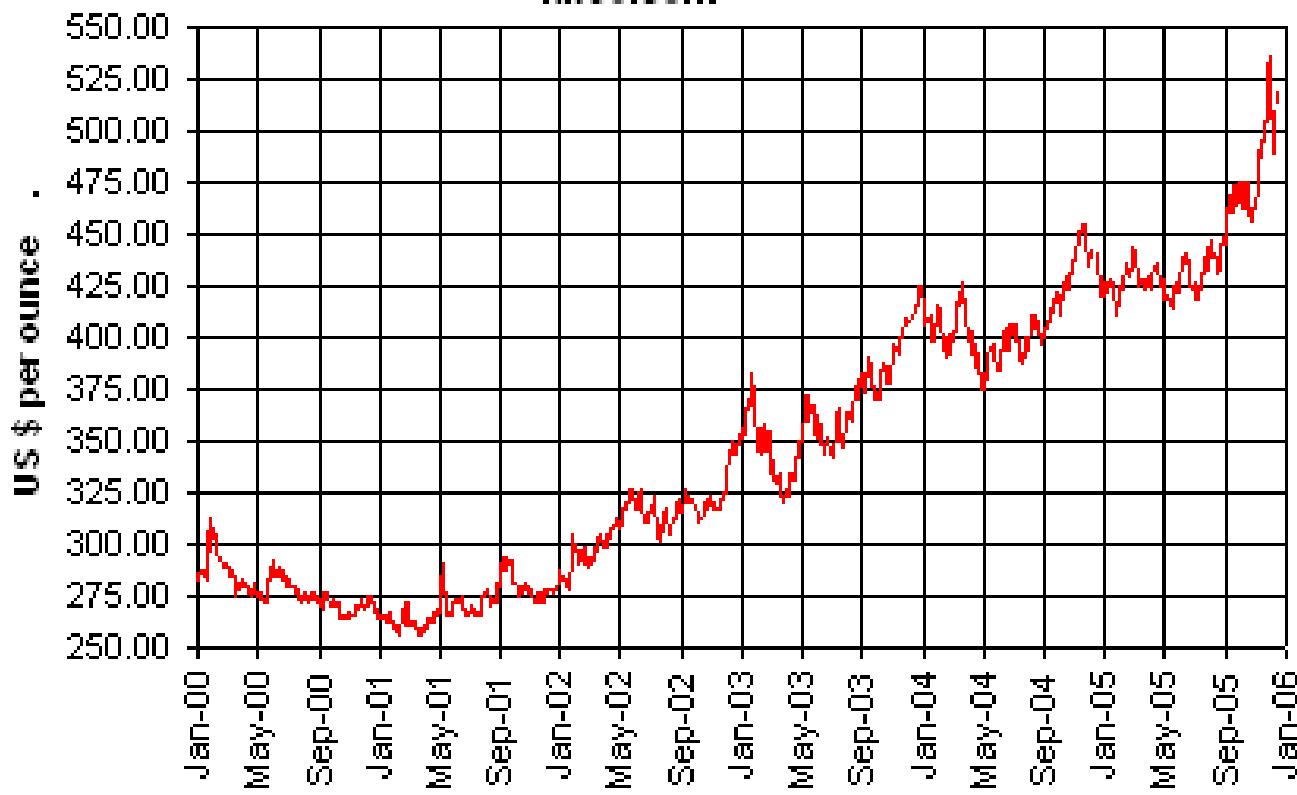
►data from 2001 through 2006 has been updated to reflect revenue to the state for the succeeding fiscal year; ex.: FY 07 receipts are shown in calendar year 2006.

►In FY2003 (calendar year 2002) more refunds were given than revenues received by the state.

^cIncludes metals, coal and material.^dMining license tax has been adjusted to reflect actual receipts for the succeeding fiscal year for the period 2001 to 2006; see note for income tax above.^edata does not match earlier reports.

GOLD - London PM Fix 2000 - 2005

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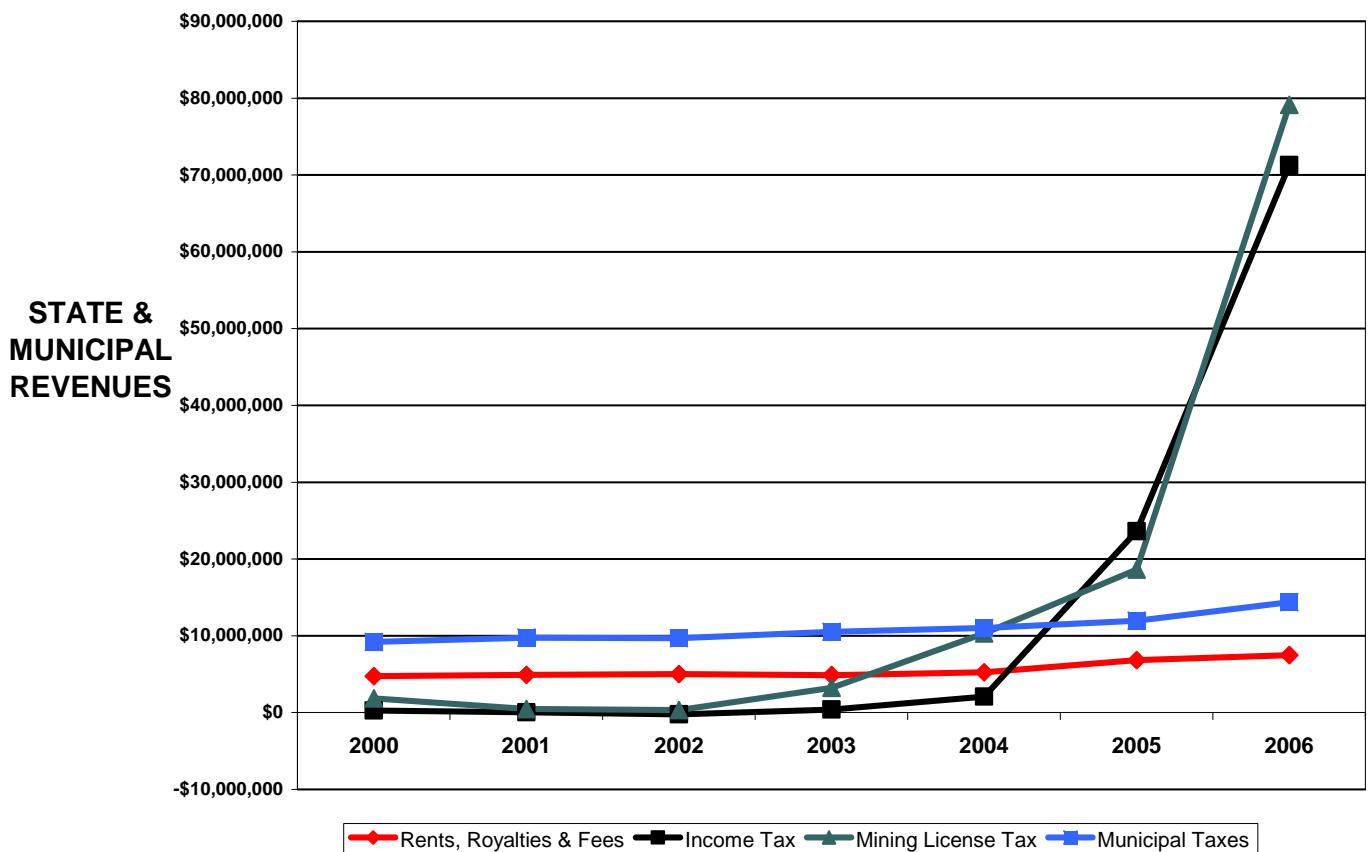


5 Year Zinc Spot



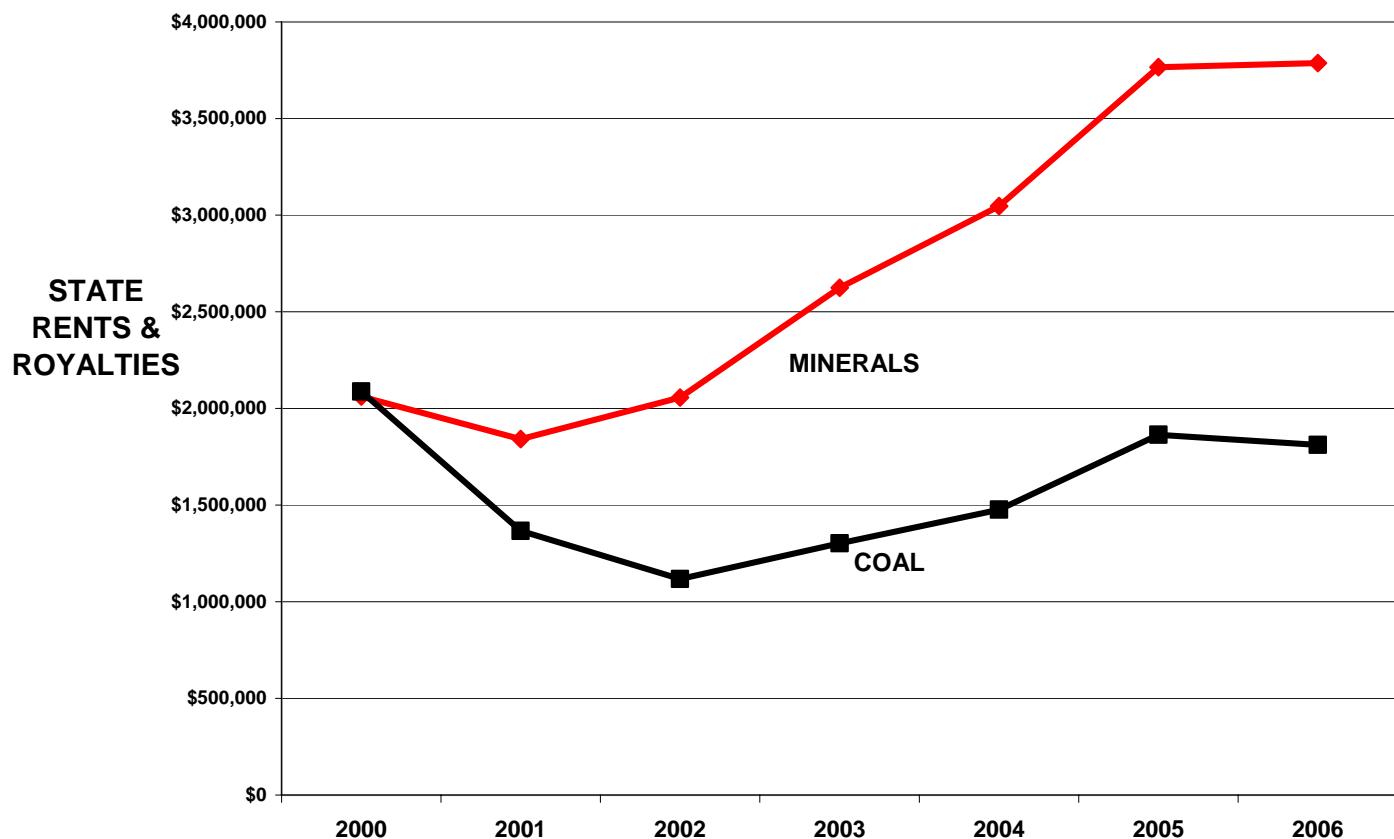
TOTAL STATE & MUNICIPAL REVENUES 2000 TO 2006

Source: Office of Economic Development



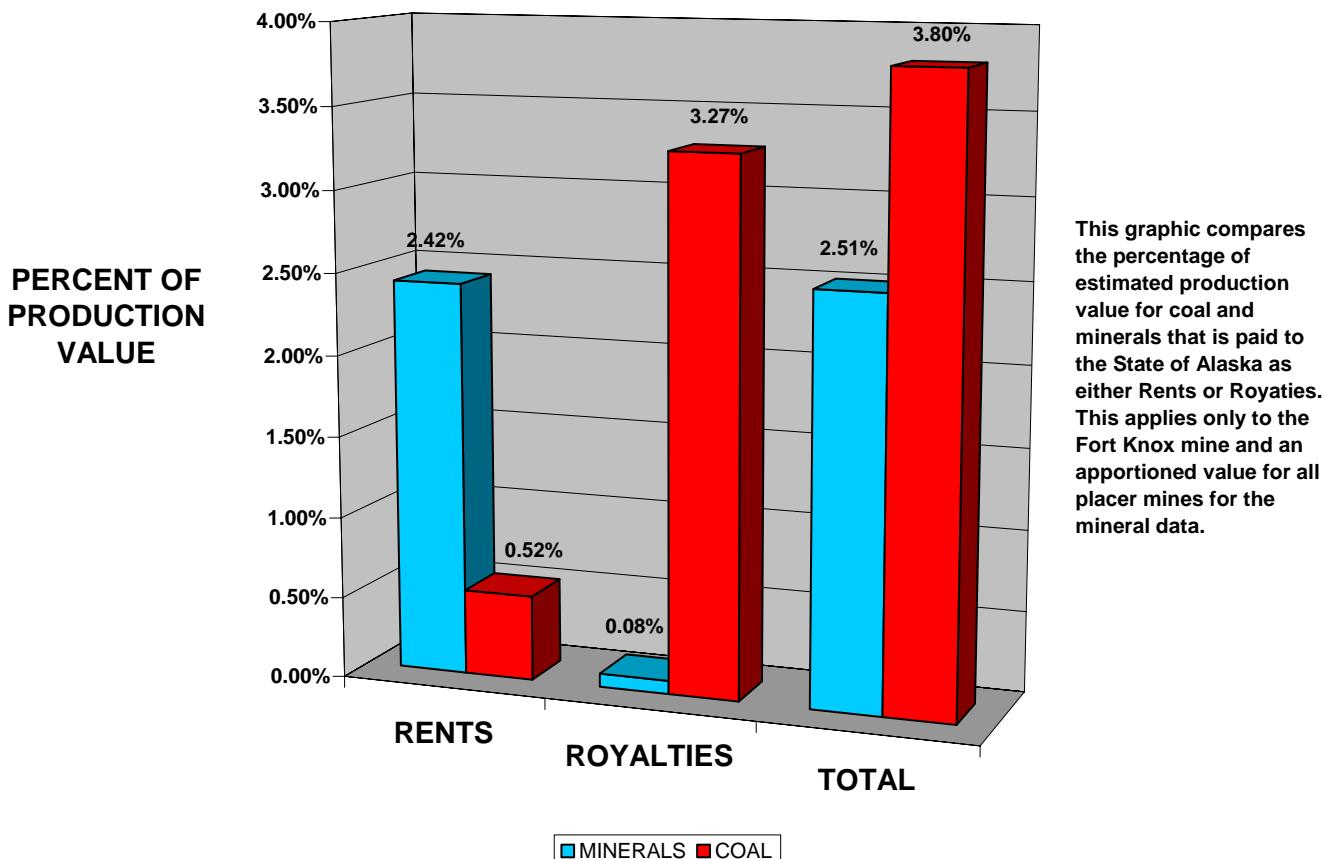
TOTAL STATE RENT & ROYALTY REVENUES BY RESOURCE TYPE

Source: Office of Economic Development



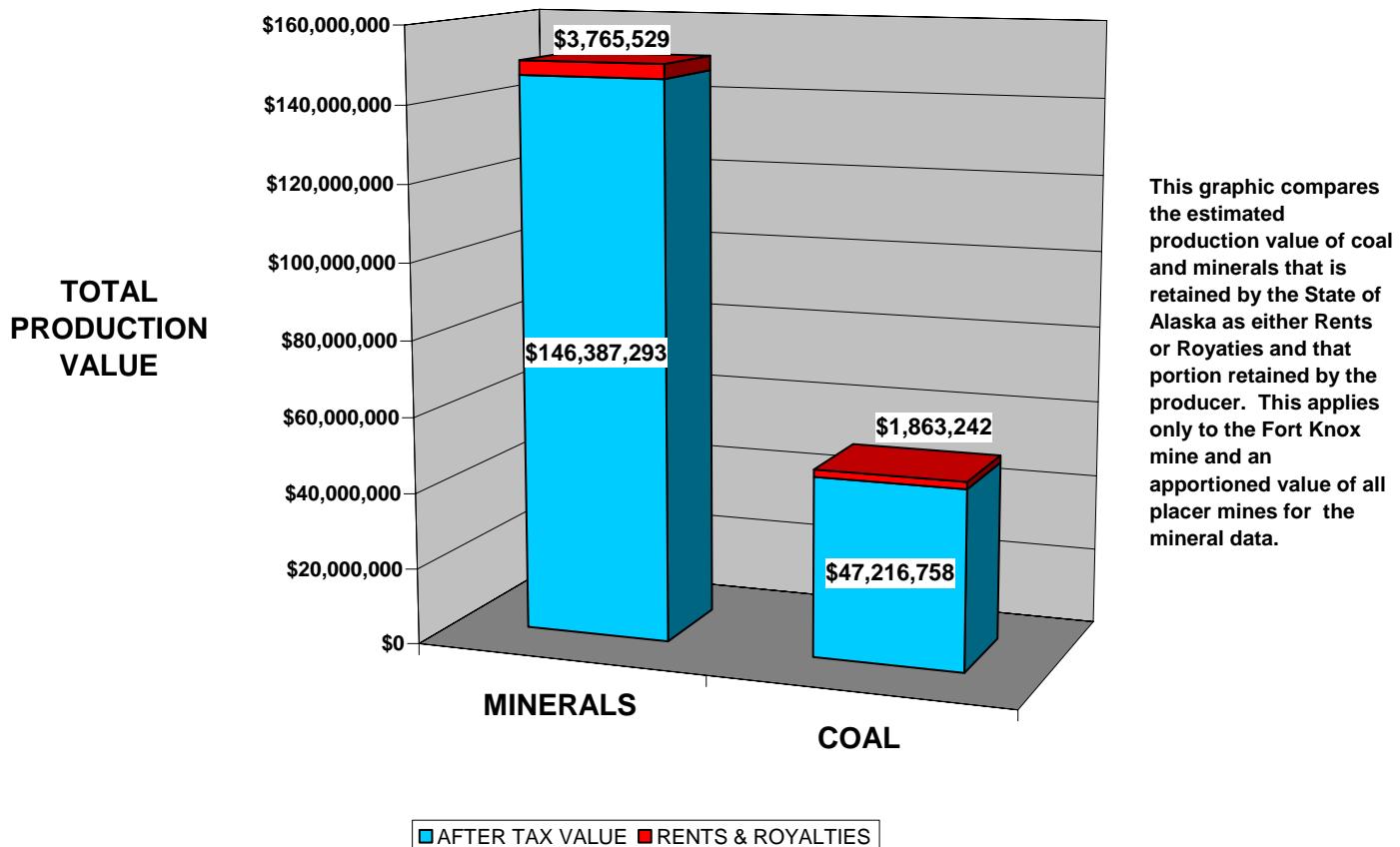
RENTS & ROYALTIES AS A PERCENT OF PRODUCTION VALUE 2005

Source: Alaska's Mineral Industry 2005 - Special Report 60 & Office of Econ. Development



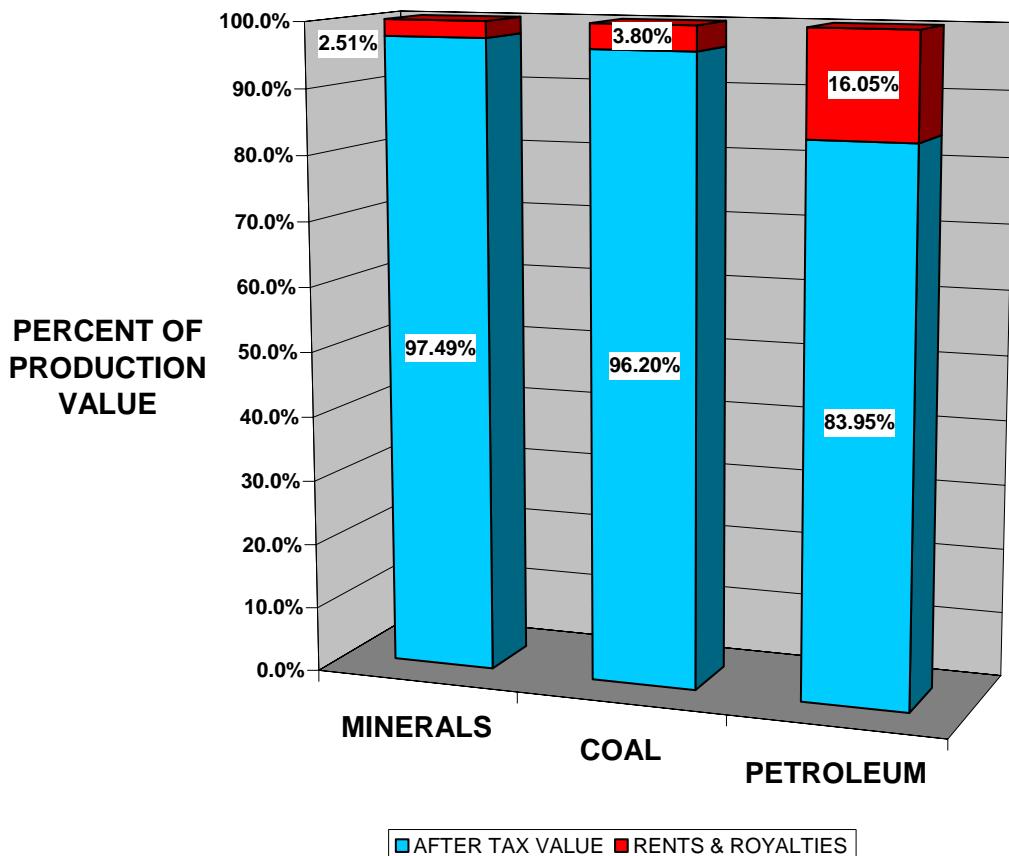
RENTS, ROYALTIES AND AFTER TAX VALUE 2005

Source: Alaska's Mineral Industry 2005 - Special Report 60 & Office of Econ. Development



RENTS & ROYALTIES AS A PERCENT OF PRODUCTION VALUE 2005

Source: Alaska's Mineral Industry 2005 - Special Report 60, Office of Econ. Development & Dept. of Revenue Estimates



This graphic compares the percentage of estimated production value for coal, minerals and petroleum that is paid to the State of Alaska as either Rents or Royalties and that portion retained by the producer. This applies only to the Fort Knox mine and apportioned value for all placer mines for the minerals data.

TOTAL TAXES AS A PERCENT OF PRODUCTION VALUE 2005

Source: Alaska's Mineral Industry 2005 - Special Report 60, Office of Econ. Development & Dept. of Revenue Estimates

