

**ALASKA STATE LEGISLATURE
HOUSE RESOURCES STANDING COMMITTEE**

February 15, 2016

1:10 p.m.

MEMBERS PRESENT

Representative David Talerico, Co-Chair
Representative Mike Hawker, Vice Chair
Representative Craig Johnson
Representative Kurt Olson
Representative Paul Seaton
Representative Andy Josephson
Representative Geran Tarr

MEMBERS ABSENT

Representative Benjamin Nageak, Co-Chair
Representative Bob Herron

COMMITTEE CALENDAR

HOUSE BILL NO. 253

"An Act requiring the electronic filing of a tax return or report with the Department of Revenue; establishing a civil penalty for failure to electronically file a return or report; relating to exemptions from the mining license tax; relating to the mining license tax rate; relating to mining license application, renewal, and fees; and providing for an effective date."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 253

SHORT TITLE: ELCTRNC TAX RETURN;MINING LIC. TAX & FEES

SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

01/19/16	(H)	READ THE FIRST TIME - REFERRALS
01/19/16	(H)	RES, FIN
02/15/16	(H)	RES AT 1:00 PM BARNES 124

WITNESS REGISTER

JERRY BURNETT, Deputy Commissioner

Office of the Commissioner
Department of Revenue (DOR)
Juneau, Alaska

POSITION STATEMENT: On behalf of the governor, introduced HB 253 by way of a PowerPoint presentation entitled, "Mining License Tax, HB 253."

FRED PARADY, Deputy Commissioner
Office of the Commissioner
Department of Commerce, Community & Economic Development (DCCED)
Juneau, Alaska

POSITION STATEMENT: On behalf of the governor, answered questions in regard to HB 253.

ED FOGELS, Deputy Commissioner
Office of the Commissioner
Department of Natural Resources (DNR)
Juneau, Alaska

POSITION STATEMENT: On behalf of the governor, answered questions in regard to HB 253.

ACTION NARRATIVE

[1:10:29 PM](#)

CO-CHAIR DAVID TALERICO called the House Resources Standing Committee meeting to order at 1:10 p.m. Representatives Seaton, Johnson, Tarr, Josephson, and Talerico were present at the call to order. Representatives Hawker and Olson arrived as the meeting was in progress.

CO-CHAIR TALERICO stated the following:

Everyone is aware that we suffered a terrible tragedy this weekend and a loss that's felt by everyone in the building. Our hearts and thoughts go out to Representative Gruenberg's family at this time. It is a very difficult situation for all of us and the incredible multitude of friends, as well, that Representative Gruenberg established over the years. There have been sentiments expressed, he will be incredibly deeply missed by each and every one of us. Those who served with him for a long, long period of time and those of us that just knew him for the last few years. His demeanor is something that I think we could probably all try and ... make a good copy of

that, those of us that knew him, his demeanor, his willingness to speak to people, and his deep desire to always do what was in the best interest of the people of the State of Alaska. I think Max always, always told me and reminded me that he was here to help people and that was his goal. And, he did that well and he did it with fervor and it accomplished quite a few things. So, in respect to that, if everyone wouldn't mind, I'd like to ask everyone just to rise and have a moment of silence for Representative Gruenberg.

[The committee stood in a moment of silence for Representative Max Gruenberg.]

HB 253-ELCTRNC TAX RETURN;MINING LIC. TAX & FEES

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CO-CHAIR TALERICO announced that the only order of business is HOUSE BILL NO. 253, "An Act requiring the electronic filing of a tax return or report with the Department of Revenue; establishing a civil penalty for failure to electronically file a return or report; relating to exemptions from the mining license tax; relating to the mining license tax rate; relating to mining license application, renewal, and fees; and providing for an effective date."

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JERRY BURNETT, Deputy Commissioner, Office of the Commissioner, Department of Revenue (DOR), on behalf of the governor, introduced HB 253 by way of a PowerPoint presentation entitled, "Mining License Tax, HB 253." Turning to slide 2, "Mining License Tax Increase, he explained that the bill would require the electronic filing of a tax return or report [with DOR].

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The committee took a brief at-ease.

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MR. BURNETT stated that HB 253: would require the electronic filing of a tax return or report with the Department of Revenue (DOR); would establish a civil penalty for failure to electronically file a return or report; relates to exemptions

from the mining license tax; relates to the mining license tax rate; relates to mining license application, renewal, and fees; and would provide for an effective date.

MR. BURNETT turned to slide 3, "Mining Tax History," and advised that the state began taxing mines in 1913, that the tax has been restructured several times, and that the original mining license tax was 0.5 percent tax on mining net income over \$5,000. The tax is collected on both net income from mining operations and mining-related royalties. So, the lessor of a mine, the owner of a mine, pays the mining license tax on the royalties.

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REPRESENTATIVE SEATON observed the bill's title does not include royalties, and asked whether the bill includes royalties.

MR. BURNETT replied the bill does nothing to change the royalties that the state collects on mining operations. Most of the large mines that would be affected by this bill are not on state land, rather they are on federal lands, Native corporation lands, or other lands. He said he is aware of only one large operating mine on state lands.

REPRESENTATIVE SEATON surmised the bill relates to net income on mining-related royalties. Therefore, he surmised, if a Native corporation is receiving royalties from mines it will tax the royalties, but not deal in any manner with royalties from state land that would be paid to the state.

MR. BURNETT responded that Representative Seaton is correct. If the owner of property that's leased to a mining operation collects royalties, those royalties are taxed under the law.

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CO-CHAIR TALERICO requested Mr. Burnett to identify the six large mines.

MR. BURNETT said these mines will be reviewed in a coming slide.

MR. BURNETT continued his discussion of slide 3. He explained that the tax is primarily businesses engaged in coal and hard-rock mining. He turned to slide 4, "Mining Tax History (Continued)," and said that between 1915 and 1953 there were numerous changes to the tax rates and the tax-free net income base, and in 1951 a 3.5 year exemption was adopted for new

mining operations, and that the current tax structure has been in place since 1955. He pointed to the chart and noted that the tax under current law is as follows: no tax until at least \$40,000 net income; 3 percent over \$40,000; 5 percent over \$50,000; and 7 percent over \$100,000.

CO-CHAIR TALERICO pointed out that the history being discussed is prior to statehood.

MR. BURNETT agreed, and said the tax was several years before statehood and has continued in its same form since then.

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ED FOGELS, Deputy Commissioner, Office of the Commissioner, Department of Natural Resources (DNR), drew attention to slide 5, "Large mining projects in Alaska," and said the map depicts the operating mines in Alaska, mines currently in permitting, and the significant projects in pre-permitting status. He then reviewed the six operating mines. The Red Dog Mine is an open pit lead and zinc mine operated by Tech Alaska and is located on NANA Regional Corporation land. It is one of the world's largest zinc producing mines, employs 610 individuals, and is the only taxpayer in the Northwest Arctic Borough. The Fort Knox Mine is an open pit gold mine located near Fairbanks on Alaska Mental Health Trust lands and private lands, is operated by Fairbanks Gold Mining, employs 650 individuals, and is the largest taxpayer in the Fairbanks Northstar Borough. The Pogo Mine is an underground gold mine located near Delta Junction on state land, employs 320 individuals, and is the only major hard-rock mine located on general state land. The Usibelli Coal Mine is a subbituminous low sulfur coal strip mine is located on state land and employs 150 individuals. The Kensington Mine is located north of Juneau on U.S. Forest Service land, is operated by Coeur Alaska, is an underground gold mine, and employs 320 individuals. The Greens Creek Mine is an underground silver, zinc, lead, and gold mine, employs 415 people, is located about 18 miles southwest of Juneau on U.S. Forest Service and private lands, and is operated by Hecla Greens Creek Mining Company.

MR. FOGELS pointed out that the map also shows Nixon Fork Mine which is an underground gold mine near McGrath. It is on U.S. Bureau of Land Management (BLM) land, and since 2013 has been in temporary cessation due to low commodity prices and it is currently being maintained and monitored. The map also shows mines in permitting that include: Donlin Gold Mine; Chuitna Coal Mine; and Wishbone Hill Mine, although the Wishbone Hill Mine is

essentially permitted and is waiting for the markets to improve. Other mines shown on the map include: Arctic and Bornite; Livengood; Graphite 1; Pebble; Palmer; Niblack; and Bokan Mountain. The state is currently working with the owners of those properties regarding pre-permitting activities and none have submitted formal applications for the large mine permits.

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CO-CHAIR TALERICO surmised Red Dog Mine and Fort Knox Mine are major contributors to their local municipalities as far as their tax base goes. He asked whether the other mines contribute to their local municipal governments as well.

MR. FOGELS responded that they all do. He noted that the Greens Creek and Kensington mines are very significant contributors to the Juneau economy, and the Usibelli Mine is a huge contributor to the Denali Borough and the Healy community.

MR. BURNETT added that Kensington and Greens Creek mines are the top two local property taxpayers in Juneau, and that Usibelli Mine is a major taxpayer for the Denali Borough in the approximate amount of \$100,000 a year in severance taxes. He noted that the employees pay taxes, and a lot of the infrastructure has been built for and by these mines. For example, the Greens Creek Mine buys excess electricity from the hydroelectric plant in Juneau, which has resulted in lowering the utility bills for Juneau residents. He referred to the discussion of another hydro plant that is proposed near Juneau that would offer zone-area heating in downtown Juneau. This proposed plant would only be made possible if Kensington Mine is the anchor client for electricity. Mines are incredibly important local infrastructure, local tax base, local jobs, and economic engines to the communities where they are located.

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REPRESENTATIVE SEATON referred to the calculation of mining net income, and asked whether it is net profit after corporate income tax or just on expenses and revenue.

MR. BURNETT answered it is before the corporate income tax; the corporate income tax has been allocated based on factors for employment and so forth in Alaska to the company's national income. In other words, he explained, when a mine pays corporate income tax, it would be a deduction from the whole company's corporate income tax, and then allocated back. The

state does receive a fairly significant amount of corporate income tax from mines. He said he will be providing the committee with a chart depicting corporate income tax by sector for all the sectors in the economy. In many years the mines could easily be the second largest sector, after oil and gas, for corporate income tax depending on how commodity prices are going during that time period.

REPRESENTATIVE SEATON referred to the base amounts that are excluded from taxation and their different rates on net income. He asked whether there is a comparison of how long it takes mines to reach net income to where the mines are taxable versus non-taxable because the tax is based on net income rather than gross income.

MR. BURNETT replied he intends to provide some of that information to the committee after this hearing. He said it is highly variable because, like the oil and gas industry, these companies are somewhat at the mercy of commodity prices. It could be very profitable or not so profitable at any given period of time; it as a relatively large gamble.

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REPRESENTATIVE JOSEPHSON understood that the mining-related royalties are not directly a subject of the bill except when looking at net income and the tax rate. He inquired whether the administration considered adjusting the royalty rate itself.

MR. BURNETT deferred to Mr. Fogels because the Department of Natural Resources (DNR) handles royalties. People are aware of it and it was discussed, but it is not part of the proposal here.

MR. FOGELS responded that DNR did not propose any adjustments to the royalty structure this year.

REPRESENTATIVE JOSEPHSON noted that traditionally the tax for oil is 12.5 percent, and asked what the amount is on royalty and, if it is different, why the difference exists.

MR. FOGELS answered that mining royalties are 3 percent, and only on general state lands which, currently, would only apply to the Pogo Mine. The royalty structure for coal is different for the Usibelli Mine, and basically the major hard-rock mine is paying royalties currently, and there are royalties from smaller

placer operators in the state. He said he does not know why the difference exists between oil and gas and the mining royalties.

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REPRESENTATIVE SEATON asked the definition of the royalty base, and further asked whether it is on net profits, net income, gross value of the material, or net smelter return (NSR), in other words after the first wholesale value.

MR. FOGELS replied it is definitely on the net, but he is unsure whether it is the value or the profit. He said he will get back to the committee in this regard.

REPRESENTATIVE SEATON said he would like to receive an answer because if there is a mine on state land, the royalty is the state's ownership portion. He said his understanding from the past is that the royalty was based on net profit; therefore, an expensive and inefficient operation could write off a lot of expenses against revenues. In that regard, he opined, Alaskans receive very little or nothing from their royalty interests.

MR. FOGELS advised that he found the answer and said the production royalties are established by AS 38.05.212(b)(1), which reads:

(b) The production royalty

(1) is three percent of net income as determined under AS 43.65; and

MR. FOGELS said it parallels the mining license tax.

REPRESENTATIVE SEATON stressed it is important to look closely at the actual factors because some mines are 17 years into their 20-year life and have not reached that profitability point for the state to receive any royalty for its ownership share.

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MR. BURNETT resumed his presentation and displayed slide 6, "Mines in Alaska." He advised there are five large hard-rock mines, one coal mine, and 200 small placer mines that, combined, have an economic impact similar to one large mine.

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REPRESENTATIVE HAWKER noted that slide 6 totals 206 mines, yet in 2015 there were 468 taxpayers. He asked why the difference.

MR. BURNETT explained that there are approximately 500 plus taxpayers filing returns, and in 2014, 13 were in the highest tax bracket. In 2014 the [highest tax bracket] had a total net income of approximately \$561 million and paid taxes on that amount. The next group is much smaller with a total income net on their tax return of approximately \$1 million. He explained that there are different brackets, with small placer gold miners for example that pay low tax rates in the \$40,000-\$100,000 range. Some may be below the \$40,000 range but still file a tax return because they continue to operate and from year-to-year they may be profitable to the level....

REPRESENTATIVE HAWKER surmised that while the state had 468 paying taxpayers in 2015, by taking the top paying 200 of the 468 there is a combination that aggregates to approximately one large mine.

MR. BURNETT said that would be fairly close to being correct.

REPRESENTATIVE HAWKER asked whether that is the intent of the slide.

MR. BURNETT agreed. The intent is to show there are big mines and many little mines, and it takes many small mines to make up the big mine. Plus, there are many little mines that do not make any money at all.

REPRESENTATIVE HAWKER said there are 260 or more mines if the chart is finished at the bottom, and these are fairly de minimis in the whole equation.

MR. BURNETT replied exactly, and advised he will send the committee a document showing the taxes paid and income by size within those brackets.

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MR. BURNETT continued his presentation, turning to slide 7, "Mining Tax Proposal." He advised that HB 253 proposes to: increase the tax rate on the highest bracket of net income greater than \$100,000 from 7 percent to 9 percent; remove the 3.5 year exemption for startups; require electronic filing and provide an exemption process; and add an application and renewal fee for tax license which is a substitute for a business license

at the same rate as a standard business license. He noted that currently mines are exempt from requiring a business license.

CO-CHAIR TALERICO asked the actual increase percentage of the taxes themselves.

MR. BURNETT responded that dividing 2 by 7 equals 0.28, and advised that it is accurate to state that it is an increase of 2 percent, but it is a 28 percent higher tax rate.

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REPRESENTATIVE SEATON queried about the efficiency of requiring a separate mining license that costs the same amount as the business license and exempting mines from the business license.

MR. BURNETT answered that he is uncertain whether there is a particular efficiency other than the fact that these companies, unlike other businesses, are paying a mining license tax anyway. There would be the same financial effect by simply requiring mining operations to have a business license and charging like any other business, and currently mines are exempt from a business license requirement.

REPRESENTATIVE SEATON asked for information regarding the efficiency of having two different licenses, and further asked whether the licenses are issued by two different agencies or by the same agency.

MR. BURNETT replied that the Department of Commerce, Community & Economic Development issues standard business licenses.

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REPRESENTATIVE HAWKER inquired about the role of the Department of Commerce, Community & Economic Development on HB 253.

FRED PARADY, Deputy Commissioner, Office of the Commissioner, Department of Commerce, Community & Economic Development (DCCED), responded that DCCED's role is around the business tax.

REPRESENTATIVE HAWKER noted that the business license costs \$50.

MR. PARADY answered that he is before the committee to support this effort.

REPRESENTATIVE HAWKER observed that Mr. Burnett's presentation does not go into the Exploration Incentive Credit provision under Title 27. He asked how that credit plays into the mining tax as it exists in the state today.

MR. BURNETT deferred to Mr. Fogels.

MR. FOGELS replied that the Exploration Incentive Credit allows a company to deduct up to \$20 million from its tax burden once production begins, and the company's deductions would be based upon exploration expenses incurred to locate the deposit.

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REPRESENTATIVE SEATON requested that, at some point, the committee be advised whether those credits are removed from costs assessing net income or whether they are reused and those same costs are then lowering net income.

MR. BURNETT responded that he would get back specifically in this regard, but noted that these are expenditures occurring in years prior to when the tax is being paid so it would be difficult to double them up.

REPRESENTATIVE SEATON requested that Mr. Burnett let the committee know whether exploration costs can be rolled forward for subtraction from when development takes place, or whether this is a totally single annual expenditure and income.

MR. BURNETT agreed to do so.

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MR. PARADY returned to previous Representative Hawker's question, and advised that his presence is in support of HB 253 on behalf of the administration. He said his presence is primarily driven by his background of 30 years in the mining industry. Although DCCED is not the bill's home department, he is present in support of the efforts in this regard.

REPRESENTATIVE HAWKER replied, "Acknowledging resident expert."

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CO-CHAIR TALERICO, in regard to the proposal to remove the 3.5 year exemption, presumed that those are typically development costs and that development costs are deducted from the gross

revenue. He further presumed that operations and overhead costs are part of what is deducted from gross revenue, along with development costs for new locations and new pits. He asked whether development costs of a mine are what is covered under the exemption. He further asked how it got to one-half year on the exemption.

MR. BURNETT replied that the one-half year occurred in 1955 and has not been revisited. The tax is paid on an annual basis so 3.5 years is awkward to handle. He confirmed that development costs are deductible as part of the net income calculation, so the expenses on the mine site for the purposes of that mine will be deducted. The 3.5 year exemption allows a mine additional return on capital during the first few years, but since this is a net tax it still would never bring a mine below zero profit regardless of the size of the net profit tax.

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REPRESENTATIVE JOSEPHSON recalled that when he asked Mr. Fogels about the establishment of the royalty rate, Mr. Fogels said it was designed to mirror the tax rate. Since the current tax rate goes up to 7 percent, he asked why it would not mirror the 7 percent where there was net money income over \$100,000. He mused that the answer could be that it was designed in the culture of the 1872 Mining Act where there was an acceptance of very low tax rates or great incentives to mine.

MR. FOGELS answered no, it is not mirroring the mining license tax, per se, it is just that the manner the net income is determined is the same determination as under the mining license tax and has no bearing on the 1872 law at all.

REPRESENTATIVE JOSEPHSON said he thought that Mr. Fogels had earlier said it was designed to be analogous to the 3 percent rate for the \$40,000-\$50,000 mining net income. He reiterated that he had asked Mr. Fogels where the 3 percent came from, it is one-quarter of a royalty rate for oil.

MR. FOGELS responded that the 3 percent is in statute, and statute says it is a 3 percent of net income as determined under AS 43.65, which is the mining license tax. Therefore, the rate is set at 3 percent but the way to determine the net income is the same determination as for the mining license tax part of the statute.

MR. BURNETT added that the royalty rate applies for all of the income and is not bracketed at different incomes, unlike the tax which is a progressive profits tax.

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REPRESENTATIVE HAWKER asked whether anyone could recall the name of the lawsuit filed over royalties that was ultimately settled by the establishment of this royalty structure, and when that lawsuit was settled. He mentioned that he could only remember that it was when Jerry Gallagher was head of mines, and that he would try to track down the information.

MR. BURNETT answered that he would also try to locate the information.

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MR. BURNETT returned to his presentation. He moved to slide 8, "Relative Mining Tax Rate," and advised that relative to other taxes, the mining taxes of most other states are based on value or tonnage, not net income. For example: Wyoming is tax on value that varies by resource, 2 percent on sand and gravel, 7 percent on surface coal; South Dakota is 10 percent on profits or royalties, \$4 per ounce of gold and not a percentage at all; Wisconsin is 3 percent to 15 percent progressive tax on net mining proceeds; and Colorado is 2.25 percent of *gross* income exceeding \$19 million. He said he will provide a document to members showing the severance taxes in all of the other states.

REPRESENTATIVE HAWKER commented that it would be helpful to see a multi-state comparison of total government take in that it is an important distinction here.

MR. BURNETT replied that the Senate Resources Standing Committee requested it be able to look at government take so it will be part of what will be looked at.

CO-CHAIR TALERICO said, "We have kind of a percentage breakdown on the actual minerals that are mined." Wyoming has a massive amount of coal compared to metals, which may tweak things.

MR. BURNETT responded that it is fairly complex because the government take, especially in Alaska, is largely local governments, so it is not easy to get all of the information necessary to perform that calculation. However, it should be possible to calculate estimates that make sense.

CO-CHAIR TALERICO asked for the comparison of the actual taxes, in that some [states] do not necessarily do the net tax as the committee is discussing, they may just have a flat 5 percent across the board on what they produce....

MR. BURNETT interjected that it could be \$0.05 a ton. He said the information will be provided to the committee quickly.

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REPRESENTATIVE SEATON requested that the structure of royalty be looked at. He allowed it will be different in the Lower 48 where subsurface rights may not hold to the state, but the comparisons would be helpful.

MR. BURNETT reiterated that it is fairly complex because, for the most part, states do not hold mineral rights as in Alaska.

MR. PARADY added that whether royalty belongs in government take is a debatable proposition in the context that royalties are generally speaking of payment to ownership rather than a taxation that goes to the state itself. Particularly, he added, in a state that has a land ownership pattern either with split estate where the subsurface estate is separate from the surface estate. For example, the Union Pacific Railroad in Wyoming has mineral rights to 4.4 million acres of ground and that royalty rate is 8 percent, where on federal sections it is 5 percent, and the difference theoretically is the difference in corporate income tax that is paid by that royalty holder. There are huge ranges of influences, such as whether discussing gross or net income, what point of valuation is chosen, and the combination of the rollup of local and state. He said the best summary possible will be provided, but noted that it is still a very arcane subject matter.

REPRESENTATIVE HAWKER advised that he and Representative Seaton have a long history with this subject. He agreed with Mr. Parady that royalty is usually what represents ownership interest in the severed resource. It is unusual for it to be on a net income basis rather than at some calculus that "when you take the resource from me, you leave me something." He asked whether the administration has a position on the propriety of a cross-recovery net profits royalty structure.

MR. PARADY replied no, not to his knowledge, but it is an interesting element of the debate.

REPRESENTATIVE HAWKER asked what "no" represented.

MR. PARADY responded that "no was a no position."

1:56:08 PM

MR. BURNETT turned to slide 9, "Impacts of Tax Proposal," and resumed his presentation. He said that the effect of this tax proposal on large and profitable mines, most of which have incomes above \$100,000, would be a rise in the effective tax rate from 7 percent to approximately 9 percent. For small mining operations, there would be little to no effect from the tax rate change; however, removing the 3.5 year exemption might have some effect on a startup mine. He allowed he is uncertain as to that effect and suggested that if there is an exemption that it be made in whole years because it is difficult to cut an entity's annual tax in half.

CO-CHAIR TALERICO asked whether properties that are currently in the process of permitting would be grandfathered in should the 3.5 year exemption be removed.

MR. BURNETT answered that HB 253 has no grandfather proposal, but he understands why someone could believe that was a reasonable issue to review. He pointed out that no large mines are expected to come online in the next four to five years, although, a number of mines are in the permitting process and have made large investments at this point.

REPRESENTATIVE HAWKER pointed out that the state has quite a history of retroactive implementation and assessment of taxes on one of its industries, and obviously it is not being done here. He asked whether the committee should consider a retroactive implementation since the interest is really raising revenues.

MR. BURNETT replied that there has been absolutely no discussion of retroactive tax implications here, nor does he believe anyone has suggested that it would be a good policy in this case.

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REPRESENTATIVE TARR referred to the suspension of activity at Nixon Fork Mine due to low commodity prices. She asked whether low commodity prices were looked at when potential impacts of the bill were being assessed. She surmised that some of [the proposals] would become less of an issue if prices increased.

MR. BURNETT responded that this is a net profits tax; a company must actually earn a profit in order for a tax to be paid. High commodity prices cause higher taxes with higher income, so where this tax has an effect is on the margin in between profitability and lack of economic return. There will always be a financial return on a profit and loss statement before paying this tax and there may not be an economic return at low commodity prices. The calculus, he explained, would be the difference between a financial and an economic return on a specific project. Mining in 2010 had a negative corporate income tax, in 2011 it contributed over \$80 million in corporate income tax, and in 2014 it was \$15 million. It is based on a company's nationwide profitability, so there is a tremendous variability.

REPRESENTATIVE SEATON asked if there is a slide of those years.

MR. BURNETT answered that a sector-by-sector comparison of corporate income tax returns will be provided.

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REPRESENTATIVE JOHNSON inquired as the amount of revenue that would be generated should the 3.5 year exemption be removed.

MR. BURNETT replied that, during the period of the fiscal note, no revenue can be predicted. However, when the next larger, tax paying mine comes onboard, the state would receive tax for 3.5 years that it would not have otherwise received.

REPRESENTATIVE JOHNSON asked whether it is conceivable that that could be the push point of not starting a mine.

MR. BURNETT answered that it is economically conceivable, but he does not know whether it would be likely.

REPRESENTATIVE JOHNSON said his question is whether the state would be putting up a roadblock that it may not need to because it is not generating any revenue for the foreseeable future. He asked why remove the exemption now and run that risk if the state could remove the exemption later.

MR. BURNETT allowed that that is a reasonable discussion point as the bill moves in this committee. He said it is certainly a concern that the mining industry has brought forth.

REPRESENTATIVE JOHNSON pointed to the Nixon Fork Mine being suspended due to low commodity prices and stated that obviously there is a balance to not produce that is fairly fragile and it is a big decision - it takes a while to start up. He expressed his concern that this proposed change might have that same effect. He opined that the 3.5 years does not generate a lot of revenue and could cause more doubts and discussion. If it would generate millions of dollars, that would be one thing, but it seems this is a gamble for not much [return].

MR. BURNETT replied that in the case of a large mine that is profitable at inception, this would bring in a fairly large amount of money. A large mine is not seen on the horizon during the period of the fiscal note, so an estimate cannot be made on what that would be.

[2:04:12 PM](#)

REPRESENTATIVE SEATON inquired whether waiting until a new mine is on the horizon and then considering [removal of the exemption] would give more pause to a company than would knowing what the tax rates are at the time that the company is going into exploration and development.

MR. BURNETT responded, "I think it would, I think you're correct there."

REPRESENTATIVE SEATON asked whether the 3.5 year exemption is only on the mining license tax or is also on the royalty.

MR. BURNETT answered that, to his knowledge, it is only on the mining license tax. He deferred to Mr. Fogels for confirmation.

MR. FOGELS offered his belief that the 3.5 year exemption does not apply to the royalty.

REPRESENTATIVE SEATON said it sounds like there is some question.

MR. BURNETT replied, "No, there's no question."

REPRESENTATIVE SEATON asked whether deferring taxes for three years while a mine is starting up and then the mine paying those taxes after starting up and recovering its costs would aid in the decision making of the companies while still providing money to the state.

MR. BURNETT responded that the administration will have to look at that issue. He said that is similar to how the 3.5 year exemption works as a practical matter now. He suggested that perhaps the rate could be set lower and not have the exemption, or perhaps the rate could be set higher and exempt it in the beginning so quicker cash flow would be achieved. It is a calculus between all of those things.

REPRESENTATIVE SEATON said he thinks the rate is a different calculation than a deferral, so that the state actually receives the money but that the economics of the development would be stimulated. He requested Mr. Burnett to review his suggestion and get back to the committee.

MR. BURNETT agreed to do so.

[2:07:12 PM](#)

MR. BURNETT continued his presentation. Turning to slide 10, "Revenue Impact," he said DOR estimates this would bring in an additional \$6 million per year beginning in fiscal year (FY) 2018 and would be highly variable over time due to commodity prices. It would also bring in an additional \$25,000 per year from the license fee and renewal. He noted that this does not account for any changes in mining activity that may occur either as a result of the bill or other unrelated factors.

REPRESENTATIVE HAWKER asked whether the \$25,000 increment on the renewal fee would cover the cost of administering this program.

MR. BURNETT believed that DOR is estimating no additional costs for administering this program on an annual basis.

REPRESENTATIVE HAWKER surmised that would be incremental costs of administering this program. He asked what the costs are today for administering the tax program.

MR. BURNETT replied that he does not know off the top of his head, but noted that the cost of administering the program is in DOR's annual report of tax operations and it shows the cost per dollar of administering each of the tax types that DOR has and how many full-time equivalents (FTEs). He said he will provide the information to the committee.

REPRESENTATIVE JOHNSON recalled that when Governor Walker rolled out his plan he said the mining tax or the license tax would generate \$11-\$12 million. He observed that [page 2 of the

fiscal note] states \$5.9 million in FY 2018 and asked whether something has changed.

MR. BURNETT responded he believes that what has changed is the expected values of mining, it is a commodity price issue. Like other commodity industries, commodity prices have declined over time, although gold has gone back up in value a bit in recent days. This tax will be volatile based on commodity prices and activity, he explained.

[2:09:53 PM](#)

REPRESENTATIVE HAWKER noted that currently the state does not have a business license charge [for mines]. He inquired whether the \$50 fee, if implemented, would be administrated by the Department of Revenue or moved over to the Department of Commerce, Community & Economic Development where all other business licenses are administrated.

MR. BURNETT understood it would be done along with the tax filings, so would be under the Department of Revenue.

REPRESENTATIVE HAWKER surmised that with the additional fee the state would not be incrementing the cost of providing services, but would simply be adding a line on a tax returns.

MR. BURNETT answered, "Pretty much, yeah, I think that's a relatively simple way to look at it, yes."

[2:11:03 PM](#)

MR. BURNETT returned to his presentation. Addressing slide 11, "Implementation Cost," he said there will be a one-time cost [\$100,000] to reprogram the system, with no additional incremental costs to administer the tax program.

MR. BURNETT turned to slides 12-13, "Closing the Budget Gap," and stated that the [FY 2017 baseline revenue after proposed legislation] would be \$4.285 billion based on the assumptions of Governor Walker's program of the [proposed] Alaska Permanent Fund Protection Act, revenue from existing taxes and fees, and earnings on savings. Spending reductions in FY 2017 would total \$500 million. New revenues from the proposals would be as follows: mining [starting in 2018] at \$6 million; fishing at \$18 million; tourism at \$15 million; motor fuel at \$49 million; alcohol at \$40 million; tobacco at \$29 million; oil & gas at \$200 million; and income tax [half in FY 2017; first full year

is FY 2018] at \$200 million. The total with reductions and new revenues would be \$5.242 billion.

REPRESENTATIVE HAWKER observed from slide 12 that reformation of the oil and gas credits is being characterized as a spending reduction due to being refundable tax credits. He posited that those are really a tax increase upon those companies that would not be receiving the benefit of those credits.

MR. BURNETT replied that the refundable tax credits have been shown as a budget item in the operating budget since the inception of the refundable credits in approximately 2006. Therefore, even though it is shown differently to the extent that those are a budgetary item on an annual basis, it is correct to characterize them both directions.

REPRESENTATIVE HAWKER quipped that Mr. Burnett offered that explanation with almost a straight face.

[2:13:47 PM](#)

REPRESENTATIVE TARR referred to slide 10 and offered her understanding that there currently is no mining license fee, so the proposal is to go with [\$50] because that is the other established license fee, and that the [annual] renewal would be \$50. This fee is small, she posited, particularly in a net profits based tax system where the only revenue the state might receive would be through this license. She asked whether there had been any consideration of something similar to 2016 pricing.

MR. BURNETT answered not at this time. He believed that the discussion was to match this with any other business activity in the state, because the state is going to tax their profits so the state would license a mine just like any other business.

[2:14:51 PM](#)

MR. BURNETT resumed his presentation to provide a sectional analysis of HB 253 as outlined on slides 14-16, "Sectional Analysis." He explained the sections as follows. Section 1 would add the tax penalty for failure to file electronically unless an exemption is received. Section 2 would require electronic submission of tax returns, license application, and other documents submitted. This would change the general tax statutes so it would be applicable to all the taxes administered by the Department of Revenue This section would also provide a process to request an exemption. Section 3 would remove the 3.5

year exemption from the mining tax for new mining operations until after production begins, and any persons engaged in the business of mining would be required to obtain a license and file an annual mining license tax return. He said he thinks there is something wrong in this paragraph and he will fix it.

REPRESENTATIVE JOSEPHSON noted that the first sentence of Section 3 implies that there would be a 3.5 year exemption once production begins. However, the administration is proposing to eliminate that exemption.

MR. BURNETT apologized that the sentences are written awkwardly and said the sentences need to be rewritten to properly match what he is trying to say.

[2:16:16 PM](#)

MR. BURNETT turned to slide 15 to continue his review of the Sectional Analysis. He said Section 4 would increase the highest tax rate from 7 percent to 9 percent for taxable income, which is a 2 percent increase or 28 percent increase.

[2:16:28 PM](#)

REPRESENTATIVE SEATON understood that the mining and license tax would be done at the same time the company files its tax return. He inquired whether that means the company would be mining for a year without a license or whether there would be an initial license that must be applied for and then the state performs renewals with the tax return.

MR. BURNETT offered his understanding that DOR would assess this on the first tax return after the effective date of the bill, not prior to going into business.

REPRESENTATIVE SEATON asked whether that is totally antithetical to the state's business licenses, which is that a company must have a business license before conducting business in the state. He said it appears to be a mismatch even though the idea is to treat them the same.

MR. BURNETT replied it would do two things: it would delay the implementation of the business license until that time; and it would make it possible for DOR to administer this program without additional costs to the program. He agreed with Representative Seaton that it would push out the time, but it

would make it a more efficient process to do the mining tax license fee.

[2:18:14 PM](#)

REPRESENTATIVE HAWKER inquired as to how thoroughly DOR audits the mining license tax returns.

MR. BURNETT responded that he will get back to the committee with an answer. He said other than the large taxpayers it is not something that would be a high priority relative to, say, oil and gas, or corporate income tax. Audits are performed and in the past taxpayers were identified as a result of activities by DOR and the taxpayers were brought into compliance. It is not like oil and gas where every return is audited.

REPRESENTATIVE HAWKER asked whether there is a provision in statute that says the state is required to assess the cost of whatever audit DOR performs against the taxpayer that DOR is auditing.

MR. BURNETT answered that he cannot answer because he cannot recall how that section reads.

[2:19:31 PM](#)

REPRESENTATIVE JOHNSON stated, "If we could carry the logic out of what Representative Seaton said, if we just did that with all business licenses we could get rid of the licensing division."

MR. BURNETT replied that it would be a very simple task if a business tax was to be established on all businesses so that sometime within the annual cycle they all have to file a tax return. Currently they do not have to file a tax return.

REPRESENTATIVE JOHNSON said it might be something to look at.

REPRESENTATIVE OLSON suggested putting it on a calendar year.

[2:20:16 PM](#)

MR. BURNETT continued his presentation and review of the sectional analysis. He returned to slide 15 and explained the following: Section 5 would conform language related to the requirement to submit tax returns or reports electronically. It would delete the current requirement that taxpayers their submit returns to the department in Juneau. Section 6 would establish

the mining license fee at \$50 per year, a license renewal fee at \$50, and would change the due date for application and renewals from May 1 to January 1.

[2:20:42 PM](#)

REPRESENTATIVE HAWKER surmised the intention is that this would be assessed on the tax return regardless of whether the tax return showed no taxes were owed due to any of the available credits or exemptions in current statute.

MR. BURNETT responded that that is his understanding of it.

REPRESENTATIVE HAWKER asked whether under current law someone with no liability is not required to file a tax return or whether anyone with activity must file and demonstrate whatever degree of taxable offset that the taxpayer might have.

MR. BURNETT understood that people engaged in a mining operation are supposed to file a tax return. He noted that DOR has a number of zero and below zero returns.

[2:21:46 PM](#)

REPRESENTATIVE OLSON asked what the cost is to DOR of handling a \$50 transaction every year.

MR. BURNETT answered he does not believe it will cost much at all if it is handled electronically through the filing system and assessed with all the other applications, so it should not be anything that shows an incremental cost.

[2:22:17 PM](#)

MR. BURNETT resumed his review of the sectional analysis on slides 15-16. He explained the sections as follows. Section 7 would conform language related to the repeal of the 3.5 year tax exemption. Section 8 is the applicability language that would clarify that the change in Section 3 would apply to all new mining operations. Section 9 is transition language so that the language that would be repealed in Section 7 would be read as it was before the effective date while administering a tax credit to a person who began a mining operation before the effective date. Section 10 is transitional language that would allow for regulations prior to the effective date of the bill. Section 11 would provide that Section 10 would take effect immediately for the transitional language. Section 12 would provide an

effective date [of 7/1/16] for the rest of the bill, including the tax rate change.

MR. BURNETT concluded by stating that he will provide the committee with the documents and information requested.

[2:23:27 PM](#)

REPRESENTATIVE SEATON asked whether there are any other purposes or implications, other than the fee, for having a business license versus not having a business license. For example, whether a company is required to have personnel withholdings or workers' compensation.

MR. PARADY replied he will need to get a deeper answer to the question relative to workers' compensation because DCCED has roughly 67,000 business licenses in the Division of Corporations, Business and Professional Licensing (CBPL) group.

REPRESENTATIVE SEATON commented that he is trying to understand the mining license and how that corresponds with a business license, and the implications of having a business license and not having a business license.

[2:24:41 PM](#)

REPRESENTATIVE TARR referred to the issue of commodity prices and requested that the committee receive more detailed information regarding anticipated revenue as to the changes of a 25 percent to 30 percent increase in commodity prices, gold probably being the most relevant.

MR. BURNETT agreed to do some of that, but pointed out the highest value mineral in Alaska might be zinc or some other non-gold mineral. Even though gold is thought of being valuable, it does not have the volume that the others do.

REPRESENTATIVE TARR suggested that the mineral resource with the most activity in Alaska be used.

[2:25:38 PM](#)

REPRESENTATIVE JOSEPHSON referred to Bob Loeffler's previous presentation regarding the impact of mining, tourism, and fisheries on Alaska's revenue. He stated he is still curious about the derivation of the 28 percent increase or 2 percentage points. He related that from his tour of the Fort Knox Mine it was obviously a massive capital expenditure investment and in an

amateur's eye it appeared to be more costly than oil and gas although he is unsure of that. Purely anecdotally, he surmised that the environmental residual risk in mining is greater than that of oil and gas, although he could be wrong since it is known from Alaska's legacy wells that there's environmental risk that continues. He asked how the 2 percent figure was arrived at rather than some other number.

MR. BURNETT responded that he cannot comment directly on that specific number at this point, but will provide the information that was used to make those decisions.

[2:27:16 PM](#)

REPRESENTATIVE SEATON observed the statement on slide 16 regarding Section 9 and understood that the 3.5 year transition language would apply "while administering a certain tax credit." He asked whether this is the mining exploration credit of \$20 million carried forward. He further asked how long that would be carried into a project.

MR. BURNETT answered he will get back to the committee on the specifics, but the intention is to not change the rules retroactively in this particular case so that it is read the same as it was before.

REPRESENTATIVE SEATON asked how far into the future this could apply and whether it means that this would apply to any mining claim even if production is not started within the next three to five years. He stated he does not understand the parameters of Section 9.

CO-CHAIR TALERICO requested a clear definition of mining production.

REPRESENTATIVE TARR requested that the committee also be provided with the relative volumes of extraction on an annual basis so members can think about how the price relates to that.

[2:29:25 PM](#)

REPRESENTATIVE HAWKER put forward that increased taxes are something to seriously consider when reviewing the state's current fiscal situation. He said what he sees here is that the administration is looking at increasing taxes across the board, basically, on the production of minerals. He inquired whether the administration has considered reducing or compromising the

major tax credits that are taken and available against this; for example, the education tax credit.

MR. BURNETT replied that serious consideration to removing the education tax credit has not been done, although it is worthy of discussions because the education tax credit is available on just about all the forms of business taxation and therefore does have an effect at times.

REPRESENTATIVE HAWKER recounted that the education credit on mining expired in 2013 and was reauthorized through 2021. He described it as something the legislature has done when times are particularly good. He requested that this be considered in regard to achieving parity amongst taxpayers in Alaska.

REPRESENTATIVE SEATON recalled, with regard to Representative Hawker's statement, that members were specifically looking at a mining program that wanted to have the tax credits go up to \$10 million because there was an initiative to do a certain mining school product. He agreed that times were good, the state had money and wanted to stimulate things, but within this current fiscal situation the question is whether the state can still afford to have those credits on the books and being used. He explained that education tax credits are a redirection of taxes that the taxpayers would be paying to the state to another institution. He said that he looks forward to the department coming back to the committee with ideas.

REPRESENTATIVE HAWKER clarified that the 2010 increase moved the education tax credit up from \$150,000 annually to \$5 million annually, not \$10 million.

REPRESENTATIVE SEATON recalled that the \$10 million was actually put forward on the table at the time of the discussions, and it was \$5 million that was settled on.

[HB 253 was held over.]

[2:35:10 PM](#)

ADJOURNMENT

There being no further business before the committee, the House Resources Standing Committee meeting was adjourned at 2:35 p.m.