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STATE COMMITTEE REPORT

DATE: 1/22/92

FURTHER: Finance

DATE TURNED INTO OFFICE: Jan 22, 1992

Resources Committee considered

SENATE BILL NO. 330

"An Act relating to an exemption from municipal property taxation for natural resources in place; and providing for an effective date."

and recommends:

replace with _____ CS _____ ()

or adopt previous _____ CS _____ ()

attaches amendment(s)

same title
 new title
 technical title change
(HB only)

adopts _____ Letter of Intent

further referral to the _____

do pass

do not pass

no recommendation

individual recommendations

NEW FISCAL NOTES: Dept/Date

zero fiscal notes _____

fiscal notes _____

appropriation--no fiscal note

PREVIOUS FISCAL NOTES: Dept/Date

zero fiscal notes DCRA 1/13/92

fiscal notes _____

DO PASS

Rich Helford
[Signature]
[Signature]
[Signature]
[Signature]
[Signature]

OTHER RECOMMENDATIONS:

[Signature]
Chair: Signature and Recommendation

A M E N D M E N T

OFFERED IN THE SENATE

BY THE SENATE RESOURCES COMMITTEE

TO: SB 330

Page 2, line 22:

Delete "stumpage"

FISCAL NOTE

STATE OF ALASKA
1992 LEGISLATIVE SESSION

BILL NO. SB 330

Revision Date: _____
Title: "...exemption from property taxation for natural resources in place."
Sponsor: Senator Adams
Requestor: _____

Department Affected: Community and Regional Affairs
BRU: Local Government Assistance
Component: State Assessor
COMPONENT SERIAL NO.

0	6	7	3
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EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL						
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REVENUE FUND SOURCE:						
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FUNDING: (Thousands of Dollars)

GENERAL FUND	0.0	0.0	0.0	0.0	0.0	0.0
FEDERAL FUNDS						
OTHER FUND SOURCE:						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

POSITIONS:

FULL-TIME	0.0	0.0	0.0	0.0	0.0	0.0
PART-TIME						
TEMPORARY						

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary.)

Prepared By: Remond Henderson
Division: Administrative Services Division
Approved by Commissioner: Ken Kelly
Agency: Department of Community and Regional Affairs

Phone: 465-4750
Date: 1/13/92
Date: 1-14-92

Alaska State Legislature

Senate District L
Al Adams

WHILE IN SESSION
P.O. Box V
State Capitol
Juneau, Alaska 99811
(907) 465-3707

OUT OF SESSION
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Kotzebue, Alaska 99752
(907) 442-3245

Official Business

TO: Senator Lloyd Jones, Chair
Senate Resources Committee

FROM: Senator Al Adams *APA*

RE: Senate Bill 330

DATE: January 17, 1992

Thank you for scheduling Senate Bill 330 pending referral from the Senate Community and Regional Affairs Committee.

This bill creates an exemption on the taxation of natural resources in place. As you may know, unless this legislation is passed this session, the state assessor and municipalities will have to begin the process of including these resources in their tax base. The exemption has broad support from both government and private sector interests.

Enclosed as background materials are:

- Bill copy
- 1992 Report to the Legislature on the Taxation on Natural Resources in Place
- Copy of 1990 statute that created a two year exemption for the purposes of studying this issue
- 1991 resolution of the Alaska Municipal League in support of this exemption
- 1991 Alaska Minerals Commission report placing this as their top legislative priority

A fiscal note has been requested, is expected shortly and will be forwarded to your office upon receipt.

Please feel free to contact Martha Stewart of my staff if you have questions.

Thank you.

KETCHIKAN SPORTS and WILDLIFE CLUB

P.O. Box 5122 • Ketchikan, Alaska 99901

City of Ketchikan
Parks and Recreation Division
344 Front st.
Ketchikan, Alaska 99901
(attn. Susie Daly)

Ms. Daly,

Jan. 3, 1992

The Ketchikan Sports and Wildlife Club, representing over 650 members, requests that an Indoor Shooting Range be included in the planning for the Recreation Center. This kind of facility would be a great benefit to Ketchikan residents, allowing programs such as Hunter Safety and Firearm Safety to be offered to the area. We have contacted several organizations and their response has been overwhelmingly in favor of such a facility in Ketchikan.

There are funds available through the Pittman Roberts act and the National Rifle Association to assist in the construction of Indoor Shooting Ranges. If you agree that this facility will be added to the planning of the Recreation Center, our organization will work toward getting these funds allocated. Please consider this request carefully and contact us if you approve of having an Indoor Shooting Range for Ketchikan residents.

Sincerely;

Lee Putman
Lee Putman NP
Ketchikan Sports
and Wildlife Club

cc; Rep. Robin Taylor
Rep. Cheri Davis
Sen. Lloyd Jones
Sen. Pat Rodey

*Ray - Terry
E. Larson is working on legis.
to reduce charter boat limit for
charter boat operators - Sag /
Commercial troll & sport fishermen
should support. - Need to talk to
Lee & Bob Pellett. L*

Testimony
SB 330
January 22, 1992

MY NAME IS KENT DAWSON. I AM HERE TODAY REPRESENTING THE ALASKAN PRODUCERS COUNCIL, WHICH IS A GROUP OF LARGE MINERAL PRODUCERS WITH AN INTEREST IN ALASKA DEVELOPMENT, INCLUDING SUCH FIRMS AS COMINCO, GREENS CREEK, ECHO BAY, AMERICAN COPPER AND NICKEL, AMAX, NORTH PACIFIC MINING, AND ALASKA GOLD.

THE ALASKAN PRODUCERS COUNCIL JOINS WITH THE MUNICIPAL LEAGUE IN SUPPORTING THIS LEGISLATION AND APPRECIATES THAT ALASKA MUNICIPALITIES HAVE ACKNOWLEDGED THE DETRIMENTAL EFFECT TO MINING DEVELOPMENT A TAX ON MINERALS IN PLACE WOULD CAUSE.

THE ALASKAN PRODUCERS COUNCIL WISHES TO ACKNOWLEDGE THE EXCELLENT JOB THE DEPARTMENT OF COMMUNITY AND REGIONAL AFFAIRS HAS DONE WITH THEIR RATHER DIFFICULT STUDY.



Resource Development Council

for Alaska, Inc.

121 West Fireweed Lane, Suite 250, Anchorage, Alaska 99503-26
Phone 937/276-0700 Fax 276-38

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Becky L. Gay

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RDC Position Paper - January, 1992 SB 330 - Resources in-place

The Resource Development Council for Alaska Inc., supports SB 330 and applauds the quick legislative action being taken to move this legislation. As the record shows, much consideration and study was given to this issue during the interim and support for the taxation change is nearly unanimous.

This issue is vital to minerals and timber companies and landowners with undeveloped resources that could be subject to municipal property taxes. SB 330 addresses the problem facing landowners, as well as local governments. Research has shown that the inventory process and tax assessment system would likely prove costly to municipalities and the state.

RDC believes SB 330, and its companion legislation in the House, represent a clean, concise exemption to the issue of taxing in-place resources. RDC's policy-making executive committee, which represents the 10,000 members of the non-profit organization, is on record supporting SB 330. RDC appreciates the opportunity to comment on this bill.

*For further information, contact Debbie Reinwand,
Executive Director, 276-0700*

MEMORANDUM

State of Alaska

To: The Honorable Walter J. Hickel
Governor

December 16, 1991

From: Rural Development Sub-cabinet

Phone: 465-4700

Re: Support for legislation exempting natural resources in place
from local property taxation

The rural development sub-cabinet has been following with concern the issue of whether or not natural resources in place should be subject to local property taxation. A study of the issue was conducted by the Department of Community and Regional Affairs, and a report will be submitted to the Legislature before January 13.

There is now consensus around the state that natural resources in place should be totally exempt from local property taxation. Legislation to effect a total exemption (with the exception of oil and gas which are treated separately under existing statutes) will be proposed in the forthcoming legislative session. Natural resource industries and associations, Native corporations, local governments, and the Alaska Municipal League have all endorsed a total exemption.

The rural development sub-cabinet supports a total exemption of natural resources in place from local property taxation, and urges the Governor to actively support legislation that will so amend Title 29 of The Alaska Statutes.

Edgar Blatchford

Commissioner Edgar Blatchford, Chair
Community & Regional Affairs

Glenn A. Olds

Commissioner Glenn A. Olds
Commerce & Economic Development

Carl L. Rosier

Commissioner Carl L. Rosier
Fish and Game

Harold C. Heinze

Commissioner Harold Heinze
Natural Resources

John A. Sandor

Commissioner John A. Sandor
Environmental Conservation

*Letter to Governor from
Rural Dev. Sub-Cabinet*

Exemption from municipal property taxation for natural resources in place.

My name is Steven C. Borell and I am the Executive Director of the Alaska Miners Association.

Thank you Mr. Chairman and committee members for the opportunity to comment on this important issue. Thank you also for scheduling this bill early in the session.

The AMA supports this legislation and the need for passing an exemption for the taxation of natural resources in place during this session of the Legislature. We are concerned that if taxation of natural resources in place is begun, the affect will be to discourage if not totally close down exploration in those areas where this form of taxation occurs.

We also wish to commend the Alaska Municipal League for taking the lead in support of an exemption from taxation for resources in place. We were very pleased to learn that the AML passed a resolution favoring exemption of taxation of natural resources in place and that the resolution passed on a unanimous vote. The AML recognized that in place taxation would have a very serious negative affect on local economies in several different ways.

Rather than addressing in detail all of the arguments why in place taxation is not a good policy, I shall list and summarize the major problems with this form of taxation.

The first and possibly most compelling reason for not taxing minerals in place is that it is extremely difficult to place a value on minerals before they are actually extracted from the ground. Major mining companies employing scores of exploration, financial, environmental, engineering, and management people have a very difficult time defining the value of a deposit.

The second major problem with the taxation of minerals in place is that it discourages exploration. Mining companies will not even look for minerals if they will be taxed for the many years that are required to determine if they have an economic deposit. For Greens Creek, the largest silver mine in North America, it took 17 years from the initial discovery until first production. For Red Dog, possibly the largest zinc deposit in the world, it took 21 years from initial discovery until first production. If an in place tax had been charged on these minerals before they were mined, there is a high likelihood that no mining would ever have taken place.

A third fact to consider is that taxation of minerals in place is an additional burden on local communities that are already struggling to encourage creation of new jobs and expand their real property tax base. For much of Alaska the only opportunity

*Alaska Miners Assoc.
letter of support*

for economic development and creation of new jobs is through development of mineral resources. If in place minerals are taxed, local communities will be hurt without even knowing it because the mining companies that have the expertise to find and develop the minerals will not even go out and explore for them.

A fourth problem involves the taxation of non-tangible natural resources that exist due to location or setting. For the city lot this non-tangible value is determined and under the doctrine of equal treatment, the value of non-tangible natural resources such as wilderness character, wilderness proximity, scenic values, proximity to rivers for rafting or floating, etc. would have to be taxed. Hunting and fishing lodges would have to be taxed for the fish and wildlife resources that are in their area.

A fifth problem involves how will the fish resources available to fishing sites be taxed? The fish are clearly a natural resource and the fish site has a measurable market value but it also has an opportunity value by virtue of the fish that pass the site.

A sixth problem is whether or not it would be cost effective to attempt taxation of in place resources. The above examples show some of the difficulties that will be encountered.

A seventh problem will arise when a company that has been taxed for several years on the in place natural resources decides that the project is not economic and asks for reimbursement of the taxes that had been paid. This could be a lodge developer that sees his potential market change or it could be a mining company that concludes that the metallurgy of the ore is too complex and costly for a mine to be profitable.

For all of the above reasons, a permanent exemption for taxation of natural resources in place is necessary during this session of the Legislature.

Thank you again and please feel free to contact me if you have any questions.

STATE OF ALASKA
LEGISLATIVE SESSION

BILL NO. SB 330

Revision Date: _____ Department Affected: Revenue
 Title: Exemption from Municipal Property Taxation for Natural Resources BRU: Revenue Operations
 Component: Oil and Gas Audit Division
 Sponsor: Senator Adams
 Requestor: Senate Resources Committee COMPONENT SERIAL NO.

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EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	\$0	0	0	0	0	0

CAPITAL						
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REVENUE FUND SOURCE:						
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FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER FUND SOURCE:						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: None

ANALYSIS: (Attach a separate page if necessary.)

Prepared By: Robert L. Doss, Director Phone: 277-5627
 Division: Oil and Gas Audit Division Date: January 21, 1992
 Approved by Commissioner: *David R. ...*
 Agency: Department of Revenue Date: January 21, 1992

STATE OF ALASKA

DEPT. OF COMMUNITY & REGIONAL AFFAIRS

OFFICE OF THE COMMISSIONER

WALTER J. HICKEL, GOVERNOR

150 THIRD STREET
JUNEAU, ALASKA 99801-1291
PHONE: (907) 465-4700

949 E. 36TH AVENUE, SUITE 400
ANCHORAGE, ALASKA 99500-4302
PHONE: (907) 563-1073

January 2, 1992

The Honorable Lloyd Jones
Alaska State Senator
State Capitol
Room 30 - Capitol Building
Juneau, AK 99801-1182

Dear Senator Jones:

With this letter I transmit to you our report on the **Taxation of Natural Resources in Place**. The study was mandated by HB 159 (CH 127 SLA 1990) and conducted by the Department of Community and Regional Affairs in conjunction with the Alaska Municipal League and the Department of Revenue.

The report concludes that there is a statewide consensus in support of a total exemption from local property taxation for natural resources in place — defined in the report as "any material in it's natural state before it has been harvested or extracted."

The study went through a long public process that involved technical and policy working groups, a working group from the Alaska Municipal League, a survey of the practices of other states and provinces, and public presentations at the Southeast Conference in Juneau, at the Alaska Forest Association Convention in Sitka, during the Alaska Federation of Natives Convention in Anchorage, at the Alaska Miners Association Convention in Anchorage, and at the Alaska Municipal League Convention in Fairbanks. Earlier drafts of the report were mailed to 120 interested parties across the state for comment.

Considerable written correspondence was received in support of a total exemption from local property taxation for natural resources in place. Because of the statewide consensus, and in an attempt to conserve resources, the correspondence was not summarized as an addendum to the report. It is available and will be transmitted to the relevant committees upon request.

If you have any questions about the report or the study process, please contact Sandra Wicks, Deputy Director and Legislative Liason, Municipal and Regional Assistance Division, Department of Community and Regional Affairs, 150 Third Street, Room 310, Juneau, Alaska 99801, or phone 465-4750.

Sincerely,

Edgar Blatchford
Commissioner

Enclosure

**Report to the Alaska Legislature
on
The Taxation of Natural Resources In Place**

January 1992

**by
The Department of Community
and Regional Affairs**

**Walter J. Hickel, Governor
State of Alaska**

**Edgar Blatchford, Commissioner
Department of Community and Regional Affairs**



**Report to the Alaska Legislature
on
The Taxation of Natural Resources In Place**

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Appendix: Property Taxation of Natural Resources
in the States and Provinces



**REPORT TO THE ALASKA LEGISLATURE
ON
THE TAXATION OF NATURAL RESOURCES IN PLACE**

I. Introduction

In 1990, the Alaska Legislature passed an act creating a temporary exemption from property taxation for natural resources in place. (HB 159, enacted as CH 127 SLA 1990, hereafter "the Act".) The temporary exemption in the Act expires July 1, 1992.

In the Act, the Legislature required the Department of Community and Regional Affairs (DCRA) to conduct a study of the potential effects of various natural resource taxation options. This report represents DCRA's effort to fulfill this directive. The purpose of this report is to raise the relevant policy issues and highlight some of the major ramifications for local governments, the state, and resource industries of various taxation strategies. Volumes could be written on the pros and cons of the various taxation strategies to be considered and how they might impact the various resource industries and the various municipalities. However, this study does not purport to be an in-depth discussion of all the possible implications of the taxation strategies examined. If the Legislature determines there is sufficient interest in, or need to further examine the questions raised, it may choose to allocate additional resources to studying those questions. However, at this time there appears to be a statewide consensus in support of totally exempting natural resources in place from local taxation.

Alaska statutes pertaining to property taxation by local governments, while presently exempting certain kinds of property from taxation, do not (except for the temporary exemption in the Act) exempt natural resources in place from taxation. Consequently, natural resources in place are required to be taxable property. As long as the resources remain in place, they could only be taxed through the method of property taxation. Thus, the basic issue of this study was:

Should natural resources in place be taxable by municipalities? Or, in other words, should natural resources be subject to municipal property taxation?

The Legislature also asked DCRA to examine natural resource taxation options other than total taxability of natural resources in place or total exemption of natural resources in place from municipal property taxation. Consequently, the study also examined the following questions:

1. **Should natural resources in place be partially exempt from local taxation?**
2. **Should natural resources in place be totally or partially exempt from local taxation at the option of the local government?**
3. **What other forms of taxation, if any, should municipalities be able to apply to natural resources?**

To answer these questions the study examined several major policy concerns:

- ✓ Fairness among taxpayers
- ✓ Fairness among municipalities
- ✓ Stimulation of economic development
- ✓ Cost-effectiveness of taxation methods
- ✓ Municipal revenue needs/sources

In particular, the study looked at the consequences of various options for taxation of natural resources on municipalities, the resource industries, and the state government (in particular the State Assessor's Office). A survey of other states and provinces was also conducted. An addendum at the end of this report discusses the results of the questionnaire on the subject of natural resources taxation in the other states and provinces.

The Act mandated that DCRA conduct the study in concert with the Department of Revenue (DOR) and the Alaska Municipal League (AML), and with the participation of representatives of municipalities and unincorporated communities in boroughs and in the Unorganized Borough. After initial meetings with technical and more broadly based working groups in 1990 and early 1991, and teleconferences specifically with the AML working group in August and September 1991, DCRA issued a Preliminary Report on The Study of Taxation of Natural Resources in Place on September 13, 1991. The report was sent to all members of the technical and other working groups for comment. Presentations on the approach to the study and its tentative results were made at the Southeast Conference in Juneau, the Alaska Forest Association convention in Sitka, during the Alaska Federation of Natives convention in Anchorage, at the Alaska Miners Association convention in Anchorage, and at the Alaska Municipal League conference in Fairbanks during the fall of 1991. Before the AML conference, a Draft Report on The Taxation of Natural Resources in Place, dated November 1, 1991, was circulated to all of the members of the various working groups and the people who expressed interest in being on the mailing list as a result of the live presentations on the study. The result of the study process is a consensus that natural resources in place should be totally exempted from local property taxation. Without legislative action during the 1992 legislative session, however, the temporary exemption from municipal taxation for natural resources in place will expire July 1, 1992, and natural resources in place will once again be taxable.

To encourage reasoned discussion of the focal issues of the study, the draft report and the live presentations discussed the existing framework of municipal taxation in Alaska, the potential effect of the assessed value of resources in place (if deemed taxable) on the state education foundation aid and state revenue sharing monies to be received by local governments, and the local revenue generation required in order to qualify for those monies under the existing formulas. Both of these formula-based programs are tied to the full and true value of real and personal property within municipalities. Certain aspects of these programs and their terminology had to be understood to lay the groundwork for discussion of the central issue of taxation of resources in place.

The balance of this report follows the format and provides the information circulated to the public as part of the study. It explains the framework for municipal taxation in Alaska, the state foundation aid program for schools, and the state revenue sharing program before returning to the specific issue of the taxation of natural resources in place. The report also examines assessing issues and the policy concerns listed above in relation to the taxation options DCRA was directed to study. This final report will also be circulated to the public before the 1992 legislative session begins.

II. The Legal Framework for Municipal Taxation in Alaska

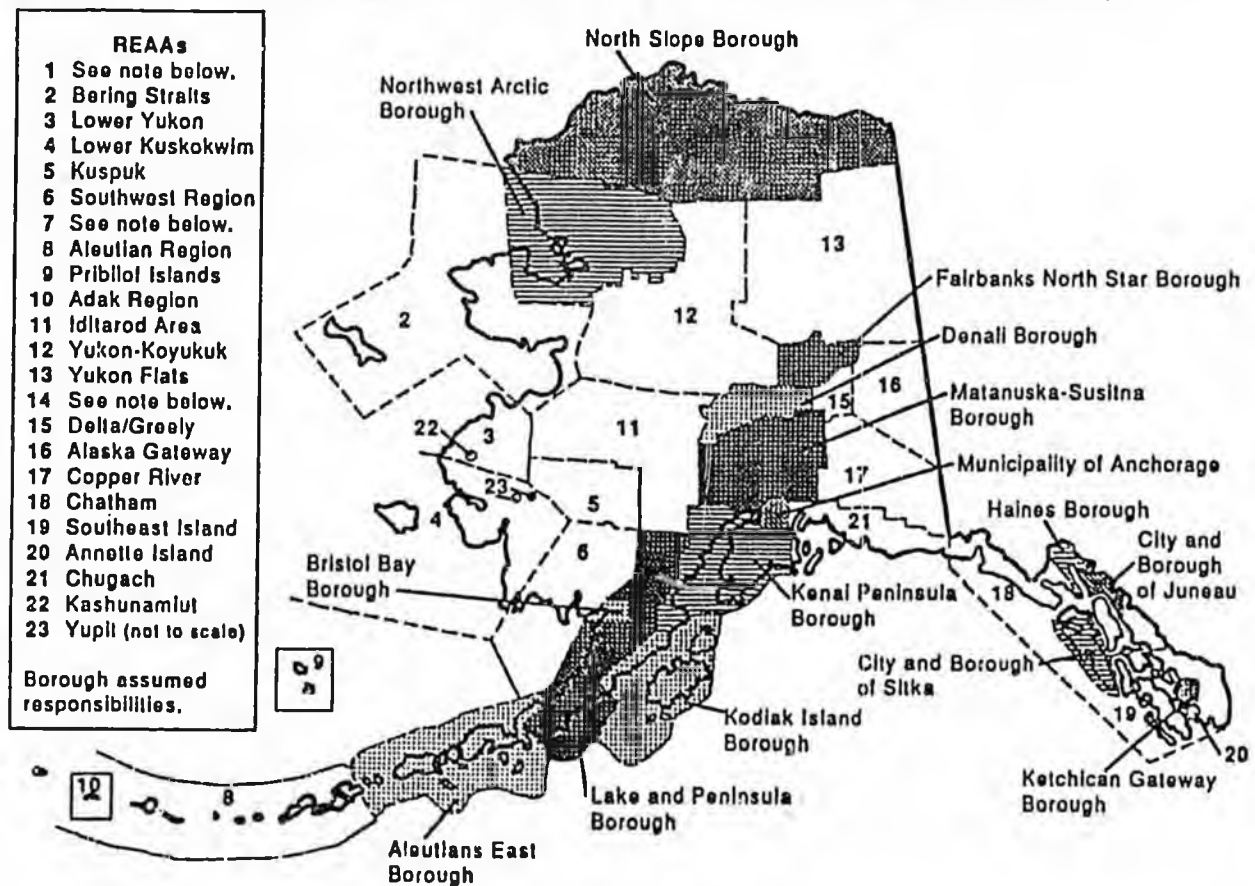
Articles IX and X of the Alaska Constitution and Title 29 of the Alaska Statutes establish the framework for municipal taxation in Alaska. Home rule municipalities are granted broad governmental powers by the Alaska Constitution, while general law municipalities are, among other specified powers, granted the right to levy a tax or special assessment, and impose a lien for its enforcement (AS 29.35.010). Home rule and general law municipalities are subject to limita-

tions on their taxing powers found in Chapter 29.45 of the Alaska Statutes. Within Chapter 29.45 there are provisions on property taxes, sales taxes and use taxes. Section 29.45.010 authorizes cities, boroughs, and unified municipalities to levy a property tax. If a tax is levied on real or personal property, it must be assessed, levied, and collected as provided in Chapter 29.45. Nowhere in Chapter 29.45, however, is there a statement of what is taxable. Instead, the assumption is that all real and personal property is taxable unless it is exempted from property taxation. That assumption is supported by Section 1 of Article X of the Alaska Constitution, which provides that "a liberal construction shall be given to the powers of local government." The following two sections describe the geographic distribution of municipal taxing powers and discuss the concept of taxability. Part IX of this report discusses various property taxation options and other taxation options that the Legislature directed DCRA to study.

A. The geographic distribution of municipal taxing powers

Natural resources in place, in order to be subject to municipal property taxation, have to be located within a city, borough or a unified municipality. The map below indicates the boroughs, the unified municipalities, and the unorganized borough. Not shown on the map are many cities located within the Unorganized Borough. Most cities do not contain many natural resource properties because of the limited area included within their boundaries. Nevertheless, any natural resource properties located within their boundaries could be affected by legislation (or lack thereof) pertaining to the taxation of resources in place. The issue of taxation of resources in place is also of significance to residents and property owners in the Unorganized Borough because, upon borough formation, whatever is taxable under state law will be taxable by the new borough, whether or not the new borough elects to levy a property tax.

Borough and Rural Education Attendance Areas (REAA)



B. What is taxable?

The focal issue of this study is: should natural resources in place be taxable by municipalities? As explained above, under the statutory framework for municipal taxation in Alaska, all real and personal property is taxable unless it is exempted from property taxation. Required exemptions from municipal property taxation are specified in AS 29.45.030. Examples from the laundry list of property exempted from property taxation by AS 29.45.030 are household furniture and personal effects of members of a household, and property used exclusively for nonprofit religious, charitable, cemetery, hospital, or educational purposes. Property owned by ANCSA Native corporations is also exempt from municipal taxation until development occurs or it is leased to a third party. In addition to these exemptions from property taxation, AS 43.56 provides for certain exemptions of oil and gas production and pipeline property, including oil and gas in place. All of the exemptions discussed in this paragraph are mandatory exemptions. In other words, the property mentioned in the above-referenced statutes is simply not taxable at all.

Section 29.45.050 of the Alaska Statutes provides for optional exemptions and exclusions from local property taxation. The exemptions and exclusions are at the option of the local government which levies the property tax. Two examples of optional exemptions are the exemption from property taxation of personal property and the exemption of up to \$10,000 of value in a residence. The exemptions in AS 29.45.050 require action by the local government and they sometimes also require approval of the voters.

Since there are existing mandatory exemptions and optional exemptions, and since there is a mandatory exemption from property taxation for oil and gas in place in particular, it is reasonable to consider some form of exemption for some other, or all natural resources in place. If a mandatory or optional exemption is to be considered, however, we must have a working definition of the term "natural resource in place."

III. What is a "Natural Resource in Place"?

The term "natural resources in place" does not correspond to any commonly used assessment terminology and appears to be very broad. The term "natural resources in place" is used several times in the Act, but only Section 2 gives an indication of what the term means. Section 2 of the Act reads as follows:

Sec.2. Temporary Tax Exemption. Natural resources in place, including proven or unproven mineral and other deposits of valuable materials and timber stumpage, are exempt from property taxation by a municipality. (emphasis added)

By the language of Section 2, the term "natural resources in place" covers 1) unproven mineral and other deposits of valuable materials, 2) proven mineral and other deposits of valuable materials, 3) timber stumpage, 4) and a category best described as "other." The "other" category arises from the wording of the Act that says natural resources in place "including" the named categories that are listed. Apparently, something in addition to the named categories in the Act was contemplated by the Legislature. Another ambiguous term in the Act is the phrase "other deposits of valuable materials." This term probably includes sand and gravel, but does it include glacial ice, for instance?

For the purposes of the study, the term "natural resources in place" was defined as:

Any material in its native state before it has been severed or extracted.

With that working definition of "natural resources in place," we looked at the effect of having natural resources in place taxable, as they were before the temporary exemption went into place in 1990. An important effect of taxability of a natural resource in place is that its market value must be included in the "full value determination" for the municipality in which the resource is located. The value of all taxable real and personal property in a municipality is included in its full value determination. The obvious question, then, is: What is a full value determination?

IV. What is a "Full Value Determination" ?

In brief, a full value determination is the sum total for a municipality of the full and true value established for each piece of taxable real and personal property within a municipality. AS 29.45.110 (a) specifies that the full and true value (FTV) is "the estimated price that the property would bring in an open market and under the then prevailing market conditions in a sale between a willing seller and a willing buyer both conversant with the property and with prevailing general price levels." AS 29.45.110 (a) also requires the assessor to assess property at its full and true value as of January 1 of the assessment year.

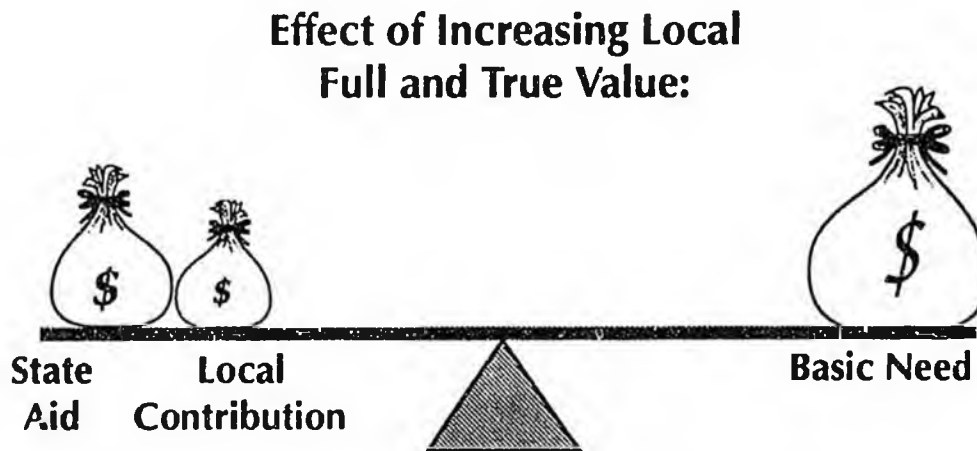
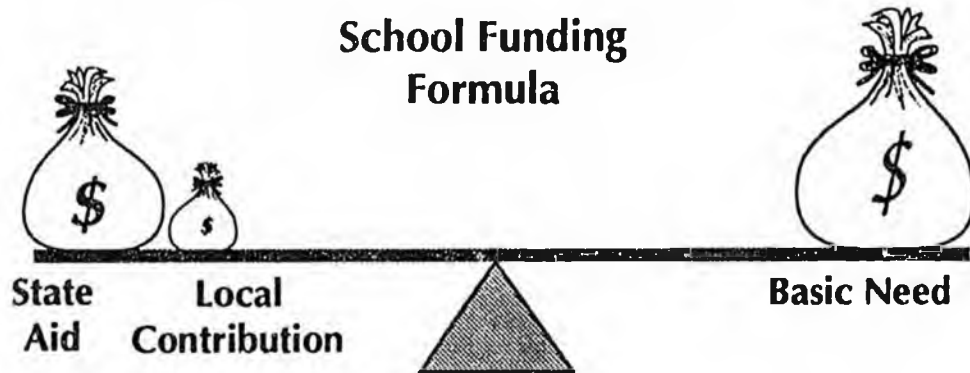
The education title of the Alaska Statutes, specifically AS 14.17.140, requires the Department of Community and Regional Affairs, in consultation with the assessor for each school district, to establish the full value of the taxable real and personal property in each city and borough school district. Not all cities and boroughs have property taxes, however, and, consequently, not all cities and boroughs have assessors. For those that do not, the State Assessor, located in the Department of Community and Regional Affairs, must estimate the full value of the taxable real and personal property without the consultation of a local assessor.

The State Assessor then compiles the full value determination for each municipality annually and notifies each municipality. As discussed below, the full value determination plays a significant role in the calculation of both the state foundation aid for education and the state revenue sharing programs. It is critical to municipalities, as well as property owners, whether natural resources in place are taxable (i.e., whether the value of natural resources in place will be added to the full and true value of the property in or on which these resources are located). The full and true value of all taxable property, whether the property is actually taxed or not, must be included in the full value determination for the municipality.

V. How does the Full Value Determination Affect State Foundation Aid?

Chapter 14.17 of the Alaska Statutes establishes the Public School Foundation Program. Under that program, a school is determined to have a "basic need" determined according to a formula spelled out in AS 14.17.021 (b). The local government is required to make a "local contribution" toward this basic need. The local contribution is defined in AS 14.17.025 as at least the equivalent of a 4 mill tax levy on the full and true value (FTV) of the taxable real and personal property in the district, unless a 4 mill tax levy on the FTV exceeds 35% of the district's basic need. A municipality will not receive its school foundation aid payment unless it makes its local contribution. AS 14.17.025 (e).

In other words, the higher the municipality's FTV, the greater the amount of money the municipality must raise to satisfy the local contribution requirement, up to the point where a 4 mill levy on the FTV exceeds 35% of the district's basic need. Historically, only in the North Slope Borough and the City of Valdez has the 4 mill equivalent exceeded 35% of basic need. This year, for the first time, a 4 mill levy on the FTV in the City of Unalaska will also exceed 35% of basic need. The following illustrations depict the relationship between state aid, local contribution and basic need, and demonstrate the effect on this relationship of increasing the local full and true value.



To further illustrate the point, assume that the FTV of the municipality is presently \$1 million. A 4 mill levy on \$1 million is \$4,000. If the FTV for the municipality increases to \$2 million, then the equivalent of a 4 mill levy will require the municipality to raise \$8,000. This may or may not be a problem for the municipality depending on the basis for the increase in FTV.

In summary, under the public school foundation program, assuming that basic need remains constant, as the FTV increases, the amount of the local contribution increases, and the amount of state foundation aid decreases. The question for the municipality is then: how will it raise the additional money to meet its local contribution requirement if the municipality's FTV increases?

VI. How does the Full Value Determination Affect State Revenue Sharing?

Sections 29.60.010–29.60.080 establish a program for municipal tax resource equalization. This tax equalization program is part of what is commonly referred to as the state revenue sharing program. Its purpose is to even out differences in taxable wealth among the municipalities in the state by paying relatively more shared revenues to those municipalities that have little taxable property.

The formula for determining a municipality's tax equalization entitlement is fairly complex. It is based on the municipality's population, actual generation of revenue, and the local tax base. The formula requires the equivalent of a local contribution. In this case, it is called "locally generated revenue."

The formula multiplies the population by the product of the locally generated revenue (LGR,) divided by one-tenth of one percent of the full and true value of the assessed property in the municipality. The formula for the product to be multiplied by the population is as follows:

$$\left(\frac{\text{LGR}}{0.1\% \text{ of FTV}} \right)$$

If we plug in some numbers, the formula looks like this:

$$\frac{100}{0.1\% \text{ of } 1,000} = 100$$

Obviously, the product will decrease if the FTV is increased unless the LGR is also increased. For example:

If local revenues are unchanged:

$$\frac{100}{0.1\% \text{ of } 2,000} = 50$$

If local revenues are increased to the same degree as the FTV:

$$\frac{200}{0.1\% \text{ of } 2,000} = 100$$

If local revenues are increased to a greater degree than the FTV:

$$\frac{400}{0.1\% \text{ of } 2,000} = 200$$

With this background in the two major funding formulas by which municipalities obtain state shared revenues, we can return to the focal issue of this study:

Should "in place" natural resources be taxable by municipalities?

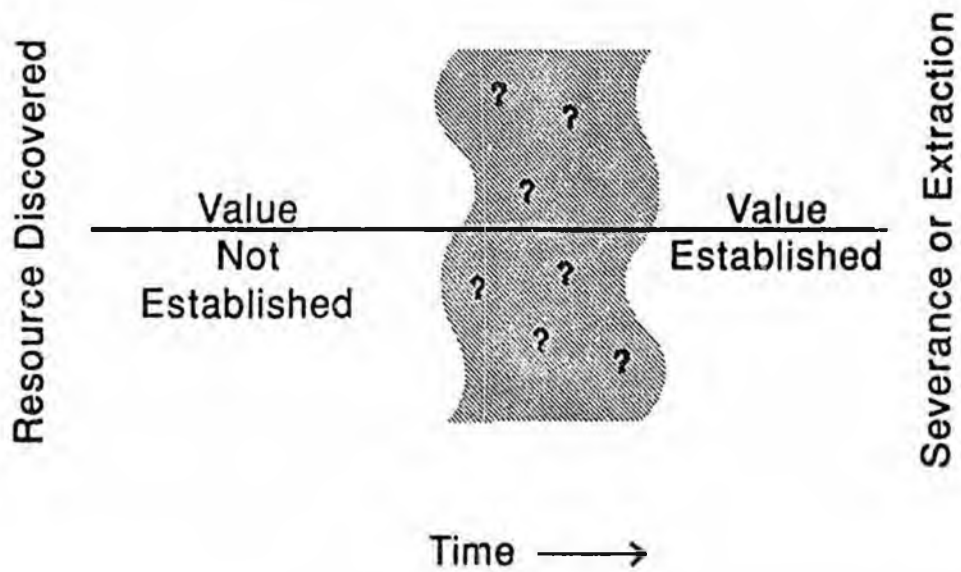
If natural resources in place — meaning resources that are not severed or extracted — are taxable, then the value of those resources in place must be added to the full and true value of the property in or on which they are located. As a consequence, the full value determination for the municipality will increase. The value of natural resources in place, however, can only be added to the assessment rolls at the point when an assessor using standard assessing practices could defensibly establish that value.

VII. The Problem of Assessing Natural Resources in Place.

Under the present temporary exemption from local property taxation, or if a permanent exemption from local property taxation is enacted, there is no issue of assessing natural resources in place. It is only an issue if the present temporary exemption expires and we return to the pre-existing status, which was that all taxable real and personal property must be assessed and included in the full value determination for the municipality in which the property is located.

When we speak of assessing natural resources in place, however, it should be clearly understood that the value of every resource in place would not be added to the assessment rolls on January 1, 1993. Assessors only put property on an assessment roll when a value for that property can be established according to commonly accepted standards and practices.

The figure below illustrates this point. The passage of time is indicated by the arrow at the bottom of the illustration. On the left of the illustration is the indication that a resource has been discovered. At the time of discovery so little is probably known about its dimensions, marketability and costs of production, that no value can yet be placed on the resource by the assessor. On the right hand side of the illustration is the indication severance or extraction. At the point of severance or extraction, we are no longer talking about assessment of a natural resource in place because the resource is no longer in place.



Logically, at some time before severance or extraction, it was possible to put a value on the resource in place according to standard assessing practices. The point at which a defensible value can be determined is the point at which the value should go on the assessment roll. Actually, the property may have already been on the assessment roll but with a minimal value based on use of the surface only. What we are really talking about is the point at which the in place resource value will be added to the assessed value of the property.

Assessors determine value by one of three methods: direct sales comparison, the cost approach, and the income (or income capitalization) approach. The cost approach is normally not applicable to valuing raw land. The direct sales comparison approach may be applicable to the valuation of natural resource properties in the rare instances where comparable sales of mineral properties can be found or where comparable timber stumpage values can be established. The third approach, the income approach to value, is the only realistic approach by which resources in place could routinely be valued, and it has certain inherent problems when one is dealing with income that has not yet been generated. The income approach to value involves developing an estimated net income (gross income less operating expenses) which is then capitalized using an appropriate capitalization (discount) rate. The following example illustrates the problem involved when an ore body, for instance, has not yet been developed.

In attempting to value an undeveloped ore body, it is first necessary to know, or estimate, the type and grade of ore, its volume, and its configuration. If the ore body has been discovered, but has not been extensively drilled, it would most likely be impossible to know these things. If the ore body has been adequately drilled, the information from the drilling may or may not be made available to the appraiser. (There is no requirement in Alaska for such information to be made available to state or local governments.) If the information were made available, the geologist/appraiser would still be facing the problems of estimating a potential income stream from development of the ore body, while considering fluctuations in the world market for that aggregate of ores. In addition, the appraiser would have to estimate the cost of extraction, including road construction, the actual extraction process, cost of drilling, separation of the metal from the host rock, shipping, and so forth. This exercise would be extremely subjective and speculative in nature.

A great deal of feedback has been received by the DCRA staff conducting this study about the difficulty and the cost of attempting to value natural resources in place so that their value can be added to the surface value of property for property tax purposes. Indeed, cost-effectiveness of having resources in place taxable is one of the important policy issues to be considered by the Legislature in determining the action to take with regard to the taxability of natural resources in place. The issue is: will it cost more than it is worth to permit the taxation of natural resources in place by local governments? This question is examined more fully in the discussion of the policy issues in Section IX. If the Legislature decides that natural resources in place should be taxable, another question that must be addressed is who should perform the assessment? That question is discussed in Section XIII, immediately following. There is general agreement that many assessments of natural resources in place would have to be performed by assessors with special expertise different than the expertise of most assessors.

VIII. Who Should Assess Natural Resources in Place?

If natural resources in place are taxable by local governments, their value must be included in the full value determination for the municipality in which they are located. To do that, natural resources in place must be assessed by someone. Before looking into the question of who should assess natural resources in place, it is useful to look at the present process of property tax assessment by the municipalities.

Municipalities that levy a property tax either have a staff assessor or hire a contract assessor to perform the assessments for the municipality. The State Assessor then reviews the municipal assessments and makes any necessary adjustments, including addition of the value of property optionally exempted by the municipality from property taxation. The value of all taxable real and personal property, as adjusted by the State Assessor, is included in the full value determination for that municipality.

Not all municipalities empowered to levy a property tax actually do so. Those that do not levy a property tax do not assess the property within their jurisdiction. Nevertheless, by statute, the State Assessor must establish the full and true value of that municipality for purposes of the state foundation aid program and the tax equalization (revenue sharing) program. Therefore, the state has to be prepared to assess all taxable real and personal property within the municipalities in the state. If natural resources in place are taxable, the State Assessor will have to be prepared to assess them whether or not the municipality does so.

Before the temporary exemption went into effect in 1990, the municipalities did not routinely include in their assessments the value of natural resources in place and the State Assessor did not routinely add their value to the full value determinations of the municipalities. Now, however, if the temporary exemption is allowed to expire and the pre-existing law is again in effect, the full and true value of each municipality will have to include the value of natural resources in place within its boundaries because awareness of this issue has now been heightened statewide. Someone will have to establish that in place natural resource value. Under our present statutory structure, either the value will be established initially by the municipal assessor and reviewed by the State Assessor or, if the municipality does not levy a property tax, and therefore does not establish an assessment roll, the State Assessor will have to establish an estimated assessment in order to arrive at the full value determination for the municipality.

Municipal assessors are not generally trained to assess the value of mineral ore, coal, gravel, rock or timber in place. The two appraisers presently working in the State Assessor's office do not possess the necessary qualifications or experience either.

Typically, an economic geologist is hired by a mining company to determine the value of an ore body. Specially qualified forest appraisers are hired by timber companies to value timber resources. People with comparable skills will be necessary at the local and/or state level to assess natural resources in place, whether those people be hired as staff or hired under contract to provide assessing services.

The difficulty of assessing an ore body is illustrated by the Red Dog mine example where the State and the Northwest Arctic Borough hired a geologist and appraisal consultant at the rate of \$150 per hour to use the income approach and estimate the value of the entire mining operation, including the ore body under development. Under a separate agreement, the Borough contracted with the same geologist/appraiser for an appraisal of the mine utilizing the cost approach. The cost

approach appraisal was conducted in order to estimate the value of the mine improvements without the value of the ore body. By comparing the two appraisals, the consultant concluded that the value of the ore body was approximately \$30,000,000. The same consultant stated, however, that before certain metallurgical problems with smelting the ore were encountered, the value of the ore body had been \$100,000,000. He expected that within two to three years, when the metallurgical problem was solved, the value of the ore body would then again be \$100,000,000, absent some dramatic change in the world price for the mineral. This example illustrates the dramatic increases and decreases in the value of an ore body which often occur because of variable factors beyond the control of the industry.

Municipal assessors are not typically knowledgeable about the geology of mineral ores, smelting and metallurgy, world mineral prices and the other factors that go into appraising a mining property. In fact, the economic geologist who performed the Red Dog mine appraisal has stated it is easier to train a geologist to become a mining appraiser than to train an appraiser to become a mining appraiser. Likewise, appraisers of timber resources must have the training to estimate types and grades of timber, calculate the costs of road construction, harvesting, transportation, storage and loading, among other things, as well as world timber prices. Again, it is not expected that a municipal assessor will have had this training and experience.

At least two other states in which natural resources in place are taxable have gone to a centralized assessment of natural resource properties by the state. (More details on the practices of other states are found in the addendum.) If natural resources in place are to be taxable, the issue of who is going to perform the assessments of those properties will need to be resolved. If the assessments are to be performed by the State Assessor's office, additional staff with the required expertise will have to be hired or, in the alternative, funding for contract assessors with the necessary training will have to be allocated.

IX. Taxation Options and Policy Considerations

The act mandating the study asked DCRA to examine five taxation options:

1. Total exemption from municipal property taxation.
2. Partial exemption from municipal property taxation.
3. No exemption from municipal property taxation.
4. Total or partial exemption from municipal property taxation at the option of each municipality.
5. Taxation other than property taxation.

A discussion of these options pertaining to natural resource taxation must include a discussion of at least the following policy considerations:

- ✓ Fairness among taxpayers
- ✓ Fairness among municipalities
- ✓ Stimulation of economic development
- ✓ Cost-effectiveness of taxation methods
- ✓ Municipal revenue needs/sources

These policy considerations are examined, followed by a discussion of the five taxation options in the context of the present legal framework for municipal taxation and the policy considerations.

A. Policy Considerations

Fairness Among Property Owners

This policy consideration raises the issue of fairness among owners of various types of property. Upon whom should the tax burden to support government services within a municipality fall? Upon only the owners of personal property? Upon only the owners of real property? Upon only the owners of zoned real property? Should the owners of real property that is zoned have their assessment reflect the value of the particular zoning classification? Should owners of natural resource property have their assessment reflect the value of the resource in place? How can you be fair to all potential taxpayers? If one group of potential taxpayers is eliminated, does the burden fall unfairly on the remaining groups of taxpayers?

Fairness Among Municipalities

Fairness among municipalities is an issue because not all municipalities in Alaska are equally endowed with a tax base from which to raise revenues. Should those municipalities with a potential tax base of natural resources in place be permitted to not include the value of those natural resources in their full value determinations? If they are not required to include the value of those natural resources in their full value determinations, those municipalities will not have to increase their local contribution to schools, even though they actually have a tax base from which they could generate local revenue. As a consequence, municipalities that could raise more local revenue will still get their same share of the school foundation aid from the state. Municipalities that have no possibility of raising more revenue for their schools would be disadvantaged under this scenario in which municipalities with resources in place are not required to make a local contribution commensurate with their actual wealth.

Stimulation of Economic Development

With this policy consideration, the issue is whether or not making natural resources in place taxable would be a disincentive for economic development. It is necessary to keep in mind that taxability of natural resources in place does not necessarily mean that the taxing jurisdiction will choose to levy a property tax. If a property tax is levied, however, it must be levied equally against all taxable property. Consequently, one must contemplate whether levying a property tax on the assessed value of resources in place will act as a deterrent to economic development. What specific impacts might such a tax have on economic development? Will it discourage exploration for minerals? Will it encourage the exploitation of only the highest grades of ore? Will it encourage the rapid cutting of forests in order to eliminate the source of a higher property tax? DCRA was told by the resource industries and the Department of Commerce and Economic Development that the impact of making natural resources in place taxable will be uniformly detrimental to economic development. No contrary evidence was provided and DCRA does not have the means to hire economists to make an independent assessment of these assertions.

Cost-Effectiveness

Cost-effectiveness is an important policy consideration because assessment of natural resources in place is expected to be much more complicated and costly than the municipal property assessments typically performed now. All sources indicate that ore bodies are extremely difficult to evaluate, even for the professionals hired by mining companies to perform evaluations on the

basis of which millions of dollars may or may not be invested. Assessment of timber stumpage is also a highly specialized skill not normally possessed by municipal assessors or state assessors whose job it is to review standard municipal assessments. Assessments of both of these categories of natural resources in place would have to be accomplished either by extensive particularized investigations of specific resource properties, or through elaborate computer modeling for which both the data and the programs are not now available either to municipal assessors or to the state assessor.

If such assessments of natural resources in place are performed by the municipalities, they might sometimes have to be confirmed by the State Assessor's Office. In that case, presumably both the municipalities and the State Assessor's Office will face additional costs for contracted expert help or additional staff possessing the necessary expertise. If the municipality does not intend to levy a property tax and, therefore, does not assess property, the State Assessor's Office would still have to assess the natural resources in place in order to add their value to the full value determination for the municipality.

Several agencies and the Alaska Miners Association have commented that because of the difficulty of assessing ore bodies, serious disputes over assessed values of minerals in place can be expected, with the associated probability of litigation. At least two states have attempted to deal with the problem of assessing resources in place by centralizing the function in a state agency. (See the addendum on the results of the survey of states and provinces.) It is a policy question for both local governments and the state as to whether it would be cost-effective to have to assess natural resources in place in order to have the possibility of taxing them.

Municipal Revenue Needs and Sources

Municipalities are being required by the federal and state governments to assume more responsibilities. Most often these additional responsibilities are not accompanied by sufficient funds to cover the cost of the new activity. At the same time, municipalities are seeing the state cut the amount of money allocated to state revenue sharing and municipal assistance. While municipalities are facing these problems, they may also face the impacts of natural resource development in their area. Natural resource development may provide long-term economic benefits, but it may also require extension of roads, water lines, sewer lines, and power lines as well as the development of additional housing, schools and commercial infrastructure. In this situation, municipalities might be hesitant to give up a taxing power that would potentially provide a present revenue stream for the payment of present infrastructure costs.

Several state agencies and natural resource owners have stated that if there must be taxation of natural resource development, the taxation should not begin before severance or extraction of the resource takes place. While this may be preferable for the natural resource industries, it could leave the municipalities without the revenue needed to develop the infrastructure necessary to deal with impacts and provide support for economic development that is needed before the natural resource industry is in production. In the worst case, a community might experience impacts for many years during pre-production activities and the enterprise might never go into production with the consequence that there is never any revenue derived from a severance tax.

With these five policy considerations in mind, the five taxation options the Legislature asked to have studied were examined. A synopsis of the thinking developed on each option during the study is provided below.

B. Taxation Options

Option One: Total Exemption from Municipal Property Taxation

Total exemption from municipal property taxation means that natural resources in place would not be taxable by local governments. This is the option for which there appears to be a statewide consensus.

Those who commented in favor of this option include the Department of Natural Resources, the Department of Commerce and Economic Development, the Department of Revenue, and the State Assessor, among state agencies. Support for this option was also voiced by the Alaska Miners Association, Sealaska Corporation, Chugach Forest Products, Afognak Native Corporation, Konkor Forest Products Corporation and NANA Corporation, among other individuals and organizations.

At the Alaska Municipal League conference, the AML unanimously adopted a resolution in support of a total exemption. In the view of the local governments, the value to be derived from having natural resources in place taxable is not worth the cost and difficulties arising from the need to assess natural resources in place, municipalities would have to increase their local contribution and locally generated revenue to obtain state monies, and, finally, the municipalities do not want to risk impeding economic development that might benefit their communities.

One potential benefit to local governments from a total exemption is that municipalities will not be required to assess natural resources in place, and they will not face possibly dramatic changes in their full value determinations that might result if natural resources in place are assessed. (For example, based on Robert Paschall's studies, the Northwest Arctic Borough could face an increase in its full value determination from \$30,000,000 to \$100,000,000 as soon as metallurgical problems at the Red Dog Mine are resolved.) Dramatic changes in full value determinations for some municipalities arising from the taxability of natural resources in place would require that those municipalities increase the absolute amount of their local contribution to the basic need for their schools. (Remember the required local contribution under the school foundation aid formula is the equivalent of a four mill levy or 35% of basic need.)

On the one hand, a property tax provides a revenue stream as soon as a value can be placed on property. It avoids the situation described above where a community may have had to deal with resource development impacts for years and then have production never start so that reliance on a severance tax would provide no revenue. (See, however, the discussion below under Option Five.)

On the other hand, owners of natural resource properties point out that a property tax is the worst possible tax for stimulating economic development. They say a property tax on resources in place will discourage exploration and encourage cutting trees prematurely. It will also encourage closing mines when only the highest grade ore has been extracted.

Option Two: Partial Exemption from Municipal Property Taxation

The Legislature asked that a partial exemption from municipal property taxation be one of the options considered in this study. The Legislature did not indicate, however, what it meant by partial.

A partial exemption could mean that some natural resources are exempted from property taxation while others are not. Alternatively, a partial exemption could mean that a portion of the assessed value of the natural resource in place would be exempted from property taxation. The former interpretation raises serious questions of taxpayer equity. The latter interpretation triggers serious concerns about the cost-effectiveness of a partial exemption.

An exemption of some natural resources in place but not others would obviously have a differential impact on potential taxpayers. Owners of timber land might question whether it was fair to exempt mineral land from taxability but not their timber land, for example. There would also be a differential impact on municipalities since natural resources are not all distributed evenly across the state. Municipalities whose resources were exempted from taxability would no longer be able to raise revenue by levying a property tax on the value of those resources in place. On the other hand, municipalities whose natural resources were not exempted would have to add the assessed value of those natural resources in place to their full and true value. The consequent increase in the full value determination means those municipalities would have to raise more revenue in order to meet their local contribution requirement for state foundation aid. Those municipalities might not have a large tax base from which to raise revenue other than by a property tax, and yet they might feel that levying a property tax would be detrimental to economic development and also to their residents who might live a largely subsistence life style.

The cost-effectiveness issue discussed above is even more persuasive against the other interpretation of "partial exemption," by which a portion of the assessed value of all natural resources in place would be not taxable. The same difficult and costly assessing work would be required to correctly assess the property, but in return only a certain portion of the assessed value would be put on the tax rolls. Under this scenario, the revenue to be derived from a property tax would be lower, while the amount and cost of the assessment work would remain the same.

Option Three: No Exemption from Municipal Property Taxation

The option of no exemption from municipal property taxation will be the conscious or unconscious result if the Legislature takes no action on the issue of the taxation of natural resources in place during the coming legislative session. As mentioned above, the temporary exemption in the Act expires July 1, 1992. On that date, if no legislation has changed the law on taxability, natural resources in place will once again be taxable. The difference is that now people are very conscious of this issue and there is a statewide consensus that natural resources in place should not be taxable.

If there is no exemption from taxation for natural resources in place after July 1, 1992, it is unlikely that resources in place that have an assessable value will be kept off the assessment rolls. Taxpayers who feel they are unfairly carrying the tax burden in their municipality might sue to put assessable resource properties on the tax rolls. If the municipality does not put assessable resource properties on the assessment rolls, the State Assessor will still be obligated to include the full and true value of those properties in the full value determination for the particular municipality. That will have differential impacts on the municipalities' shares of education and state revenue sharing funds depending on whether the municipalities have or do not have assessable natural resources in place. Taxability of natural resources in place will also impact the staffing and funding necessary for municipal assessing offices and the State Assessor's Office.

The resource industries have commented that if natural resources in place are taxable, that will have a detrimental impact on economic development within the state. The cost of the property

tax, if one is levied, will have to be factored into the cost of development in a situation where fluctuating market prices and high development costs make long term investment risky. It will not be enough to say that although the natural resource in place is taxable, the local government will not levy a tax, because the next council or assembly could change that policy, particularly since the value of the resource in place will be included in the municipality's full value determination with the resultant impact on state program formula requirements to raise the local contribution and locally generated revenue. In addition, the resource industries have commented that the next worst thing to taxation is instability in taxation policies. Since they have to plan for long term investment, they need to know what to factor into their plans.

At the same time, it should be pointed out that as long as the natural resource in place is not assessable according to standard assessing techniques, it will not go onto the assessment rolls. Furthermore, much of the natural resource land that might be susceptible to property taxation is held by Native corporations that are insulated from taxation by federal law until development occurs. Leases of Native corporation land are not so protected, however. Nor are leases of state or federal land.

Option Four: Total or Partial Exemption from Municipal Property Taxation at the Option of Each Municipality

The discussion of the framework for municipal taxation found at the beginning of this report explained that the present statutory scheme contains provision for local option with regard to property tax exemptions. The local option exemptions are found in AS 29.45.050. It is conceivable, therefore, to enact an optional exemption, either total or partial, for natural resources in place. That decision should not be made, however, without consideration of all of the consequences.

On the one hand, local option is often favored because it allows local governments maximum control. Local option exemptions, however, do not exclude the property exempted from a municipality's full value determination. A local decision to exempt natural resources in place from taxation would still leave them taxable as far as the State Assessor is concerned. An increase in the full value determination would mean an increase in the absolute amount of the local contribution and the locally generated revenue required. If natural resources in place were locally exempted from property taxation, the local contribution and the locally generated revenue would have to be raised from other property tax payers or through sales and/or excise taxes. This, of course, raises the issue of fairness among tax payers. It also raises the issue of cost-effectiveness. Is it cost-effective to create a situation where the State Assessor must assess natural resources in place, while the municipality may optionally exempt resources in place from taxation?

Option Five: Taxation other than Property Taxation

In the Act, the Legislature asked that the study examine options for taxation of natural resources other than the property tax. As discussed above, of the types of tax that can be levied by a local government, only a property tax can be levied against the value of a natural resource in place. As long as it remains in place, the natural resource is part of the property. This section looks at other forms of taxation that local governments might levy against some aspect of natural resource production.

At the time a natural resource is severed or extracted, a local government can levy a severance tax. In fact, two boroughs (the Denali Borough and the Kodiak Island Borough) have already done so since the temporary exemption from property taxation went into effect. These boroughs levy a tax against the value or tonnage of the resource that has been severed or extracted.

The Kodiak Island Borough adopted what it feels is a long term progressive tax policy that levies against the gross production value of natural resources that have been severed or extracted. While this tax currently targets timber and fish harvesting operations, it can accommodate any resource development activity where a value-by-unit can be established. The value of the severed or extracted resource is multiplied by the local property tax mill levy as determined annually by the borough assembly. The borough maintains that this assures consistency and equity of taxation between natural resource property owners and the owners of other property within the borough that is taxable by the property tax method.

The Denali Borough has also adopted a natural resource severance tax. This tax targets coal, limestone or gravel that has been extracted. The tax is based on a flat rate per unit of production. The tax levy for coal and limestone is \$0.05 per ton of gross production. For gravel the tax is \$0.05 per cubic yard of production.

A severance tax is but one form of excise tax. Other forms of excise tax that might be levied include a tax on exploration activities, transportation activities, processing activities, storage activities, and the like. While a severance tax is recommended by the natural resource industries in lieu of a property tax on natural resources in place, it should be pointed out that excise taxes and property taxes are not mutually exclusive and could be levied at the same time.

Under the Alaska Constitution, Title 29, and the Alaska Supreme Court cases, local government authority to tax is very broad. According to a 1986 Attorney General's opinion, interpreting the above authorities in the context of a question about severance taxation, the provisions of Title 29, other than AS 29.45.010, are limitations on local government authority to tax. Following that interpretation, one concludes that there are no statutory or case law limitations on the power of local governments to enact excise taxes. Only property taxes and sales and use taxes are covered by Title 29 and Alaska Supreme Court cases.

X. CONCLUSIONS

The study on the issue of taxation of natural resources in place has been concluded and it is now clear that the Legislature must provide an explicit resolution to this taxation issue during the coming legislative session. The temporary exemption for resources in place expires July 1, 1992. Unless the Legislature totally exempts natural resources in place from local taxation during this session, a state of confusion will ensue for the municipalities, the State Assessor's Office and the resource industries. The study raised the consciousness of these interested parties about the meaning of taxability of natural resources in place and the implications which this taxability holds for all concerned. There is a statewide consensus that the Legislature should adopt an amendment to AS 29.45.030 totally exempting natural resources in place from local property taxation.

**Appendix A:
Property Taxation of Natural Resources
in the States and Provinces**

The Department of Community and Regional Affairs surveyed Alaska, the other forty-nine states, and the Canadian provinces regarding property taxation of natural resources. The survey questionnaire was formulated into technical and policy sections and was intended to identify resource taxation policies and procedures currently in use throughout North America. The questionnaire was mailed to state and provincial property tax officials in the spring of 1991 and responses were received over a several month period. No questionnaires were mailed to local assessors or to tax officials at the city or county level, as we thought state and provincial agencies would have a better overall picture of what is taking place, in terms of resource taxation, within their jurisdictions.

Many responses to the questionnaires were inadequate or simply raised more questions. Also, some states did not respond at all to the questionnaire. Therefore, we often made follow-up contact by phone. It was interesting, although not altogether surprising, that the phone interviews revealed that resource property taxation practice does not always conform to law or stated policy. Officials were occasionally more candid on the phone than they were in completing the questionnaire and admitted that property taxation on natural resources may not always be administered to the letter of the law. The primary reason for this was that natural resource taxation was not a significant issue in their jurisdiction because of limited resources and, therefore, the time and expense to administer such a tax aggressively could not be justified.

Through the use of the questionnaire, we also hoped to discover specific resource taxation problems or successes that may be shared by various taxing jurisdictions. After our review of the questionnaires and as a result of our phone interviews we found that problems which taxing jurisdictions share are usually of a technical nature. It is generally the old story of lack of market data and lack of comparability between subject properties that makes the job difficult for the appraiser. Lack of adequate training in the appraisal of special purpose properties such as mines and quarries is also a common problem among taxing agencies.

The policy similarities between states and provinces are simply that severance taxes and property taxes are the two most common forms of natural resource taxation. They are used, in some form, in nearly every state and province. This is really where the policy similarities end between states and provinces, however, because the extent and manner in which these two forms of taxation are implemented in each taxing jurisdiction varies so much as to make each unique.

One survey question asked if states and provinces levied taxes against natural resources that are "completely undeveloped." The term "completely undeveloped" was not defined in the questionnaire, however, generally the answer that we received on this question was no. Only eight of the states that responded to the questionnaire answered yes to this question and two of those assess undeveloped resources at a flat rate per acre; \$75 per acre in Illinois and \$60 per acre in Indiana. Four of the states that answered yes to this question only assess against mineral rights that have been severed from the fee ownership. Although several other states answered no to this question, they do in fact assess standing forest lands to some degree (generally some set amount on a per acre basis.)

For those states and provinces that stated they did not assess against undeveloped resources, a follow up question asked officials to describe at what point in the production process was taxability triggered. Most stated that taxability was triggered at the point of production or harvest. The terms to describe this point of taxability vary. For example, taxation is triggered in the Yukon Territory "when production starts" in Wyoming resources are taxable "when the mineral reaches the mouth of the mine," and in Michigan, "sometimes, the trigger is severance."

A general summary and some specific highlights of the survey follow.

General Summary:

- Thirty-one states can legally tax natural resources in place, but only twelve states actually do to varying degrees. Those states are: Arizona, Colorado, Indiana, Kentucky, Michigan, Mississippi, Missouri, South Dakota, Texas, Virginia, West Virginia and Wisconsin. Of the states that currently include in place natural resource value in real property assessments, only a few do so aggressively. This may be due to the lack of expertise at the local and state level to reliably value and defend assessed values for resources. It may also be that where there is little natural resource value, it is not cost effective to undertake the valuation of natural resources that do exist.
- Nineteen states statutorily exempt the in place natural resource value from the assessment of real property.
- The states with the most advanced programs of natural resource assessment are those resource rich states that can generate enough tax revenue to justify the staff to assess resource properties. Arizona and Kentucky are both very active in resource assessment, and both centralize the assessment activity. Assessments are made by state agencies, and tax collection can either take place at the state level with revenues being passed through to local governments, as is the case in Kentucky, or, assessed values can be provided by the state to local governments for local tax collection, which is the current policy in Arizona.
- Taxing agencies in other states that indicated they do assess and tax natural resources apply several different approaches. Many rely on the market data or sales comparison approach to value. Officials stated, however, that actual sales of resource properties are rare, hard to verify, and are often not very comparable to other properties being assessed. This results in a general disregard for assessing this type of property or at least minimizes their value estimates. Many states are aided by mandatory sales disclosure laws which require sales information on all transactions to be provided to assessment officials. Unfortunately sales information is still generally inadequate to result in reliable assessments for resource properties. Alaska does not have any mandatory sales disclosure law at this time.
- The general nature of natural resource taxation in Canada is similar to ours in the United States. Active natural resource developments are subject to federal, provincial and local government taxes mostly in the form of income and severance taxes. In British Columbia minerals are not subject to property tax, and other natural resources, such as water and timber, are taxed at the time of use or harvest.

Specific Highlights:

- Within the area of property taxation there are nearly as many different levels of assessments and applications of millage rates as there are states and provinces.
- Policies for taxation of natural resources also vary from state to state since different states have different types of resources. Taxing jurisdictions adopt taxing policies that best suit their individual needs, kinds of resources, and resource availability. Arizona assesses all recoverable minerals in the ground, Indiana values mineral ownership at \$60 per acre, Michigan exempts ore bodies up to 10 years or until they become part of an operating mine, and Montana values unproductive mining claims as agricultural grazing land.
- Across the country, in states which have elected to levy property taxes against natural resource properties, varying degrees of sophistication exist within agencies responsible for resource assessment. Kentucky has developed an elaborate geographical information system (GIS) for its resource management. They have identified and quantified their natural resources and have developed an assessment scheme that considers current economic and market conditions. The GIS is designed to manipulate resource data to create a three dimensional geographic map of the state which allows for the assessment of each coal seam or mineral deposit of taxable value parcel by parcel. Kentucky was actually forced into developing this assessment system as a result of a state supreme court case. The case determined that state constitutional restrictions did not allow the State Department of Revenue to assess natural resources at levels lower than other types of property. State officials found themselves in the position of being required to assess the resources of the state at full value with very limited resource information. They now have the GIS and a staff of 35 to value natural resources.
- Other states such as Hawaii and Rhode Island have limited mineral deposits and as a result have no specific statutes pertaining to the taxation of these resources and no resource assessment staff. Some states that exempt natural resources from property taxation levy other kinds of taxes on these resources. For example, most states levy some type of excise tax based on the production value of a severed resource or on its production unit (i.e. tax per ton.) In addition, it is common for states to levy income taxes on the resource industry.