Mineral Taxation & DCFROR

- **Taxes** – any nonpenal yet compulsory transfer of resources from the private to the public sector levied on the basis of predetermined criteria & without reference to specific benefits received so as to accomplish some of the government’s economic and social objectives.

- **Objectives & principles:**
  1. *Raising revenues* – for government to operate
  2. *Economic development* – to provide economic development and full employment.

  Taxation policies can be designed to inhibit or promote the efficient use and development of natural resources, and to influence efficient allocation of capital resources among competing uses.

  3. *Price stability* – by controlling spending and taxing levels, a government can either contribute to or inhibit inflation and affect price stability.

  4. *Wealth redistribution* – based on the belief that one pattern of wealth distribution is healthier than another.

  5. *Regulatory medium* – taxes may be imposed for nonfiscal purposes, such as to influence social behavior considered detrimental to society. e.g., alcohol and tobacco taxes, SMCRA, black lung taxes, etc.

- **Taxes are generally imposed on one of the following bases:** (1) income; (2) wealth; (3) expenditures (sales tax); (4) activity (severance taxes, franchise tax, excise tax or privilege taxes).

**Cannons of Taxation**

- **Four criteria for a “good tax”** (Adam Smith, 1904):


     - **horizontal** equity: all purchasers of the same equity pay the same tax
     - **vertical** equity: unequally situated taxpayers being taxed on their ability to pay as per progressive taxation philosophies.

     For mining industry – natural conflicts.

     Mining goal ==> the maximization of resource utilization;
     Taxing authority goal ==> the maximization of social economic benefits to the individual state of taxing power.

  2. *Convenient* – a tax that can be readily and easily assessed, collected, and administered.

  3) *Certain* – the consistency & stability in the prediction of taxpayers' bills and the amount of revenue collected over time.

  4) *Economical* – compliance and administration of a tax should be minimal in terms of cost.

Three additional criteria:
5. **Adequacy** - a tax should have the ability to produce a sufficient and desired amount of revenue to the taxing authority.

6. **Achievement of social and economic effects** - the use of taxes to reallocate resources to achieve various specific social and economic objectives.

7. **Neutrality** - a tax should not encourage inefficient allocation of resources by being so extreme that taxpayers make counterproductive economic decisions.

For the minerals industry, the key features of any tax code should incorporate:

- uniformity,
- stability,
- simplicity, and
- recognition of mining's special features.

A tax policy which provides an incentive to their minerals industry for continuously channeling new investment capital into the exploration, development, and exploitation of ore deposits.

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**Mineral Taxation**

- Critical project cost, just like labor, material and supplies, utilities, etc. Often have a significant impact on corporate decisions. Reduce project yields and tend to drive investment capital elsewhere.

- Varies from state to state, from country to country, and from one mineral commodity to another ==» **essential** to compare the relative economics of investment alternatives on an **after-tax basis** to have a valid economic analysis.

- **After-tax rate of return** commonly is referred to as Discounted Cash Flow Rate of Return, or: Profitability Index (P.I.), Investor's Rate of Return, True Rate of Return, and Internal Rate of Return (IRR).

- Fundamental attitudes of heavy taxation on minerals:
  - "Natural heritage" theory – minerals, a free gift of nature for the benefit of all mankind, so the benefits derived should be shared by all.
  - Captive theory – orebody cannot be dismantled and moved to another location, any mine can be taxed with impunity.
    - Also, corporate owner is typically an absentee owner that has little representation within the taxing jurisdiction – failing to recognize, the mobility of investment capital.

- Interest in mining taxation has increased recently due to:
  - higher taxes to discourage mineral development– environmental concerns
  - high taxes used to discourage for conservation concerns due to shortage of certain minerals
  - ever-increasing need for revenue to pay for growing social programs.
Type of Mineral Taxes

1. **Income taxes** – Imposed on individuals and on corporations. Levied by the federal and most state governments, the tax is usually based on net income, or gross income less certain defined deductions. The tax rate is generally either fixed or progressive.

2. **Property Taxes** – Typically an ad valorem (according to value) tax based on appraised value of real and personal property. In the case of mining it is extremely difficult to accurately determine the fair market value of property – particularly when the ore deposit is taxed.

3. **Severance Taxes** – A tax unique to the extraction of natural resources (renewable as well as nonrenewable). It is distinguishable by the fact that it is related in some manner to the actual removal of natural resources (fish, timber, minerals).

4. **Transaction Taxes** – A tax imposed upon the consummation of a retail sale. A good example is the common retail sales tax which is levied against all retail sales of certain commodities.

5. **Excise Taxes** – A tax imposed on the manufacture, sale, or consumption of specific, selected commodities and/or activities. They are not imposed on persons or property as such. All license taxes are considered to be excise taxes.

6. **Miscellaneous Taxes** – Other taxes commonly paid by mining companies are: (a) unemployment tax, (b) import and export taxes, (c) franchise taxes, and (d) user taxes on various activities. The distinction between these different types of taxes is not always well defined.