Fool's Gold: Why Nevada's Net Proceeds of Minerals Tax Is Not A Real Tax

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Executive Summary

Kersten Communications Inc. has found that mining companies extracting gold from mines in Nevada are paying an extremely minuscule tax rate, on the order of 1%, to Nevada's General Fund despite record production and profit numbers in recent years.

Moreover, Nevada's current Net Proceeds of Minerals Tax fails to capture the huge economic benefits that international mining companies reap from the state by extracting gold from two dozen mines located in the state.

This brief report seeks to update a 2009 report issued by the Progressive Leadership Alliance of Nevada, titled "Fool's Gold: The Silver State's Tax Structure Inadequate and Inequitable.

Total gross production value of gold in the state reached an all-time high of $6.6 billion in 2010, yet mining companies only paid taxes on 42% of this amount or $2.7 billion due to Nevada law which provides a series of generous deductions for expenses related to mining operations. Nevada mining companies' deductions reduced their reported taxable value by 58% through the aggressive use of tax deductions that had rarely, if ever, been audited, according to the Nevada Department of Taxation.

For 2010, mining companies only paid $71.7 million through the Net Proceeds of Minerals Tax to the state's General Fund, despite having gross production value of $6.6 billion—an effective tax rate of 1%. A total of six mines, or ¼ of the 24 mines in the state reported no taxable value despite reporting $88.6 million in gross production value. Thus, it could be said that Nevada's mining tax regime is more "deduction" than tax—fool's gold.

A brief review of the tax regimes of other major gold producing jurisdictions by Kersten Communications Inc. has found that Nevada's 1% effective tax rate puts the state near the bottom of other jurisdictions in terms of the mining tax burden. This low 1% rate is compounded by the state's modified business tax that fails to adequately tax the profits of big box stores such as Walmart, while placing and added burden on the state's smallest businesses.

Thus, we conclude that Nevada could reform its "Net Proceeds" tax to raise additional revenues without compromising the international competitiveness of mining companies doing business in Nevada.

A review of company financial statements filed by the state's two mining industry leaders Barrick and Newmont shows that these companies are posting record income and profits, certainly suggesting that these companies could afford to pay a fair share of taxes to aid our struggling state.

The Nevada Mining Oversight and Accountability Commission (MOAC) and the Nevada Legislature are urged to take the findings in this report under consideration and advance efforts to reform the state's current Net Proceeds of Minerals Tax.

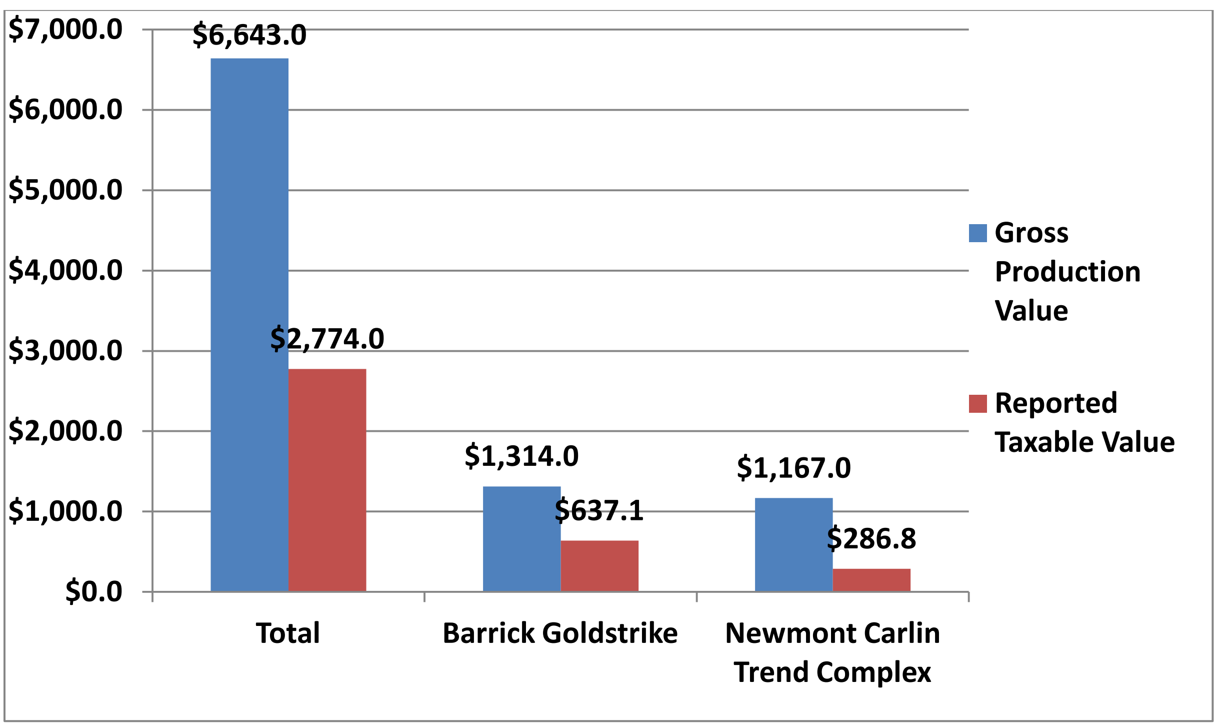
Summary of Key Findings

Chart #1 and Table #1 on the next page summarize the most recent publicly available information on Nevada's Net Proceeds of Minerals Tax. This tax primarily impacts gold and silver production since these are the two primary minerals mined in Nevada, particularly gold, accounting for roughly 90% of overall annual production value.

Chart #1 below illustrates the large gap between the "gross production value" of gold and the "reported taxable value" of gold for all Nevada mining operations for 2010, the most recent year for which data is available. The total value of gold produced in the state was $6.6 billion, but companies are only required to pay taxes on 42% of this value or $2.7 billion due to the aggressive use of deductions allowed by Nevada law. This method for taxing gold runs counter to the tax regimes in place in other jurisdictions as will be discussed in greater detail later.

Barrick and Newmont's two largest mines, Goldstrike and Newmont Carlin, account for more than 1/3 of total gold production in the state.

Chart #1: Summary of Gross Production Value and Reported Taxable Value of Gold for the 2010 Calendar Year



Source: Nevada Department of Taxation

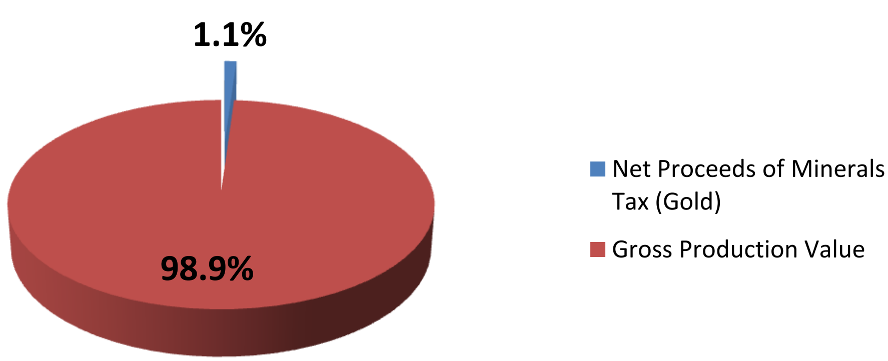
As Table #1 below illustrates, mining companies operating in Nevada only paid an effective tax rate of 1.1% of this value or $71.7 million to the state's General Fund. (Note: 50% of the Net Proceeds tax go to local governments and the total tax amount is capped at 5% in the state constitution). (isn't this a result of the NPOM? The split is 71.7 M for the counties in which the minerals are mined and 71.7 M goes to the general fund)

Table #1: Nevada Gold Mine Industry Deductions from Gross Production Value 2000-2010 ($ Millions)

Year	Gross Production Val.	Reported Taxable Value	Deducted Value	% Deducted	NPOM Taxes Paid to General Fund	Taxes Paid to GF as % of Gross Production Value
2010	$6,643	$2,774	$3,869	58%	$71.7	1.08%
2009	$5,102	$1,542	$3,560	70%	$44.8	0.88%
2008	$5,384	$1,525	$3,859	72%	$39.5	0.73%
2007	$4,853	$1,262	$3,591	74%	$30.4	0.63%
2006	$4,333	$1,035	$3,298	76%	$23.5	0.54%
2005	$3,388	$648	$2,740	81%	$14.1	0.42%
2004	$3,025	$710	$2,315	77%	$16.0	0.53%
2003	$2,728	$626	$2,102	77%	$14.1	0.52%
2002	$2,473	$386	$2,090	84%	$8.3	0.34%
2001	$2,270	$326	$1,944	86%	$6.9	0.30%
2000	$2,473	$483	$1,990	80%	$12.0	0.49%
Total	$42,672	$11,317	$31,358	76%	$281.3	0.66%

Source: Nevada Department of Taxation

Graph #2: Summary of Nevada's Proceeds of Minerals Tax as a Percentage of Gross Production Value for 2010



Source: Nevada Department of Taxation

Table #2 below summarizes the number of Nevada gold mines and their gross value of production for mines reporting no taxable value for 2000-10. For 2010, a total of six mines reported no taxable value despite reporting a combined gross value of production of $88.6 million. These mines paid no taxes to the Nevada General Fund since they were able to erase their total tax liability through the use of deductions.

Table #2: Number of Nevada Gold Mines Reporting Gross Values But No Taxable Values 2000-10 ($ Millions)

Year	Mines Reporting Gross Values	Mines Reporting No Taxable Values	Gross Value of Production from Mines Reporting No Taxable Value	Taxes Paid to General Fund From Mines Reporting No Taxable Value
2010	24	6	$88.6	0
2009	24	7	$111.1	0
2008	24	7	$281.3	0
2007	25	7	$365.5	0
2006	27	8	$183.7	0
2005	28	11	$802.9	0
2004	29	15	$403.1	0
2003	25	10	$573.6	0
2002	28	15	$639.7	0
2001	30	17	$711.0	0
2000	31	16	$245.9	0
Total			$4,406.4	0

Source: Nevada Department of Taxation

Table #3 on the next page summarizes the gross production value and reported taxable values at the Barrick Goldstrike Mine and Newmont's Carlin Trend Project—the state's two most productive mines which account for more than 1/3 of total gold production in the state.

This table shows that Barrick paid $24 million to Nevada's General Fund in 2010 for this one mine, which is an effective tax rate of 1.75%. Newmont paid $10.2 million which represents only a 0.87% effective tax rate.

These companies note that they pay property taxes, the state sales tax and the modified business tax, but most businesses pay these other taxes and they do not even come close to making up for the miniscule amount that these companies pay through the net proceeds of minerals tax as a percentage of gross production.

Table #3: Gross Production Value and Reported Taxable Values at Barrick Goldstrike Mine and Newmont's Carlin Trend Project 2000-10 ($Millions)

Year	Gross Production Value	Reported Taxable Value	Taxes Paid to Nevada General Fund	Taxes Paid to GF % of Gross Prod. Value
		Barrick Goldstrike Mine		
2010	$1,314.0	$637.1	$23.0	1.75%
2009	$1,171.0	$481.9	$16.8	1.43%
2008	$1,252.0	$276.0	$8.5	0.68%
2007	$1,027.9	$328.1	$10.0	0.97%
2006	$1,008.5	$373.1	$11.4	1.13%
2005	$774.0	$208.4	$6.4	0.83%
2004	$679.2	$184.0	$5.9	0.87%
2003	$660.4	$160.1	$5.1	0.77%
2002	$520.7	$0.0	$0.0	0.00%
2001	$442.1	$0.0	$0.0	0.00%
2000	$459.8	$35.7	$1.2	0.26%
Total	$9,309.6	$2,684.4	$88.3	0.95%
		Newmont's Carlin Trend Project		
2010	$1,168.0	$286.8	$10.2	0.87%
2009	$1,154.0	$241.8	$8.4	0.73%
2008	$1,158.0	$276.1	$8.5	0.73%
2007	$932.9	$107.8	$3.3	0.35%
2006	$771.8	$22.7	$0.7	0.09%
2005	$622.7	$0.0	$0.0	0.00%
2004	$467.9	$20.9	$0.7	0.15%
2003	$394.7	$0.0	$0.0	0.00%
2002	$416.8	$17.2	$0.6	0.14%
2001	$384.7	$30.5	$1.0	0.26%
2000	$447.2	$101.6	$3.4	0.76%
Total	$7,918.7	$1,105.4	$36.8	0.46%

Source: Nevada Department of Taxation

Background on Nevada's Net Proceeds of Minerals Tax

Article 10 of the Nevada Constitution, ratified in 1865, provides that only the net proceeds from mines and mining claims will be taxed, as opposed to gross value which is common place in other states and nations.

From 1865 until 1989 the net proceeds of minerals tax rate was the same as the property tax in each county. In 1989, Nevada voters amended the Nevada Constitution to set the maximum net proceeds of minerals tax rate at 5%, separate from the local property tax rate, according to the NTA report.

The net proceeds from the sale of all minerals mined or produced in Nevada are subject to the net proceeds of minerals tax with the exception of sand and gravel products, which are subject to the state's sales tax.

The total amount of net proceeds of minerals tax collected statewide fluctuates from year to year, dependent on the amount of material sold and the price received. For most commodities such as gold, silver, copper, oil, gypsum and other industrial minerals, the price is influenced by worldwide market conditions.

(Source: "Understanding Nevada's Net Proceeds of Minerals Tax," 2007-08 Edition, Nevada Taxpayers Association)

Nevada's Net Proceeds of Minerals Tax Needs to Be Reformed To Ensure That Mining Companies Pay Their Fair Share of Taxes

A review of Nevada's "net proceeds of minerals tax" by Kersten Communications Inc. has found that the current tax regime does not provide for a fair level of taxation of the Nevada mining industry.

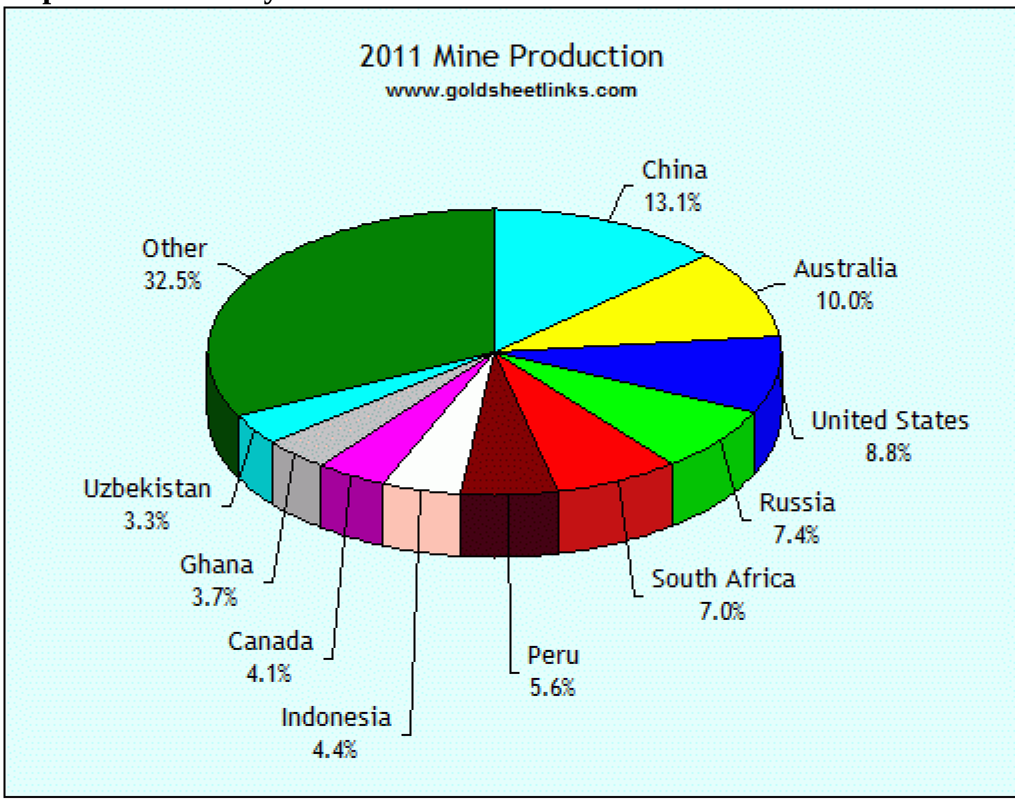
Moreover, the tax needs to be reformed to ensure that a more appropriate level of taxation is implemented that sufficiently compensates the State of Nevada and its taxpayers for the removal of scarce natural resources.

According to a report by PriceWaterhouseCoopers, "in most jurisdictions, the mining enterprise is obliged to pay some form of "economic rent" to the government as a consequence of the government's ownership of the resource."

Furthermore, "the ideal economic rent will: be internationally competitive and relate to the enterprise's ability to pay," according to the report. By these industry standards, Nevada's tax could be increased significantly without negative consequences.

A brief review of other major gold producing jurisdictions by Kersten Communications Inc. has found that Nevada's 1% effective tax rate puts the state near the bottom of other jurisdictions in terms of the mining tax burden. This low 1% rate is compounded by the state's minimal modified business tax that fails to adequately tax corporate profits.

Graph #2: Summary of Worldwide Gold Production for 2011



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Source: Goldsheetlinks.com

Graph #2 above shows that many of the countries included in Table #4 account for a significant portion of global gold production in 2011.

Table #4 on the next page summarizes the mining related taxes for a dozen of the major gold producing countries around the world. Mining companies typically pay some sort of mining tax which is typically based on gross value, as opposed to net value.

A review of these findings shows that Nevada's 5% tax on "net proceeds," which amounts to about a 1% tax on "gross proceeds" to the state General Fund places the state among the lowest in terms of mining tax burden on a worldwide basis.

Thus, we conclude that Nevada could reform its "net proceeds" tax to raise additional revenues without compromising the international competitiveness of mining companies doing business in Nevada. Moreover, mining companies established in Nevada are highly unlikely to leave the state even if the tax was increased in large amount.

Table #4: Summary of Mining Related Taxes for Major Gold Producing Nations

Country	Summary of Mining Related Taxes
Angola	Mining Companies are subject to specific taxation regime, pay same 40% corporate income tax Mining Surface Fee: Due based on surface area licensed during prospecting, varies between $1-4/Km Mining Royalty: Charged ad valorem on market value of annual output at various rates between 2-5%
Argentina	Mining taxed at 3% net smelter return.
Botswana	Mining taxed at 15% of gross sales less realization expenses.
Brazil	Gold taxed at 3% of gross sales
Canada (Ontario)	Mining taxed at 20% of taxable profit.
Chile	Tax on annual sales of copper ranging between 12.00 and 50.00 metric tones of fine copper at a marginal rate ranging from 0.5% to 4.5% is applied over the taxable operational mining income. Annual sales over 50.00 metric tones of fine copper are subject to an effective tax burden ranging from 5% to 14% over the taxable operational mining income.
China	Resource tax rates varies according to the type of mineral. A pilot program of 5% of sales value is being tested in the Xinjiang region and is foreseen to be rolled out nationwide. Compensation fee for mineral resource rate is 0.5% to 4% on sales revenue of mineral.
Guyana	Gold taxed at 5% of gross sales.
Indonesia	Gold taxed at $235 per kg.
Peru	New legislation signed in 2011 required new royalty payments ranging from 1% to 12% of operating profits, along with a windfall profits tax ranging from 2% to 8.4% of net profits aimed at increasing tax revenues during mining boom years. Companies that have legal tax stability agreements, including Barrick Gold, which protected them from future tax changes, now must pay a special contribution tax of between 4% and 13.2% of operating income, depending on the operating margin.
Russia	Mineral Resources Extraction Tax (MRET) is levied at the rate ranging between 3.8% and 8.3%, depending on the mineral and based on the value of the extracted mineral. Rate is 6% for gold.
South Africa	Additional 10% rate is levied on mining companies.

Sources: PwC Global Mining Group, PKF Worldwide Tax Guide, PriceWaterhouseCoopers.

Leading Nevada Mining Industry Companies Barrick and Newmont Record Income and Profits

A review of company financial statements filed by the state's two mining industry leaders Barrick and Newmont shows that these companies are recording record income and profits, which proves that these companies could afford to pay their fair share of taxes.

According to the Barrick Annual Report for 2011, "Barrick recorded its most profitable year ever." "Our total cash margins broke through previous all-time highs, expanding by 37% to $1,118 per ounce from $819 per ounce in 2010 as we captured the benefit of rising gold prices and one of the lowest total cash costs among our senior peers," states the report.

In 2001, Barrick's adjusted net earnings rose 33% to $4.7 billion from $3.5 billion in 2010 and translated to a return on equity of 22% which surpassed the senior gold producer average return on equity of 14%.

Newmont is a similar success story. *The Wall Street Journal* called Newmont Mining the "Apple of Gold Stocks" in a September 2011 report.

Newmont's 2011 annual report also reported record financial gains for the company. The company's total revenues grew to an all time high of $10.4 billion and adjusted net income increased to $2.2 billion as the company generated $3.6 billion in operating cash flow.

In April 2012, Newmont Mining Corporation reported that its income for the first quarter of 2012 was up 9% from the first quarter of 2011. Average realized gold and copper prices were up 22% from the prior year quarter, which were largely responsible for the increased income and profits, according to a company news release.

"We also saw gold operating margin expansion of 29%, which outpaced the 22% increase in the average realized gold price from the prior year," said Richard O'Brien, President and CEO.

Conclusion: Nevada's Net Proceeds of Minerals Tax in Dire Need of Reform

Nevada needs to reform its current net proceeds of minerals tax with a sensible tax regime that provides for a fair tax on mining companies doing business in Nevada.

In 2011, the Nevada Legislature approved Senate Joint Resolution 15 which repeals the constitutional provision establishing a separate tax, not to exceed 5%, on the net proceeds of mines. This measure will need to be approved by a majority of voters to take effect.

The intent is to provide the Nevada Legislature with the freedom to redesign the net proceeds of minerals tax through legislation, as opposed to having to go to the ballot to revise any of the constitutional protections that are currently granted to the mining industry.

As has been seen in the comparison with other nations, most other jurisdictions tax gold production based on gross value as opposed to net value, and levy a significantly higher rate than Nevada's effective 1% on gross value. Taxing gold production on gross value would effectively disallow the manipulation of the net minerals tax through the aggressive use of deductions, as is allowed under current law.

Nevada Department of Taxation officials have admitted that the current system "operates under a self-reporting tax system," according to a report by Mineweb.com.

Past audits of these deductions conducted by the Nevada Department of Taxation have led to the significant disallowance of deductions and settlement agreements requiring mining companies to pay significant amounts of additional taxes, according to a 2011 report by the Nevada Department of Taxation.

The current system of endless deductions gives mining companies carte blanc to reduce their tax bill by claiming excessive deductions without fear of any oversight due to the lack of oversight and auditing of mining company net proceeds tax returns. Reform of the system should address this current enforcement problem and ensure that mining companies pay a fair tax on their gross production value of minerals produced in the state.

The Nevada Mining Oversight and Accountability Commission and Nevada Legislature are urged to take the findings in this report under consideration and advance efforts to reform the state's current net proceeds of minerals tax.

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