Committee on Resources

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Witness Statement

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Effect of Federal Mining Fees and Proposed Federal Royalties

on State and Local Revenues and the Mining Industry

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Chairman Cubin, members of the subcommittee, my name is Tom Myers. I am a director of the Nevada based mining advocacy group *Great Basin Mine Watch*.

Thank you for this opportunity to testify on an issue of immediate concern to members of our group and the state of Nevada.

This hearing effectively considers two subjects: federal mining fees such as the claim maintenance fee and royalty payments. As I will describe, both fees and royalties have a positive impact on the economy at large, statewide and locally and on the environment. They are also essential for maintaining the BLM's role in managing the minerals program.

Claim Maintenance Fees Have Protected the Public's Resources

As a part of their 1993 appropriations bill, Congress allowed the BLM to start collecting a $100 per year per claim fee on mining claims as a part of their appropriations. This was a two-year authorization. During the 1994 appropriations process, the fee was reauthorized through September, 1998 and an additional $25.00 location fee was added. Finally, the 1998 appropriations reauthorized both fees through September, 2001. These fees are in addition to the $10 recording fee authorized by the Federal Lands Policy and Management Act in 1976.

The maintenance fees (originally called a rental fee) replace the requirement for the claimholder to perform $100 of development on the claim. In general, prior to mining, the development was for exploration on the site. Annually, the claimholder would provide to the BLM a signed affidavit that they had completed this work. It is our opinion that many of the affidavits would have been false statements. If they were not false, the amount of damages and unreclaimed roads and exploration scars would be far greater than currently

exists. The legislation provided for a small miner exemption: anyone holding less than ten claims could continue to perform maintenance on the site.

The money collected from these fees goes directly to the mining law administration budget of the BLM. It is deposited in a special account from which Congress appropriates to the program in the BLM. Any additional fees go to the federal Treasury to help balance the budget. The following table shows the amount of money paid nationally for claim maintenance and location fees and the appropriation to the BLM from this fund(1).

Fiscal Year	Fees Collected	Appropriations
1993	53,200,000	
1995	30,700,000	28,500,000
1996	33,800,000	28,500,000
1997	35,800,000	32,500,000
1998	30,000,000	32,500,000

In FY 1998, the claim brought in $13,387,600 in Nevada alone(2). As the table illustrates, the fee provides an important revenue stream. Fees from the industry are paying for the administration of the program. If this subcommittee proposes the elimination of the fee, the administration of the program must be funded from general revenues. Without some source of funding, the public lands will be damaged and the BLM will not be able to fairly administer the Mining Law which will be a negative deterrent to the efficient development of the nation's mineral resources. Defunding the program is not an option.

Who could oppose this fee? For large companies, the amount is a mere blip on their annual budget. The small miner exemption eliminates the fee as an issue for honest, small scale miners and exploration companies. For large companies with many claims that are actively pursuing the resource on their claim, the claim maintenance fee may represent an additional cost. For companies that are just holding the claim until the market improves, the fee frees them from doing expensive and environmentally damaging maintenance work.

The only people really hurt by this fee are speculators. These are people who stake multiple claims in a minerals rich area in hopes of mining the legitimate mining companies who would rather buy out a claim than challenge its validity before the Appeals Board or in the courts. These speculators may not have the money to pay the annual fees.

It is also to important consider what type of fee a maintenance fee is. We conclude that this is a holding fee rather than a mining fee. By holding fee, we mean that the fee is a fee paid to the federal government for the right to hold the land for the future use by the claimholder. The land is not subject to disposal under other laws without paying off the claimholder. The fee is not paid for the right to mine the land.

Most proposed Mining Law reforms would also impose "holding fees" or rental charges on all unpatented mining claims on Federal land. In the proposed legislation, these per acre rental fees would increase with the age of the claim. Both the proposed rental fees and the current maintenance fee primarily affect holders of **non-producing** Federal mineral claims. They represent only a tiny part of the overall costs of an operating mine. For non-producing claims, rental or maintenance payments can be avoided by simply abandoning

those claims that have little prospect of profitable near term development. In 1993 in Nevada, the number of registered claims dropped from 258,000 on February 28 to 125,700 claims on September 1[(3)] while nationally claims dropped from 760,000 to 294,000[(4)]. In any case, since the burden of these payments does not fall on operating mines with substantial employment, the employment impacts are likely small or non-existent. If mining claims are abandoned because profitable future development is not imminent, those minerals are not lost. As economic conditions change and mining of that land becomes viable, claims could be filed again. The primary impact of these rental charges is to discourage the indefinite holding of claims to minerals on Federal lands for speculative (as opposed to production) purposes. No substantial negative employment impact can be attributed to this.

Royalties: Does the Public Get its Fair Share?

Great Basin Mine Watch supports an 8 percent net smelter royalty which is in the low end of the 5 to 15% range charged by states on their lands. It may be slightly higher than the average charged by private owners[(5)]. A gross royalty calculates the payment based on the value of the refined mineral minus the nonmining costs of smelting. Smelting is more relevant with respect to copper than gold as the costs of smelting gold are less than $1.00/ounce[(6)].

What will be the effect of this additional cost to the industry? The following table illustrates a series of calculations of net profit for the production of 1,000,000 ounces of gold at the average production price of $212/ounce for three different gold prices[(7)]. A net smelter royalty is based on the final sales price of the mineral minus the cost of refining which, for gold, is less than $1.00/ounce[(8)]. The term is based on copper smelting and outdated for gold, but continues to be used in royalty proposals.

Price of Gold per Ounce

	$350	$300	$250
Gross Revenue for 1,000,000 oz	350,000,000	300,000,000	250,000,000
(smelting costs, $1.00/oz)	(1,000,000)	(1,000,000)	(1,000,000)
(transportation, guessed)	(1,000,000)	(1,000,000)	(1,000,000)
Net Smelter Returns	348,000,000	298,000,000	248,000,000
(8% Net Smelter Royalty)	(27,840,000)	(23,840,000)	(19,840,000)
Gross Mining Income	320,160,000	274,160,000	228,160,000
(operating costs)	(212,000,000)	(212,000,000)	(212,000,000)
Net Operating Income	108,160,000	62,160,000	16,160,000
(depreciation)	(10,000,000)	(10,000,000)	(10,000,000)
Predepletion Income	98,160,000	52,160,000	6,160,000
(depletion @ 50% of pre income)	(49,080,000)	(26,080,000)	(3,080,000)
Pretax Profit	49,080,000	26,080,000	3,080,000
Federal Tax @ 32%	(15,705,600)	(8,345,600)	(985,600)
State Tax @ 5%	(2,454,000)	(1,304,000)	(154,000)
Net Profit	30,920,400	16,430,400	1,940,400
Without the Royalty			

Net Operating Income	136,000,000	86,000,000	36,000,000
Predepletion Income	126,000,000	76,000,000	26,000,000
(depletion)	63,000,000	38,000,000	13,000,000
Pretax Profit	63,000,000	38,000,000	13,000,000
Federal Tax at 32%	(20,160,000)	(12,160,000)	(4,160,000)
State Tax at 5%	(3,150,000)	(1,900,000)	(650,000)
Net Profit	39,690,000	23,940,000	8,190,000
Decrease in profit due to royalty	8,769,600	7,509,600	6,250,000

Based on these conditions, the effective royalty rate, after deductions are considered, is only 5.48%. More importantly, profits are still made even at the industry average production costs even with gold prices dropping to $250/oz. It also must be mentioned that the depletion allowance is not a net cash flow loss to an operation but a tax deduction representing the fact that reserves are being depleted.

When compared to a net profit of $39,690,000 with gold selling at $350/oz without a royalty, the profit loss is 79.3% just for a price drop to $250/oz. With the proposed royalty, the additional profit loss is only 15.7%. During the past week, the price of gold dropped by about $15.00/ounce which also represents about a 15% drop in profit. A royalty would be a small portion of the profit loss.

But a longer term look reveals much more about the industry and production. Consider the impact of overall price changes since 1987. Between 1987 and the end of 1992 the real price of gold fell by 40 percent or about $220 per ounce. During that time period of precipitous price declines, gold production boomed, increasing 128 percent. An industry that can boom amidst price declines that are 15 times the likely effective size of a Federal royalty is unlikely to be crippled by that royalty.

It is very difficult to believe that royalties will cause much of a difference in mining investment and employments, especially since royalty costs will be far less than the general price changes, generally negative, experienced by investors in the gold market during recent years.

But more importantly, the industry has adjusted to changing prices by decreasing their costs substantially with time. For US producers, total cash operating costs have declined from $256/ounce in 1995 to $214/once in 1997 and are projected to be under $190/ounce in 1998[(9)]. Recent costs at Cortez's Pipeline Deposit have been $125/ounce and were previously below $100/ounce. Placer Dome reports their average costs have dipped below $200/ounce globally.

How does a company reduce its costs? The preferred method, both by the company and the worker, is to discover and produce higher quality ore. When a company moves less ore per ounce of mineral, its costs go down.

But unfortunately for the worker and Nevada's economy, production costs are often lowered by more efficient processing, which usually means more mechanization and less labor. Nationally, about 2000 workers lost their jobs in the mining industry in 1998. About 1200 of those were due to production cutbacks and about 800 were due to bankruptcy which may have been affected by gold prices. In 1997, about 14,800 workers were employed directly in Nevada's mining industry [(10)].

Another way of decreasing costs is through mergers. During periods with low prices, corporations frequently

expand their reserves by buying out smaller producers. Newmont recently purchased Santa Fe to become the largest US gold producer. Today, approximately 75% of Nevada's gold production is derived from two companies, Newmont Gold Co. and American Barrick Gold Co., although there continues to be active participation by numerous other larger and medium sized companies with Nevada holdings[(11)]. This consolidation has allowed Newmont to decrease costs by processing ore at centralized facilities rather than at each mine. This, of course, decreases costs, and employment.

Currently, the average royalty over all lands in the United States is about $11.00/oz. Because it is an average, the actual royalty on state and private lands must exceed the average because all production on federal lands is free of royalties. Because only 30% of all gold production occurs on public land, the actual royalty must have been about $14.00. Thus, the lack of a royalty on public land represents a subsidy of about $14.00/ounce to the industry to produce on public land.

The total cash cost average may also be considered as a distribution of cumulative production as a function of the price of gold. Because of a few very high cost producers, almost 6.5 million of the nation's 8.5 million ounce production occurs at costs below the current average cost. Almost 88% of all production costs less than today's price of gold (5/12/99, $272/ounce). Even if the royalty adds $15.00 directly to the cost, more than 85%, or just a 3% decrease, of all production will still occur at rates less than the current price of gold.

Many of the highest cost producers will continue to produce at a loss because of their high capital investment or because they must process poorer to reach more profitable ore so that their costs will decrease. Pits that extend below the water table will fill with water if operations cease; due to water quality problems, temporary shutdowns may cause permanent loss of mining opportunities, therefore few companies will allow this to occur. Not many will experience Alta's problems where they were improperly processing their ore which caused very high costs[(12)] and possibly led to the company's bankruptcy.

In conclusion, the impact of a Federal royalty will likely be a 2 percent reduction in total production and employment, which represents about a day's worth of normal job growth in the West. Only one in a thousand western jobs are in metal mining and only one in six of

those jobs relies upon Federal land, therefore royalty payments have the potential to affect only a

tiny sliver, about 3 out of every ten thousand jobs (0.025 percent), of total western jobs. And that

potential impact itself will only be a tiny fraction of these jobs. It should not be surprising, then, that the potential negative impact of Mining Law reform on the western economies is

tiny.[(13)] And the minerals will still be there for future extraction.

This is not to make light of the concern of local communities in eastern Nevada who do depend to a substantial degree on minerals production. However, the answer is not continued subsidized low costs of production; the answer is more diversification of the local economies. Elko and Ely should capitalize on the beauty of their location in the state with the most remaining defacto wilderness of any Western state. As Tom Powers has reported, counties with the most wilderness have, by far, the highest growth rate of any other places in the West[(14)]. Extraction is not sustainable; natural beauty is.

Great Basin Mine Watch recommends that royalties be used for abandoned mine reclamation and cleanup at existing operations that are insufficiently bonded. Production in Nevada alone will yield about $143,000,000 per year. Nevada is loosing a huge economic opportunity because the federal government does not charge a royalty that is applied to abandoned mine cleanup. Reclamation activities require skilled engineers and labor. The number of sites requiring cleanup could assure a sustainable source of jobs for decades, unlike primary production which is extremely boom and bust. Consider two problems in Nevada which may require large sums of money to fix.

According to the Nevada Department of Environmental Protection (NDEP), 13 mines in the state are owned by companies in bankruptcy.(15) Potential difficulties recently prompted the NDEP to request a special appropriation of $1,000,000 from the state to establish an emergency response fund to provide for operation of those mines in the event the operators decide to abandon the mine sites, which was approved by the state in 1998. The state is also concerned about the cost of interim operations prior to beginning reclamation and closure of the mine sites under bankruptcy, and in cases where bankruptcy appears imminent they have made requests for additional bonding to provide for up to six months interim operations.

NDEP has also expressed concerns with the situation in the state with respect to self-bonding. Approximately 75% of the $438,000,000 in total bonding liability by the state and federal agencies is covered under self-bonding provisions allowed in Nevada. In the event of continued depressed gold prices, the probability of additional mines closing and companies filing for bankruptcy protection will increase. In addition there is the potential that some of the major mining companies could potentially face financial difficulties, in part because some of those companies livelihoods are entirely based on gold production.(16)

Royalties could be used to help remedy these local problems.

This discussion may best be summarized by quoting from the Mineral Policy Center(17):

a. Metal mining employment in the West is a very small part of total employment (one tenth of one percent).

b. Most metal mining (70 to 85 percent of it) in the West does **not** take place on Federal land. It takes place on private, state, and tribal lands where royalties are already being paid.

c. The net impact of the proposed 8 percent royalty is very modest compared to the value of the minerals when offsetting reductions in taxes and other royalties are considered.

d. The royalty would not raise the cash costs of any significant number of mines above current commodity values.

e. In the near term, mines often continue to operate even when cash costs are above the value of the mineral being extracted.

f. Mines can control their costs per unit by adjusting the quality of the ore that they process and engaging in other cost control measures.

Conclusion

It is time to change the economy of most of Nevada and the rest of the rural West from a third-world style,

raw material exporting economy to a first world economy where environmental amenities and open space are valued and lead to growth and prosperity. The fastest growing rural Western regions are places where people want to live because of their beauty, not because of what they can extract from the Earth or feed their animals with.

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1. Roger Haskins, BLM Washington Office, 5/13/99, personal communication.

2. Steward, L., BLM NV State Office, 5/12/99, personal communication.

3. Id.

4. Haskins, note 1.

5. Dobra, J.L., 1999. The U.S. Gold Industry 1998. Natural Resource Industry Institute, University of Nevada, Reno page 22.

6. Id., page 21.

7. These calculations follow the report: Humphries, M., Mining Law Reform: The Impact of a Royalty, Report 94-438 ENR, Congressional Research Service, Washington.

8. Dobra, page 21.

9. Dobra, page 4.

10. Price, J.G., 1998. Overview, pages 3-9 in The Nevada Mineral Industry, 1997. Nevada Bureau of Mines and Geology Special Publication MI-1997.

11. Kuipers, J., 1999. DRAFT Report to the National Wildlife Federation. To be released Summer, 1999.

12. At the company's Olinghouse Mine. Local newspapers reported processing problems. A local mining engineer suggested to me that they were using improper techniques.

13. MPC, All that Glitters.

14. Power, T.M., 1996. Lost Landscapes and Failed Economics. Island Press.

15. [15] The list of mines currently in bankruptcy includes the County Line, Paradise Peak/Ketchup Flat, and Yerington mines owned by Arimetco International Inc (the County Line and Paradise Peak/Ketchup Flat mines were formerly owned by FMC Gold Corp, which sold the closed mines and reclamation liability to Arimetco), the Florida Canyon mine owned by Pegasus Gold Corp. (now Apollo Gold), the Mt. Hamilton mine owned by Mt. Hamilton Mining Co., the Tonkin Springs mine owned by the Tonkin Springs Joint Venture, and the Gold Bar and Gold Canyon mines owned by Atlas Gold Mining Inc.

16. Kuipers

17. MPC, All that Glitters.

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