

MEMORANDUM

TO: Subcommittee on Energy and Mineral Resources

FROM: Randy Foote, General Manager, Intrepid Potash New Mexico LLC

SUBJECT: Potash Royalty Reduction Act

**HEARING: Thursday, September 9th 2004, at 2:00 p.m.
Room 1324 Longworth House Office Building**

Potash History in Carlsbad, New Mexico

In 1981, when I started working in the potash industry, there were seven independent potash mines operating in Carlsbad, New Mexico. Today, through mine closures and consolidations, there are two potash companies remaining. (1) Intrepid Potash New Mexico LLC – owns the mining facilities once owned by Potash Company of America, Kerr McGee, National Potash, and Mississippi Chemical. (2) IMC Global – owns the mining facilities once owned by Duval.

<u>Production & Employment Statistics</u>	<u>Product</u>	<u>YTD Tons</u>	<u>Employees</u>
<i>Carlsbad Potash Industry – 1981</i>			
<i>International Mineral Chemical (IMC)</i>	Potash	350,000	650
	Potassium Sulfate	200,000	
	K-MAG	550,000	
	Total	1,100,000	
<i>Potash Company of America (PCA)</i>	Potash	1,000,000	650
<i>AMAX</i>	Potash	800,000	425
<i>Kerr Mc Gee</i>	Potash	600,000	500
<i>Duval</i>	K-MAG	300,000	250
<i>Mississippi Chemical Company (MCC)</i>	Potash	300,000	250
1981 TOTALS:		4,100,000	2,725
<i>Carlsbad Potash Industry – 2004</i>			
<i>IMC Global</i>	Potash	500,000	550
	K-MAG	1,000,000	
	Total	1,500,000	
<i>Intrepid Potash New Mexico LLC</i>	Potash	900,000	455
2004 TOTALS:		2,400,000	1,005

Major Events Impacting the Carlsbad Potash Industry

Potash is primarily used as a fertilizer so the economics are tied to the fertilizer industry, which is directly affected by the farming economy. During the 1980's, the farming economy was hampered by over production of grain and large inventories of farming commodities around the world. The farmer's reacted to this situation by trying to lower production costs instead of reducing production due to the government subsidy they received for their products. Farmer's decreased their use of potash, which drove down potash prices and sales.

In addition, the Federal Government implemented a program in the mid 1980's in an effort to lower farm commodity inventories. "The PIK Program" (Payment in Kind) was designed to pay farmers to reduce their planting acreage, which would reduce production and lower inventories. This program did help the farming community, but did nothing for the industries supporting farmers. Farmers reduced their production and purchased less equipment, chemicals and fertilizers. This legislation was devastating for the industries that supported farming, and put some companies out of business.

The potash industry suffered during this time. In Carlsbad, several mines were forced to take extended outages due to high inventory levels, which resulted in employees having to be furloughed for several months. This started the decline of the potash industry in Carlsbad.

Another big factor in the decline of the potash industry occurred when the Canadian Potash Industry started aggressively pricing their products. The Carlsbad Potash Industry felt the Canadian's behaved predatorily trying to drive them out of business by selling potash under their cost of production.

The potash industry was struggling due to low prices, which was largely due to low priced potash imports coming from Canada. In an effort to save the Carlsbad Potash Industry, community leaders formed a grass roots committee to lobby elected officials and the Justice Department to investigate Canadian trading practices in potash sales. In due course, the investigation was conducted but before a final ruling was made, the Canadian Potash Industry agreed to a self imposed quota system for exports to the United States.

Ultimately, these sales practices also damaged the Canadian Potash Industry, which lead to the privatization of the potash industry in Canada. In 1987, the Canadian Potash Industry signed a five year trade agreement with the United States Government

that limited the amount of potash imported into the United States. "The Antidumping Agreement" allowed for a resurgence of the potash industry in the late 1980's.

This action was a shining moment for the Carlsbad community. In addition, it was the catalyst that allowed Mississippi Chemical Corp. to reopen their mining facility that had been shutdown for five years.

Potash prices remained stable until the Potacam mine, in New Brunswick, was flooded in the mid 1990's. Due to the closure of this mine, there was a shortage of granular potash. This shortage resulted in an increase of potash prices for a two year period. The Carlsbad industry did well during this time. However, the Canadian industry was able to make-up the shortfall in granular production and potash prices once again started to drop.

During the late 1990's, and early 2000, farm commodity prices dropped to very low levels. This occurred even with the fall of inventories in world commodity stocks. From 1999 through 2003, the world consumed more grain than it produced. In early 2004, farm commodity prices climbed very quickly, which resulted in increased planting and fertilizer use world wide. However, there is no way of predicting how long this trend will last. Therefore, we feel that the potash industry is still in grave danger.

Potash Royalty Rates

The royalty rate originally listed on our potash leases was set at 5% of net sales.

However, in 1979 the Bureau of Land Management changed our royalty rate to a sliding scale method. This method set a variable royalty rate that was tied to the ore grade. At a 10% ore grade a 2% royalty was paid, which climbed to 5% at a 16.5% ore grade. The Bureau of Land Management implemented the sliding scale method due to the natural deterioration of ore grades that occurs in mature mining areas.

In the mid 1980's, the royalty rate was reduced to 2% across the board due to the poor condition of the potash industry. In addition, the 2% royalty rate was renewed every two years. Then in 2000, the Bureau of Land Management decided to reinstate the sliding scale method because better potash prices were received for a brief period of time in the late 1990's.

In 2000, Mississippi Potash, Inc. and IMC Global decided to litigate the Bureau of Land Management's decision to increase royalty rates. Eventually, the rate increase

was reversed by the Bureau of Land Management and the royalty rate was returned to 2% in 2003.

October 5, 2001, Mississippi Potash, Inc. applied for a royalty rate reduction due to a continued weak potash market, which started in 1999, and the dramatic increase in production costs due to the steep rise in natural gas prices. During this time, Mississippi Potash, Inc. and Intrepid Potash New Mexico LLC have been working closely with Bureau of Land Management officials in an effort to receive a reduced royalty rate. Recently, the State Bureau of Land Management office informed Intrepid Potash that our request had been forwarded, with a positive recommendation, to the Federal Bureau of Land Management office for a final decision.