MINUTES

Assembly

TAXATION COMMITTEE
FEBRUARY 13, 1975
9:30

Members Present: Chairman May
Mr. Bennett
Mr. Christensen
Mr. Demers
Mr. Harmon
Mr. Murphy
Mrs. Ford
Mr. Young

Members Absent: Mr. Mann

Guests Present: C. E. Pollock, Virginia City Crier
R. W. DeLaMare, Carson City
J. Obester, Virginia City
Ken Martin
Ralph Anctil, Reno
Ryall Bowker
Nicholia Bowker
James D. Salo, Dep. Attorney General
M. K. Blomdal, Nevada Tax Commission
J. M. Reynolds, Advisory Mining Board
M. Douglas Miller, Chairman, Advisory Mining Bd.
M. B. Byrne, Clark County Assessors Office
Bob Alkire, Nevada Mining Association, Ely
F. W. Lewis
Assemblyman Joe Dini, District 38
Leslie Gray, Attorney
Carl Soderblom

The meeting was called to order at 9:35 by Chairman May. Chairman May explained for the benefit of the audience that Assembly Bills 62 and 198 concerned the same aspects in regards to defining royalties in mining claims. Since testimony for a particular bill would be difficult to separate because of the closeness of subject matter, Chairman May said that both bills would be discussed simultaneously..

Mr. James Salo, Deputy Attorney General assigned to the Nevada Tax Commission was the first to testify in favor of A. B. 62. He explained that A. B. 62 was drafted for the Nevada Tax Commission at their request. According to Mr. Salo, this bill is an attempt to put into law what the present interpretation by the Attorney General is, as used now by the Tax Commission. He cited Attorney General Opinion(AGO) 264, December 13, 1961 and AGO 49, April 25, 1951.(Attachments 1 and 2).

He said there is a problem in this area because there is no real definition of "royalty" in the law, only what the Attorney General has decided to interpret it as. He continued that no matter which bill, A. B. 62 or A. B. 198, is adopted there has to be a legal definition made. Mr. Salo did point out that there were two places where the determination for tax obligation could begin and that they were when active exploration begins or when actual production begins.
Mr. Demers asked Mr. Salo if the Tax Commission is attempting to tax the mines prior to their production, and if so, is it constitutional?
He was answered that he believes it is constitutional and that Montana has a similar law requiring this tax payment. He also stated that the Attorney General has ruled that taxing of some property before actual production starts is alright and that is what we are doing.

The next speaker was Assemblyman Joe Dini, "Go back to the constitution to work on the definition of proceeds. According to Article X section 1, the proceeds alone of which shall be assessed at...." Mr. Dini continued by saying that the Attorney General's Opinions that have been used by the Tax Commission (Attachments 1 & 2) were on the basis of the Minnesota constitution and therefore not applicable to Nevada. He summed up his statement by saying that only proceeds from the mines were taxable and that with the passage of A. B. 62 we would be trying to tax things other than proceeds and it would be unconstitutional. He submitted a letter from Mr. Leroy R. Bergstrom, a certified public accountant, who had written to Mr. Dini citing his concerns about A. B. 62. The letter included a copy of language that Mr. Bergstrom thought would be suitable for the definition of royaltY. It excludes rental payments and purchase payments of a mine. (Attachment 3)

Mr. Frank Lewis of the Nevada Small Mines and Prospectors Association was the next to speak. He explained that A. B. 62 tried to tax not net income but gross income. He submitted to the committee a net proceeds of mines royalty paid report. (Attachment 4) Mr. Lewis also submitted a copy of a brief by the Nevada Miners and Prospectors Association in opposition to the taxation of rent received by lessors of mining claims under the net proceeds of mines act. The cover page and opening statement and summary are enclosed as (Attachment 5). The entire brief is in the secretary's minute book, if anyone wishes to view the completed brief. Mr. Lewis said that his

association is in favor of passage of A. B. 198 with one change in the wording. He advocates the addition of the word "production" after the word "the" and before the word "proceeds" in line five of the bill. He also stated that they were totally opposed to the definition of royalty in A. B. 62.

MR. DEMERS WAS EXCUSED AT THIS POINT.

Mr. Leslie Gray was the next speaker. His submitted statement in the form of a letter to Chairman May is included as (Attachment 6). He also advocated the use of the language chosen by Mr. Bergstrom in his letter to Mr. Dini (Attachment 3).

Mr. Ryall Bowker testified next. He wanted to explain to the committee the difference between net proceeds and simple exploration. He said that when you look at the property to see whether it should be mined, that is exploration. When you start taking things from the mine, that is when the proceeds begin. He, too, felt the need for a legal definition.

Mr. M. Douglas Miller, Chairman of the Advisory Mining Board spoke next. He cited NRS. 513.000, the objects of the advisory board, as his reason for testifying. It is the mining board's duty to suggest legislation that will further the mining industry in the state. Their suggestion at the present time is that for the past ten years rental mines have been taxed and that the AGOs are in error. He says that double taxation on mines is unfair to the industry. He cited the Boston Tea Party as an example of what double taxation can lead to. He also wants the word "production" added to A. B. 198 in line 5.
Mrs. Ford asked at what point do you quit calling it exploration and start calling it production. She was answered that production actually begins at the first sale of the ore. When money is received from the sale of that ore, that is when production actually begins.

Mr. Ron DeLaMare then testified that he, too, was opposed to A. B. 62.

Mr. Carl Soderblom then testified that he wanted the addition of the word "production" added to A. B. 198 in line 5.

Mr. Bob Alkire, of the Nevada Mining Association, said that A. B. 62 was detremental to the small miners.

MRS. FORD WAS EXCUSED AT THIS POINT.

Mr. C. E. Pollock, from the Western Mining Council and also the Virginia City Crier, stated that taxes on rentals of mines are unfair unless the tax is over all kinds of property.

Mr. Bob Warren, Nevada League of Cities, testified that mines represent a large part of the income to many of Nevada's towns and counties. He cited Gabbs, Elko, Yerington, and Fernley as examples. He said that A. B. 62 could possibly take away from the income of some of these cities and counties, because it might make the small miner have to give up some of his claims and that would make some of the large mining companies not come to mine the small mining sites. His reason was that when a small miner works his claims he knows every inch of his land and just what is there. If he has to leave or is not able to work his claim, the big companies will come in and say that there is nothing in the ground because the small miner, who has already left, did not work it. Small miners who have been on the sites of their mines for years know their land a lot more than some geologists that come in from the major companies and test the ground for a day.

Mr. Jim Lien of the Nevada Tax Commission then testified that the staff of the Nevada Tax Commission has no objections to the use of the definition of royalty payment as defined in A. B. 198 but that there were other elements in A. B. 62 that he felt should not be left out.

Chairman May appointed a subcommittee of Mr. Christensen, as chairman, Mr. Bennett and Mr. Young to put together an acceptable compromise between A. B. 62 and A. B. 198. The minutes of that subcommittee meeting are included as (Attachment 7).

With no further business, Chairman May adjourned the meeting at 10:43.

Respectfully submitted,

Kim Morgan

Kim Morgan
Assembly Attache

ASSEMBLY

AGENDA FOR COMMITTEE ON TAXATION

Date February 13, 1975 Time 9:30 Room 316

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Bills or Resolutions to be considered	Subject	Counsel requested*
A.B. 62	Adds definitions and revises procedures and penalties relating to taxation of mines	
A.B. 198	Defines "royalty payment" as used in provisions relating to taxation of mines.	

*Please do not ask for counsel unless necessary.

(Attachment 7)

MINUTES OF SUBCOMMITTEE

TAXATION COMMITTEE
February 13, 1975
3:00

MEMBERS PRESENT: Mr. Christensen
Mr. Young

MEMBERS ABSENT: Mr. Bennett

Chairman Christensen explained that this was a subcommittee appointed by Mr. May, chairman of the Assembly Taxation Committee, to work out the differences of A. B. 62 and A. B. 198.

Mr. Jim Lien, of the Nevada Tax Commission, said that the Tax Commission staff was willing to accept the wording of the definition of royalty payment in A. B. 198. He added that there are also a few other aspects in A. B. 62 that needed included. He explained the need for section 3. He cited that from January, 1973 to December, 1974 the Tax Commission recovered $143,000 from out of state audits at a cost of $2,554. He then turned to Mr. Bill Liebel of the Nevada Tax Commission who explained why it is really necessary to go to out of state offices to do audits of the net proceeds of mines. He said that many large companies who own mines in Nevada keep their records in computer banks at their main offices across the nation. Usually the company does not want to let the mine superentendents know more than is absolutely necessary and therefore they do not give him the fiscal records.
Mr. Lien continued by saying that the Tax Commission already has a small allownace built into its own budget for out of state audits, but if the out of state companies paid for the expenses of the audit itself then the Tax Commission could audit more big companies and bring back more tax money that it recovered. He added that it is the privelege of the out of state company to keep its records out of state but that they should pay the cost of the audit.
Mr. Lien then explained the need for section 4 of A. B. 62. He said that this was a recommendation by the Governor's Tax Equity Study and from the Tax Commission itself. He explained that with the adoption of the royalty language of A. B. 198, section 4 of A. B. 62 would give a necessary tax break to the small miners as well as the large miners by lessening the failure to file tax penalty. He also stated that there will be no essential fiscal impact to the new penalty.

The members of the audience all agreed to the acceptance of the language of A. B. 198 and then to the two other sections of A. B. 62 .
Mr. Christensen said he would put the two sections together as an amendment to A. B. 198 and submit it to the Taxation Committee as the subcommittee's recommendation.

Respectfully submitted,

Kim Morgan

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264 **Nevada Tax Commission; Net Proceeds of Mines Tax (Chapter 362 of NRS construed)—Held: Payments denominated "royalties" in a lease-option-to-purchase agreement, and paid to the lessor (or his assignee) of nonoperated mining properties, but applicable to the purchase price upon exercise of the option, constitute a deductible item to the lessee under the provisions of NRS 362.120, subparagraph 2(k), but is taxable to the lessor (or assignee) receiving payment of such "royalties." "Royalties" defined as including any payment for the privilege of mining and removing ore, whether any mining does or does not take place, and the State is not concerned as to who, as between the lessor (or his assignee) and the lessee, is contractually liable for payment of the tax. Minimum annual payments of "royalties," by a lessee, in such circumstances, are deemed advance royalty payments in lieu of minimum output or production of the mining property involved, which, for whatever reason, may, in fact, never be effected by the lessee. Claim for refund of taxes paid under protest by lessor's assignee held, therefore, to be without merit, and should be denied. (Accord: Attorney General Opinion letters dated September 30, 1937, March 3, 1945, and June 4, 1945; also Attorney General Opinion No. 49, dated April 25, 1951.)**

CARSON CITY, December 13, 1961.

MR. R. E. CAHILL, *Secretary, Nevada Tax Commission, Carson City, Nevada.*

STATEMENT OF FACTS

DEAR MR. CAHILL: It appears that the Columbia Iron Mining Company is the assignee of a lease between Mineral Materials Company, lessee, and Nevada Iron Ore Company, Inc., lessor, relative to certain mineral properties located in Pershing and Churchill Counties, Nevada. Pursuant to said lease, the lessee is required to pay annually to the lessor the sum of $4,000 as a minimum royalty which, upon exercise of a purchase option (also contained in the lease) shall be applicable in reduction of the purchase of the properties, fixed in the amount of $40,000.

The taxpayer-assignee of the lease contends that there is no provision in the lease agreement for application of the $4,000 annual payments against the value of the production or output of the involved mining properties for the term of the lease, and submits that, in fact, there has been no production whatsoever, or extraction of any ore tonnage, at least for the year in which the questioned tax has been imposed; and that the annual payments should be strictly construed to relate to the purchase price solely, insofar as the lessee seeks to benefit therefrom. In other words, that said annual payments, though denominated "royalties" are not tax-deductible to the *lessee* under the provisions of NRS 362.120, subparagraph 2(k).

The assignee and protesting taxpayer, in this connection, invite our attention to the provisions of NRS 362.100, 362.110, 362.190 and 362.230 as authority for the proposition that the jurisdiction and power of the Nevada Tax Commission to levy and exact a net proceeds of mines tax presupposes an "operating" mine, and that where a mine is not in actual operation and, therefore, unproductive, no proper basis for any such tax exists; in short, the $4,000 annual payments, it is alleged, are merely "minimum amounts paid as required by the lease and not "royalties" in actual fact, albeit so denominated in the lease.

Columbia Iron Mining Company, having paid its taxes under protest now demands refund thereof.

QUESTIONS

1. Are payments denominated "royalties" which are paid by a lessee to a lessor of nonoperated mining property (or his assignee) and which are applicable to the purchase price thereof in the event of an exercise of an option to purchase, also contained in the lease agreement, a deductible item under applicable law relating to the net proceeds of mines tax?

2. If the answer to the foregoing question is in the affirmative, are such "royalties" taxable to the lessor-optionor, or his assignee?

CONCLUSIONS

Question No. 1: Yes.
Question No. 2: Yes.

ANALYSIS

As here pertinent, NRS 362.120 (Computation of gross yield and net proceeds: Deductions) provides as follows:

> 1. The Nevada tax commission shall, from the statement and from all obtainable data, evidence and reports, compute in dollars and cents the gross yield and net proceeds of each semiannual period.
>
> 2. The net proceeds shall be ascertained and determined by subtracting from the gross yield the following deductions for costs incurred during such 6-month period, and none other:
>
> * * *
>
> (k) All moneys paid as royalties by a lessee or sublessee of a mine, or by both, shall constitute a deductible item for such lessee or sublessee in determining the net proceeds of such lessee or sublessee or both; but the royalties so deducted by the lessee or sublessee shall constitute part of the gross yield of the mine for the purpose of determining the net proceeds upon which a tax shall be levied against the person, corporation, association or partnership to which the royalty has been paid.
>
> * * *

On the basis of the facts presented to us, and hereinbefore set forth, the Nevada Tax Commission has scrupulously applied existing law consistently with the above provision. The Commission is not concerned with the question as to who shall pay the tax; this is a matter of contract solely, as between the lessor (or, in the instant case, his or its assignee) and the lessee.

The interest of the lessee in said mining properties is based upon contract. At the time of execution of the contract, it was assumed that the lessee would enter upon the mining claims and begin active mining operations thereon. For such mining privilege, the lessee was required

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to make a *minimum* annual payment, apparently in the said sum of $4,000, which would be applied to the total purchase price of the involved properties, represented to have been fixed in the amount of $40,000. Whether or not the lessee (optionee) intends to exercise the option to purchase is conjectural; certainly, the lessee's intention in such respect is not presently known and will not be known until long after payments of annual royalties are, in fact, made. If the ultimate purchase of the involved properties is in fact not made through exercise of the option contained in the lease agreement, then the royalties constitute compensation to the lessor (here, the assignee) for the exclusive *privilege* of mining and removing mineral-bearing ores from the involved properties.

It is to be noted that the provided annual payments of $4,000 were *minimum*; that the contract further provides for payment of an additional 25 cents royalty per long ton for all iron ore extracted and removed, which additional payment would be credited to the *minimum* annual payment; and that "[A]ny and all payments made by the Lessee to the Lessor up to the time of the exercise by the Lessee of the Option . . . shall apply upon and form a part of the purchase price hereinabove mentioned."

In view of such understanding and contractual agreement between the parties, we are compelled to the conclusion that the minimum annual payments must be deemed advance royalty payments in lieu of minimum output or production. This circumstance brings the matter within the rule laid down in State ex rel. Susquehanna Ore Co. v. Bjornson, 194 Minn. 649, 259 N.W. 392, wherein the Court held as follows:

"Royalty" is a share of the product of a mine reserved to the owner, *or the payment made him, for the privilege of mining and removing ore, the compensation paid for that privilege,* and is rent and not the purchase price of ore in place, *and if the grant of the privilege of mining and taking the ore from the land is the consideration for the payments, they are "royalties."* (Emphasis supplied.)

See also State ex rel. Susquehanna v. Bjornson 262 N.W. 574; State ex rel. Inter-State Iron Co. v. Wallace 264 N.W. 774; State ex rel. Burnquist v. Commissioner of Taxation, 295 N.W. 653.

We conclude, therefore, that imposition and collection of the net proceeds of mine tax was proper and valid in the described circumstances, and that the demand for refund must be rejected. (Accord: Letter Opinions from this office dated September 30, 1937, March 3, 1945, June 4, 1945; Attorney General Opinion No. 49, dated April 25, 1951.)

Respectfully submitted,

ROGER D. FOLEY, *Attorney General.*

By JOHN A. PORTER, *Chief Deputy Attorney General.*

49. Interpretation of Mining Lease and Option for the Purpose of Determining Payments To Be Considered as Royalties.

CARSON CITY, April 25, 1951.

NEVADA TAX COMMISSION, *Carson City, Nevada.*

Attention: R. E. Cahill, Secretary.

GENTLEMEN: This will acknowledge receipt of your recent letter in which you have enclosed a copy of a lease and option agreement with the request that we interpret the said agreement for the purpose of determining the taxable status of the amounts paid to the lessor pursuant to section 8 of this agreement. Section 8 of the agreement provides in part as follows:

> In consideration of the foregoing premises and the payment of the sum of One Dollar ($1.00), paid by Lessees to the Lessor, the receipt whereof is hereby acknowledged, the said Lessor does hereby give and grant to said Lessees the exclusive right and option to purchase from said Lessor the whole of those certain mining claims, premises and appurtenances, as in the foregoing lease set forth, for the full purchase price of fifty thousand dollars ($50,000.00) payable by the Lessees to the Lessor as follows:
>
> One Thousand Dollars ($1,000.00) down, the receipt whereof is hereby acknowledged by Lessor; and the balance in monthly payments of not less than $200.00 per month beginning June 15th, 1950, and a like and similar payment on or before the 15th day of each and every calendar month thereafter, however, it is understood and agreed that the purchase price of said premises in full shall be paid by Lessees to the Lessor on or before April 30th, 1955, the termination date of the lease hereinbefore set forth.
>
> The payment of $200.00 per month as herein provided shall be interpreted to be and designated as advance and guaranteed monthly royalties.
>
> All royalty payments paid by Lessees to the Lessor either in cash as herein set forth or upon production as in the lease agreement set forth shall be credited upon the purchase price and each installment thereof as herein provided.
>
> Any and all payments paid to the Lessor by the Lessee, either under the lease or the option to purchase herein, shall immediately become the property of the Lessor. All payments provided to be made herein by the Lessees to the Lessor shall be paid direct to the Lessor at c/o Box 1062, Elko, Nevada, until the Lessor shall have received the sum of $5,000.00 upon the purchase price and thereafter to the Escrow Holder hereinafter named.

Section 5 of this agreement provides as follows:

> To pay to Lessor a royalty of not less than ten percent (10%) of the gross mill or smelter returns on each and every ton of ore taken, treated or extracted from said property, which said royalty shall be paid to the Lessor direct from the mill or smelter effecting treatment thereof upon instructions given to said mill or smelter by the parties hereto and pursuant to this lease and option agreement, and said Lessor shall be entitled to and shall receive a copy of the mill or smelter returns on each and every shipment of ore made from said premises. In connection with the shipment of ore to the mill or smelter aforesaid, it is understood and agreed that Lessor shall bear and pay one-half (½) of all freight

charges of shipments via railroad, but none of the expense of shipment by truck from the mining premises to a railroad, however, in the event that shipments of ore are made direct from the premises to the mill or smelter via truck the said Lessor shall bear and pay one-half (½) of said trucking charges. Such freight charges to be paid by Lessor shall be deducted from the gross royalty to be paid him by the mill or smelter and as provided for herein.

In order to determine the meaning of any particular section it is essential that the entire agreement be read together and one section construed in the light of others dealing with the same particulars.

First, it is important to note that the relationship existing between the parties to an option agreement is not a vendor-vendee relationship, but that of lessor-lessee, with the lessee obtaining the privilege of becoming a purchaser—in legal effect an option. Colyer v. Lahontan Mines Company, 54 Nev. 353.

The agreement provides in section 8 for a forfeiture in the event the lessee in any way defaults, consequently the $200 monthly payments would be nothing more than rent. There are numerous cases that stand for the proposition that rent and royalties are synonymous. Barnard v. Jamison, 177 Pac. 351; McIntires Admin'r v. Bond, 13 S.W.(2) 772; 64 A.L.R. 630.

The $200 monthly payments are to be paid to the lessor in cash or upon production and the parties have expressly designated the said payments as advance and guaranteed royalties, which is some assistance in ascertaining intent of the parties at the time the agreement was executed.

With the above in view, we are of the opinion that the $200 monthly payments from the lessee to the lessor are royalties and taxable to the lessor under the applicable statutes.

In our opinion the $1,000 down payment, which receipt has been acknowledged by the lessor, to be applied on the purchase price is not to be considered as a royalty payment, as it would not be considered as rent but merely as a bonus or part payment of the total purchase price. This $1,000 in reality has nothing whatsoever to do with the actual mining of the property in question, therefore, it is not taxable to the lessor.

Respectfully submitted,

W. T. MATHEWS, *Attorney General.*

By ROBERT L. MCDONALD, *Deputy Attorney General.*

(Attachment 3)

(3)

KAFOURY, ARMSTRONG, TURNER & CO.
A PROFESSIONAL CORPORATION
CERTIFIED PUBLIC ACCOUNTANTS

100 CALIFORNIA AVENUE
RENO, NEVADA 89502
TELEPHONE (702) 322-9471

February 3, 1975

Honorable Joe Dini
Nevada Legislature
Carson City, Nevada 89701

Dear Joe:

My partners and I have had occasion to review AB 62 which seeks, in part, to codify current Tax Commission practices in the Net Proceeds area. I understand from Jim Lien that you are considering proposing amendments to this bill.

The definition of royalty proposed appears to us to be oversimplified. We understand the objective of the law to be a tax on the proceeds of production. If that is correct, we strongly believe that delay rentals not applicable to royalties arising on future production should be excluded from the definition. We enclose a copy of language we believe will clarify this area.

Second, we find the concept of differential taxation of operators maintaining their records out of the State of Nevada to be a dangerous and unreasonable practice. It would afford a precedent which could logically be extended to all other forms of taxation involving interstate or international business operating in Nevada. While we recognize that the out-of-state audit costs are not described as an additional tax - that's most certainly what they amount to.

We have also expressed our concern to the Nevada Mining Association. We would be pleased to discuss with you or the Taxation Committee our reasons for objection to the bill as originally proposed, and would, of course, be pleased to discuss any amendments contemplated.

With best regards.

Very truly yours,

Leroy R. Bergstrom

LRB:ks
Enclosure

3. "Royalty" or "royalty payment" means a payment received for a right to minerals in place that entitles the owner to a specified fraction, in kind or value, of the total production from the property, free of the expense of development and operation and includes without limitation advance royalty payments or bonuses which are recoupable by the payor from the proceeds of production. The term "royalties" does not apply to delay rental payments which are carrying charges on nonproductive property where they are made for the privilege, during the primary period of the lease, of deferring development of the property, nor to payments directly applicable to the purchase of a mine.

(Attachment 4)

NEVADA TAX COMMISSION
NET PROCEEDS OF MINES
NEVADA REVISED STATUTES 362.120(3)
ROYALTY PAID REPORT

Following is a statement of Royalties Paid on lease of mine or mining claims:

Located in _____ County, for the Six-Months Period Ending _____, 19 ___

Name _____ _____
Lessee Street or Box No.

_____ _____
Name of Mine or Claim City State Zip Code

+Royalties Paid to each: - Name, full address (including zip code) and amount paid (Attach additional sheets if necessary).

_____ $_____

_____ $_____

_____ $_____

_____ $_____

_____ $_____

_____ $_____

_____ $_____

Total. . . . . $_____

+"Royalties" defined as including any payment for the privilege of mining and removing ore, whether or not any mining takes place. (Ref: A.G.O. #264, Dec. 13, 1961). Royalties, rents, lease and installment payments, etc., are synonymous. (Ref. A.G.O. #49, Apr. 25, 1951).

I hereby certify to the best of my knowledge and belief that the foregoing is a full and true statement of royalties paid for the six-months period above indicated.

_____
Name and Title

_____
Name of Company

_____
Date

THIS FORM TO BE FILED IN DUPLICATE

NPM - 10

(Attachment 5)

(1)

TO THE HONORABLE JULIAN C. SMITH

DEPUTY ATTORNEY GENERAL, STATE OF NEVADA

BRIEF OF NEVADA MINERS AND PROSPECTORS ASSOCIATION IN OPPOSITION TO THE TAXATION OF RENT RECEIVED BY LESSORS OF MINING CLAIMS UNDER THE NET PROCEEDS OF MINES ACT

OPENING STATEMENT AND SUMMARY OF ARGUMENT

The Nevada Tax Commission now taxes, as proceeds of mines, payments made to lessors of mining properties for the right of exploration granted to the lessees. The parties, in executing a lease, contemplate the eventual mining of the claim and the marketing of ores produced.

We do not contest the taxation of the proceeds once mining operations begin and ore is removed from the mine; however, we are opposed to the taxation of payments received by the lessor while the operations are in the exploratory stages and before actual production takes place.

It is our contention that the Nevada Constitution and statutes enacted pursuant thereto permit only the taxation of "proceeds" of mines which term does not include payments received by the lessor prior to the extraction of mineral substances from the earth. "Proceeds" of mines, under Nevada law, refers only to "the value of the ore delivered at the mouth of the mine."

In taxing the payments made to lessors the Tax Commission relies on Attorney General Opinions 49, April 25, 1951, and 264, December 13, 1961. It is our position that these two opinions were erroneously decided and are based on the law of Minnesota, which has a tax structure completely foreign to

Nevada's. We urge the adoption of the methods followed by the State of Montana, which has a system of taxing "net proceeds" and "royalties" identical to our own, but which does not include "rent" in its definition of "royalty."

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Argument

TABLE OF AUTHORITIES

Cases

Constitutional Provisions

Other Authorities

I

ATTORNEY GENERAL OPINIONS 49 AND 264, WHICH HAVE DIRECTED THE TAX COMMISSION TO TAX RENT RECEIVED BY LESSORS OF MINING CLAIMS, ARE NOT SUPPORTED BY AUTHORITY AND SHOULD BE DISCARDED AS ERRONEOUSLY DECIDED.

During the early 1950's the Nevada Tax Commission began taxing, as "proceeds of mines", payments made by lessees to lessors of mining claims for the privilege of exploration with a view to the eventual mining of ores. The Tax Commission justified its position by denominating the payments received "advance royalties", although they were in reality nothing more than rent, since no ores were mined and no production had taken place.

The Tax Commission relied on Attorney General Opinion 49, April 25, 1951, which had held that "rent and royalties are synonymous" and, later, on AGO 264, December 13, 1961, which held that "if the grant of the privilege of mining and taking the ore from the land is the consideration for the payments, they are 'royalties'."

AGO 49 cited two cases for the proposition that "rent and royalties are synonymous:" Barnard v. Jamison, 177 Pac 2d 341 (Cal. 1947), and McIntire's Administrator v. Bond, 13 S.W. 2d 772 (Ken. 1929), neither of which is relevant to the issue of whether rent received by lessors of mining claims may be taxed as "proceeds of mines" pursuant to Nevada law. Indeed, neither case is concerned with taxation at all.

Barnard was concerned solely with the question of whether payments received from an oil company prior to drilling under an oil lease should be divided among several lessors in the same proportion as the royalties which might be paid after actual production began. In McIntire the issue was whether several lessors were each entitled to a share of the production from an oil well after partitioning certain real property that had been leased to an oil company. Subsequent to the partition suit a well had been drilled on one of the parcels, the owner of which claimed the entire royalty to the exclusion of eight other persons who, with the owner, had formerly owned the entire leased premises as tenants in common. The court held that the royalty should be divided among all nine in the same manner as the payments received prior to the partition suit.

Neither Barnard nor McIntire was concerned with the taxation of the payments received but dealt solely with the manner of apportioning payments among several lessors. In each case the court reached an equitable solution by holding that the royalties should be apportioned in the same manner as the rent. By no stretch of the imagination do these cases support the Attorney General's opinion that "rent and royalties are synonymous."

AGO 264 cites as its authority AGO 49, supra, and the following cases from Minnesota: State ex rel. Susquehanna Ore Co. v. Bjornson, 194 Minn. 649, 259 N.W. 392 (1935); State ex rel. Inter-State Iron Co. v. Wallace, 264 N.W. 774 (Minn. 1936); and State ex rel. Burnquist v. Commissioner of Taxation, 295 N.W. 653 (Minn. 1941). Each of these cases held

that rent received by a lessor of mining claims was taxable as "royalty" payments.

The Minnesota Constitution and statutes provide for a two-step method of taxation of mines: (1) The actual production is taxed to the mine operator, as it is in Nevada; (2) Rent received by the lessor (defined as "royalty" under Minnesota law) is taxed to the lessor. The lessee-operator is also allowed a deduction for all sums paid to the lessor.

The following Constitutional provision and statutes are essential to an understanding of why the above cited cases were so decided:

The operator of the mine is taxed pursuant to the following:

> "Every person...engaged in the business of mining... shall pay to the State of Minnesota an occupation tax on the valuation of all ores produced, which tax shall be in addition to all other taxes provided by law..." Minnesota Constitution, Article 9 § 1A.

Pursuant to this constitutional authority the Minnesota Legislature has provided for the taxation of "all ores produced", which tax is paid by the operator of the mine. St. 1927 § 2373, now MSA § 298.01.

Minnesota has defined "royalty" in a unique manner and taxes the lessor of the mine pursuant to the following:

> "For all purposes of this chapter the word 'royalty' shall be construed to mean the amount in money or value of property received by any person having any right, title, or interest in or to any tract of land in this state for permission to explore, mine, take out and remove ore therefrom." St. 1927 § 2392-2, now MSA § 299.02 (emphasis added).

> "There shall be levied and collected upon all royalty received during the year ended December 31, 1923, and upon all royalty received during each year thereafter, for permission to explore, mine, take out and remove ore from land in this state, a tax of six (6) percent." Laws 1923, C 226 § 1 (emphasis added)

It is readily apparent that prior to the Minnesota decisions cited in AGO 264, Minnesota had provided by law for the taxation of ores to the operator of the mine and, in addition, the taxation of rent (defined as "royalty" in the Minnesota statutes) to the lessor of mining property irrespective of whether actual production takes place.

When the Nevada Attorney General, in AGO 264, quoted the following passage from State ex rel. Susquehanna Ore Co.,

> "Royalty is a share of the product of a mine reserved to the owner, or the payment made him, for the privilege of mining and removing ore, the compensation paid for that privilege, and is rent and not the purchase price of ore in place, and if the grant of the privilege of mining and taking the ore from the land is the consideration for the payments, they are 'royalties',"

he ignored the fact that the decision is based on the peculiarities of Minnesota law and is without validity in Nevada where there is no provision for the taxation of rent as "royalty." It does not follow that because Minnesota has provided by statute to tax rent received by a lessor of mining properties, Nevada may do the same in the absence of appropriate legislation.

Neither AGO 49 or AGO 264 is supported by authority and both should be discarded as erroneously decided. The opinions set out to explain why rent should be taxed under the Nevada provision for the taxation of royalties and fall far

short in the undertaking. The two opinions also evade the ultimate issue, which is: Whether any amounts received by lessors of mining properties can be taxed as "proceeds" of mines before actual production commences.

The Nevada Attorney General has also frequently cited Koyen v. Lincoln Mines, Inc., 63 Nev. 325, 171 P 2d 364, and, recently, New Silver Bell Mining Company v. County of Lewis and Clark, 284 P 2d 1012 (Mont. 1955), in support of its position that rent received by a lessor of a mining claim prior to the actual extraction of ores should be taxed as "royalty." It should be noted that in each cited case there was actual production of ores. Koyen involved a controversy between the lessor and lessee as to who was obligated to pay the net proceeds tax on actual production pursuant to the lease terms, and is totally irrelevant to the present issue. New Silver Bell held that the lessor's share of net smelter returns could not be credited against the purchase price prior to the exercise of the purchase option, and is also irrelevant to the question of whether rent may be taxed as "proceeds" under Nevada law.

It is our contention that the Nevada Attorney General's office has not, in the past, come to grips with the problem, but has issued opinions based on an indiscriminate reading of foreign law which has no application under the Nevada tax structure. The question of whether "proceeds" of mines includes rent received by a lessor prior to the extraction of ores from the mining claims remains unanswered.

II

NEVADA LAW LIMITS THE TAXATION OF MINES TO THE "PROCEEDS" THEREOF, WHICH TERM DOES NOT INCLUDE PAYMENTS RECEIVED BY THE LESSOR OF A MINING CLAIM PRIOR TO THE EXTRACTION OF MINERAL SUBSTANCES.

A. THE TERM "PROCEEDS" AS EMPLOYED IN ARTICLE X OF THE NEVADA CONSTITUTION REFERS ONLY TO ORES, BULLION AND MINERAL SUBSTANCES.

Section 1 of Article X, Nevada Constitution, 1864, originally provided:

> "The Legislature shall provide by law for a uniform and equal rate of assessment and taxation, and shall prescribe such regulations as shall secure a just valuation for taxation of all property, real, personal, and possessory, excepting mines and mining claims, the proceeds of which alone shall be taxed." (emphasis added).

The "Net Proceeds of Mines Act", presently NRS 362.100 et seq., was enacted pursuant to this constitutional mandate; thus the history of Article X, Section 1, is of crucial importance in ascertaining the meaning of the term "proceeds" as used in the tax law.

The first Constitution of Nevada, which emerged from the 1863 Constitutional Convention, was defeated at the polls. One of the primary reasons for its defeat was the strong opposition from the mining industry, led by William M. Stewart, Nevada's first U.S. Senator, which objected to the taxation of mines. Goldfield Consolidated Co. v. State, 35 Nev. 178, at 185; see also Bushnell, The Nevada Constitution, Third Edition, at 45, 46.

The 1864 Convention produced our present State Constitution, including Article X, Section 1, supra.

MR. DeLONG. I suggest to the gentleman from Humboldt to incorporate the word "net" in his amendment.

MR. BANKS. I prefer not to incorporate that word, if it can be avoided, for the reason that I wish to leave the question, which is a difficult one, to the Legislature.

MR. DeLONG. . . . Now let us come up squarely to our work. If we want to tax gross proceeds, let us say "gross proceeds," and if we want to tax net proceeds, let us say "net proceeds," . . . .

MR. BANKS. I would prefer very much indeed to have that question left to the decision of the Legislature. (page 223)

MR. HAINES. I had the honor of occupying a seat in the previous convention, in which this subject was discussed for six or seven days, and we then put in this provision as it now stands, in a form which seemed then, at least, to be generally satisfactory. Now, I find members here from Storey County who apparently feel called upon to give us four or five hours more of discussion, upon a subject which we have already discussed until it has become absolutely a stench in the nostrils of the people. Now, I assure you gentlemen that one thing is certain -- that unless our taxes can be made uniform and equal, we can never have a state government in Nevada. That question may as well be settled at once. If our mining property has got to go untaxed, for the benefit of the few, then you can never have a state government. (pages 223-224)

MR. HAINES. I tell you plainly that my constituents never will consent to be taxed for a state government, unless the tax shall be made uniform and equal. Your proposition to tax the net proceeds, if it went to the people, would never be heard of again on earth. I venture to say, if we were to adopt such a provision, that there would be found no net proceeds of the mines, if the state should last a thousand years. I am satisfied that my constituents would never submit to anything of the kind, and they have discussed the subject for weeks and months gone by.

MR. DeLONG. That kind of talk is not going to drive me at all, because I could, if I pleased, retort by saying that the proceedings of the previous convention to which the gentleman has referred, so stunk in the nostrils of the people, that the people voted its action down, and very harmoniously too, there being hardly a dissenting voice. (page 224)

On pages 416-417, an amendment was proposed including the proviso "provided, that in the taxation of mines, only the proceeds thereof shall be taxed." Mr. Chapin, who proposed this amendment, argued:

> I have only a very few remarks to make upon the amendment . . . .This substitute leaves it open for the Legislature to tax the bullion, if they please, or by putting the property-owners, or the owners of mines, under oath, or in any other way they see fit, to get at the correct proceeds of the mines . . . . Then we relieve entirely the prospecting miners from that taxation which we know would become so heavy a burden upon them, and which would raise up an opposition to our Constitution so powerful that it would be certain to defeat it. We relieve those miners, and at the same time destroy that opposition. . . .
>
> MR. BELDEN. Does the gentleman mean to provide for taxing the net or gross proceeds of the mines?
>
> MR. CHAPIN. The amendment leaves that to the Legislature entirely; that is my idea.
>
> MR. COLLINS. I hope this amendment will be voted down. . . . Why, sir, the first tendency will be to retard the development of our mines. . . . That will be the view taken by the capitalists, and the state will be the sufferer all the time. Then, again, if you are to tax the mines on their production, I say the fairest way will be to tax them, not on the gross proceeds, but on the net proceeds. (page 417)
>
> MR. NOURSE. . . . Now it is claimed by some, and I know other gentlemen here whose opinions are entitled to the highest respect agree with them, that the decision in regard to what constitutes the proceeds of a mine, was an inequitous one. . . . Clearly, the proceeds of a mine are nothing else than the value of the ore delivered at the mouth of the mine. If after that, by sending the ore to the mills and having it reduced, its value is increased, that increase is the product of the mill and not of the mine; if you may take the value of the bullion after this additional labor is put upon it, to purify it from everything except the clear metal, if you may add to the value of the ore as it comes from the mine, the labor and material laid out upon it at the mill, why may you not go further, and add the labor which is expended in converting it into watches, finger-rings, jewelry and everything of that description? It seems to

me that the proceeds of the mines can be, in any point of view, only the value of the ore as it is delivered at the mouth of the mine. . . . Does it make any difference, practically, whether the reduction takes place in this state or out of it? If it is sent out of the state, and if it is the property of the miner, as of course it is, is it not taxable just the same as if it were reduced in the state? (pages 515-516; emphasis added)

MR. FRIZZEL. . . . The way the language reads is, that the proceeds of the mines shall be taxed. Now what are the proceeds of the mine? That term is general and broad, and in my opinion, it embraces anything and everything that proceeds from a mine and is valuable, and you will find that the Legislature will tax everything of that kind. I ask, gentlemen, if they know not that to be the fact. Do they not know that everything which issues from or comes out of a mine, everything which emanates from it, your Legislature will tax under that clause as it stands? It may be bullion, or it may be ore; it may be ore which is sent out of the state; it may be first class ore or second or third or fourth or fifth class ore; but whatever it is, under that clause, it must be taxed. . . . Not only the bullion will be taxed, but on the same day when the assessor goes around and finds the bullion, he may also find 250 or 300 or 1,000 tons of ore which has proceeded from the mine, which is property and which has emanated from the mine, and he will certainly assess that. (page 518; emphasis added)

MR. COLLINS. Now there is too much indefinite in this word "proceeds" as it is here employed for certainly when you take from the mines the ore which exists in them, it occurs to me that those ores really constitute the proceeds of the mine, and that the milling part of the operation, which converts them into bullion, is something subsequent to the proceeds and additional thereto. (emphasis added)

The preceding discussion took place on Wednesday, July 20, 1864, on which day Article 10, containing the above-quoted language was adopted. Clearly, the framers of this section of the Constitution meant to tax only the minerals to be extracted from the mines. Although there was some disagreement as to whether "proceeds" meant "net proceeds" or "gross proceeds" there was never any suggestion that proceeds should

be construed so as to include rent in addition to the minerals themselves.

B. THE NEVADA SUPREME COURT HAS CONSTRUED "PROCEEDS OF MINES" AS USED IN ARTICLE X, NEVADA CONSTITUTION, AS SYNONYMOUS WITH "PRODUCTS OF MINES."

In the years immediately following the enactment of Section 1 of Article X, the Nevada Supreme Court had the opportunity or at least two occasions to interpret the meaning of "proceeds" as used in that section, although there are no cases discussing the issue of whether "proceeds" includes "rent", the cases are highly instructive and the meaning ascribed to the term "proceeds" is entitled to the greatest respect.

City of Virginia v. Chollar-Potosi Gold and Silver Mining Co., 2 Nev. 86 (1866) was a suit by the City of Virginia for the collection of Taxes on the proceeds of the Defendant's mines. Justice Beatty quoted Article X of the Constitution and stated:

> "The leading feature of this section is that taxation shall be equal and uniform, and that the proceeds of the mines only shall be taxed. In other words, whilst the body of the mine remains untaxed, the ore taken out (for that is the primary proceeds of the mine) shall be subject to the same ad valorem taxation as other property. The mode of assessment prescribed by the Legislature, and followed by the City Ordinance, was doubtless intended to arrive at the true value of the ore and taxed at that value." (at page 92)

In another passage from City of Virginia Justice Beatty states:

> "The /city's/ ordinance in prescribing the manner of assessing the taxes or the proceeds

> of mines follows the same course prescribed by the state legislature for assessing them for state purposes. That is in substance to ascertain the amount and yield of ores for each mine for one quarter, to deduct from the gross yield first twenty dollars per ton; then to deduct from the remainder one-fourth, or twenty-five per cent., and to assess the remaining three-fourths at the same ad valorem tax as other property. (page 88; emphasis added)

State v. Kruttschnitt, 4 Nev. 178 (1868), was an action brought by the state against a county assessor for malfeasance in office in having failed to assess the proceeds of mines in his county for certain tax periods. The court analyzes the method in which the assessment was made:

> "If the calculation was made on nearly any of the other mines, it would appear that the mode of taxation is more favorable to them than if they paid on the body of the mine. It will be seen then that the paying mines do not often pay more, generally hardly so much as other property in proportion to their real value. Whilst they are nonpaying or producing no pay ore, they entirely escape taxation." (4 Nev. at 203. emphasis added)

> "Look at this in another light. The mines pay on the products of the mine in lieu of the mine itself." (4 Nev. at 202. emphasis added)

The Nevada Supreme Court, in construing Article X in City of Virginia and Kruttschnitt makes it abundantly clear that when the term "proceeds" of mines is employed it is synonymous with "products" of mines.

C. THE NEVADA LEGISLATURE HAS GRANTED THE TAX COMMISSION THE POWER TO TAX ONLY THOSE MINES FROM WHICH ORES ARE BEING EXTRACTED, WHICH ARE REFERRED TO IN THE STATUTES AS "OPERATING MINES."

The provision of the Nevada Constitution, insofar as it provides for taxation of the proceeds of mines, is not self-executing. Goldfield Consolidated Mines Co. v. State, 60 Nev. 241, 106 P. 2d 613 (1940); Wren v. Dixon, 40 Nev. 170, 161 P. 722 (1916). Thus, it has been necessary for the Legislature to enact statutes to effectuate the constitutional provisions. This legislation is presently codified in N.R.S. 362.100 to 362.240, inclusive. Nevada Revised Statutes, including the supplementary and replacement pages, constitute all of the statute law of Nevada of a general nature enacted by the Legislature. All statutes of a general nature enacted prior to the adoption of Nevada Revised Statutes have been repealed. All sections of N.R.S. speak as of the same date, except that in cases of conflict between two or more sections, or of any ambiguity in a section, reference may be had to the Acts from which the sections are derived, for the purpose of applying the rules of construction relating to repeal or amendment by implication, or for the purpose of resolving the ambiguity. 1957 Statutes of Nevada, Chapter 2, Sections 4, 5.

N.R.S. 362.100 provides:

> The Nevada Tax Commission is hereby empowered and authorized to investigate and determine the net proceeds of all operating mines and to assess the same as provided in N.R.S. 326.100 to 362.240, inclusive. (emphasis added)

Thus, under the present state of law, the scope of the Tax Commission's power to determine and assess taxes upon mines,

as elaborated upon in the sections following Section 362.100, is limited to the assessment of the "net proceeds" of "operating mines." This interpretation of the statute is consistent with the constitutional mandate that only the "proceeds" of mines may be taxed.

In order to understand the meaning of the term "operating mine", it is crucial to examine the revenue acts from which NRS 326.100 et seq. is derived.

The Revenue Act of 1867, the first to be enacted pursuant to Article X of the Constitution provided, in applicable part:

> "...the county assessor shall ascertain by diligent inquiry and examination, the name, title, and location of all mines and mining claims in his county, from which gold and silver, or either, is extracted;...and he shall then ascertain and determine, as provided in this act, the number of tons and the value per ton of all ores...extracted for reduction from the said mines or mining claims...and shall list and assess the same to the person...extracting the ores or minerals..." (Section 101; emphasis added)

The Nevada Supreme Court, discussing the Revenue Act of 1867 in Kruttschnitt, supra, had this to say:

> "The present Revenue Law, altogether a piece of incongruous patchwork, amended at every session of the Legislature in some sections, without making other sections conform to those amended, is still clear enough, and plain enough, as to the proper manner of assessing the products of mines. The most essential things in the assessment are these:
>
> First -- The ores are to be assessed at their value when severed from the mine and deposited on the surface. Second -- All assessments are to be on a paper currency basis. Third -- The assessment is not to be made until after the ores shall have been worked and the bullion extracted,

> so far as ores are concerned, which are worked in this State. (at page 210; emphasis added)

The Revenue Act of 1867 is not referred to in the source notes to Chapter 362, NRS; however, since it was the first measure enacted pursuant to Article X of the Constitution it is, in essence, the source of all subsequent revenue acts.

The earliest revenue act referred to in the source notes in N.R.S., Chapter 362, is that of 1891, found at page 135 of the Session Laws of the 15th Session of the Nevada Legislature. The following provisions of that act are instructive upon the definition of the phrases "proceeds of mines" and "operating mine."

> Section 75. All proceeds of mines, including ores, tailings, borax, soda and mineral-bearing material of whatever character, shall be assessed for purposes of taxation....
>
> Every tax levied under the authority or provisions of this Act on the proceeds of mines, is hereby made a lien on the mines or mining claims, from which the ores or minerals bearing gold, silver or other valuable metal or material is extracted for sale or reduction;.... (emphasis added)
>
> Section 80. In case of neglect or refusal of any person...having charge of the books of mines of any person...engaged in working tailings or in extracting ores or materials for reduction or sale, to give under oath or affirmation the statement required by this Act, the assessor...shall make an estimate from the best resources within his reach, of the number of all tons or tailings, ores or minerals worked or extracted by such person...for the preceding quarter... (emphasis added)

> Section 82. The /owner/ of any mill, arastra, smelting furnace, or any process by which gold or silver or other taxable products are extracted, shall keep, or cause to be kept, an accurate account of the number of tons of ores, quartz or minerals reduced or smelted in the name of the mine or mining claim from which said ore, quartz or mineral was taken. The amount and value of the bullion or other taxable product derived by smelting or reducing from the ore, quartz or mineral from such mine or mining claim.... (emphasis added)
>
> Section 95. The District...attorneys of the several counties of this state are hereby authorized and directed...to commence action ...against the person...and against the mine or mining claims from which gold and silver-bearing ores, quartz or minerals or other taxable products were extracted and assessed, so delinquent. (emphasis added)

The Nevada Tax Commission was created by Chapter 177 of Nevada Statutes, 1917. Section 13 in part provides:

> /The/ Commission is hereby empowered to investigage and determine the net proceeds of all operating mines. In pursuance thereof, said Commission, in each instance, shall investigate and determine from all obtainable data, evidence and reports, the gross value of the bullion actually extracted from the reduction of the ores and the proceeds from the sale of the ores of any mine, mining claim or patented mine, and to deduct therefrom only such actual costs of extraction, transportation, reduction, or sale of ores as shall be deemed by said Commission to be just, proper and reasonable, and not introduced to deprive or defraud the state from any portion of its just revenue....(page 336; emphasis added)

The source notes to the various sections of N.R.S., Chapter 362, reflect that Chapter 77 of Statutes of Nevada, 1927, is also a major source of these present sections. Pertinent sections of the 1927 Act include the following:

> Section 1. The Nevada Tax Commission is hereby empowered and authorized to investigate and determine the net proceeds of all operating mines and to assess the same as in this Act provided. (emphasis added)
>
> Section 2. Every person...operating any mine containing gold, silver, copper, zinc, lead, or other valuable mineral or mineral deposit, must...file with the Nevada Tax Commission a statement showing the gross yield and claimed net proceeds from each mine owned, worked or operated by such person.... (emphasis added)
>
> Section 7. Every person...operating any mine or mines in this state who shall fail to file with the Nevada Tax Commission the statements herein provided...shall be liable to a penalty ...and if any mine operator shall so fail to file such statement, the Nevada Tax Commission may ascertain and certify the net proceeds of such mine or mines from all data and information available. (emphasis added)
>
> Section 9. The Nevada Tax Commission shall have the right and power at any time to examine the records of any person...operating any mine... (emphasis added)
>
> Section 12. Whenever the gross proceeds received by any mine operator from the operation of any mine shall be less than $20,000 for any calendar year, such operator may make the deductions provided in Section 3 of this Act upon an annual basis. (emphasis added)

Language which indicates the legislative intent that the scope of this taxing power shall be limited to operating mines is still contained in N.R.S., Sections 362.100, 362.110, 362.120, 362.150, 362.190, 362.200 and 362.230.

The most recent amendment to any of these sections was accomplished by Chapter 690, 1973 Statutes of Nevada. None of these amendments has eliminated the requirement that a mine be an operating mine before the proceeds thereof become taxable.

The various revenue acts and statutes from which NRS 362.100 et seq. are derived frequently employ the terms "operating mine" and "extraction of ores" in a manner which makes it clear that each session of the legislature felt that no mine could be taxed unless ores were being "extracted."

NRS 362.100, which grants the Tax Commission the power to assess the "net proceeds" of "operating mines", cites as its source Section 13 of Chapter 177, Nevada Statutes, 1917, supra, wherein it was provided that the Commission in pursuance of its duty to determine the "net proceeds" of "operating mines" shall determine "the gross value of the bullion actually extracted...and the proceeds from the sale of the ores..."

The conclusion that an "operating mine", as referred to in NRS 362.100, is one from which ores are "extracted" is inescapable. Thus it is strongly urged that the Nevada Tax Commission lacks the power to tax any amounts received by lessors of mining claims prior to the commencement of mining operations and the production of ores.

III

WHERE THERE IS DOUBT AS TO THE PROPER MANNER OF ASSESSING AND TAXING MINES, NEVADA SHOULD ADOPT THE DEFINITIONS AND METHODS OF OTHER WESTERN STATES WHOSE TAX STRUCTURES ARE IDENTICAL TO OUR OWN.

Prior to Attorney General Opinion 49, April 25, 1951, no tax was assessed on rent received by the lessor of a mining claim while the mine was in the exploratory stage. AGO 49 and, later, AGO 264 sought to tax these rent payments by borrowing the definition of the term "royalty" from the State of Minnesota which, as discussed earlier, has a tax structure completely foreign to Nevada's and which has, by statute, defined "royalty" in a manner unknown to the western mining states and the mining industry generally. If it is appropriate to borrow definitions from foreign jurisdictions, it is our contention that mining terminology, as used in the mining industry generally and by states whose tax structure most nearly approximates Nevada's, should be adopted to the exclusion of definitions unknown outside Minnesota.

The taxation of mines in the State of Montana is nearly identical to our own. Article XII, Section 3, of Montana's Constitution is highly similar to Nevada's Article X, Section 1, and provides:

> "All mines and mining claims, both placer and rock in place, containing or bearing gold, silver, copper, lead, coal or other valuable mineral deposits, after purchase thereof from the United States, shall be taxed at the price paid the United States therefor, unless the surface ground, or some part thereof, of such mine or claim, is used for other than mining purposes,

> and has a separate and independent value for such other purposes, in which case said surface ground, or any part thereof, so used for other than mining purposes, shall be taxed at its value for such other purposes, as provided by law; and all machinery used in mining, and all property and surface improvements upon or appurtenant to mines and mining claims which have a value separate and independent of such mines or mining claims, and the annual net proceeds of all mines and mining claims shall be taxed as provided by law."

Hence the Montana Constitution directs the mine owner to pay a small tax on the value of the claim as purchased from the United States -- not unlike Nevada's assessment of patented claims at "not less than $500.00" -- and, in addition, a tax on the "net proceeds."

Pursuant to this provision Montana enacted the following relevant statutes (all section headings are to the Revised Codes of Montana):

> 84-5401. Taxation of mines. All mines and mining claims...shall be taxed at the price paid the United States therefor...and the annual net proceeds of all mines and mining claims, shall be taxed as other personal property. Sec 3, P 73, L. 1891.

> 84-5402. Net proceeds tax -- statement of yield. Every person, partnership, corporation, or association, engaged in mining, extracting or producing from any quartz vein or lode, placer claim, dump or tailings, or other place or sources whatever, precious stones or gems, gold, silver, copper, coal, lead, petroleum, natural gas, or other valuable mineral, must on or before the thirty-first day of March of each year make out a statement of the gross yield of the above-named metals or minerals from each mine owned or worked by such person, corporation or association during the year preceding the first day of January of the year in which such statement is made, and the value thereof. Such statement shall be in the form prescribed by the state board of equalization, and must be verified by the oath of such person or the manager, superintendent, agent, president or vice-president of such corporation,

association or partnership, and must be delivered to the state board of equalization on or before the thirty-first day of March. Such statement shall show the following:

1. The name and address of the owner or lessee or operator of the mine, together with the names and addresses of any and all persons, corporations, or associations owning or claiming any royalty interest in the mineral product of such mine or the proceeds derived from the sale thereof, and the amount or amounts paid or yielded as royalty to each of such persons, corporations, or associations during the period covered by the statement.

2. The description and location of the mine.

3. The number of tons of ore, barrels of petroleum, cubic feet of natural gas or other mineral products or deposits extracted, produced, and treated or sold from the mine during the period covered by the statement. (Then follows certain other requirements comparable to NRS 362.110) Sec 1, Ch 237, L. 1921

84.5403. Net proceeds -- how computed. The state board of equalization shall calculate and compute from said returns the gross product yielded from such mine, and its gross value in dollars and cents for the year covered by the statement, and also shall calculate and compute the net proceeds in dollars and cents of said mine yielded to such person, corporation or association so engaged in mining which said net proceeds shall be ascertained and determined by subtracting from the value in dollars and cents of the gross product thereof the following, to wit:

1. All royalty paid or apportioned in cash or in kind by the person, corporation or association so engaged in mining. (Then follows a list of deductions comparable to NRS 362.120.) Sec 2, Ch 237, L. 1921

84-5406. Assessment of royalties. Upon receipt of the list or schedule setting forth the names and addresses of any and all persons, corporations and associations owning or claiming royalty, and the amount or amounts paid or yielded as royalty to such royalty owners or claimants during year for which such return is made, the state board of equalization shall proceed to the assessment of all such royalties, and shall assess the same at the full cash value of the money or product yielded during such preceding calendar year, and the same shall be taxed on the same basis as net proceeds of mines are taxed... Sec 3, Ch 188, L. 1935

> 84-5409. Taxation and payment on royalty interests. At the time of transmitting net proceeds assessments the state board of equalization shall also transmit the royalty lists or schedules to the county assessor of each county in which such mines and mining claims are located and thereupon the county assessor shall prepare from such net proceeds and royalty assessments a tax roll which shall be by him furnished to the county treasurer on or before the fifteenth day of September following, upon which date said taxes shall be due and payable. Assessments of royalty on production of metals, and minerals other than petroleum and natural gas, shall be entered by the county assessor in the personal property assessment book in the name of the recipient or owner of such royalty. The county treasurer shall proceed to give full notice thereof to such recipient or royalty owner, and to collect the taxes thereon in the same manner as taxes on net proceeds of mines. Sec 6, Ch 188, L. 1935.

Under the Montana system the lessee-operator of the mine takes a deduction for royalties paid the lessor, 85-5403, which royalties are taxed to the lessor pursuant to 84-5409. This method of taxing royalties and net proceeds is identical to Nevada's.

It is our contention that if the guidance of foreign jurisdictions is desirable, we should follow the tax pattern established in Montana, which has a system identical to our own, rather than Minnesota's.

The State of Montana does not tax rent received by the lessor prior to the extraction of ores since there is no "royalty" prior to that time. A mining "royalty" can only be generated by a producing mine. In Rist v. Toole County, 159 P 2d 340 (Mont. 1945), the court stated:

> This court long ago adopted the standard and universal definition of royalty. In Hinerman v. Baldwin, 67 Mont. 417, 215 P. 1103, 1108, it said: "The word has a very well understood and definite meaning in mining and oil operations. As thus used, it means a share of the produce or profit paid to the owner of the property. (at page 342; emphasis added)

In Homestake Exploration Corporation v. Schoregge, 264 P. 388 (1928), the Montana Supreme Court stated, at page 392:

> The word "royalty" has a definite and well understood meaning in mining and oil operations. It means a share of the product or profit paid to the owner of the property. (emphasis added -- See also Hinerman v. Baldwin, 67 Mont. 417,215 P 1103; Indiana Natural Gas & Oil Co. v. Stewart, 45 Ind. app. 554, 90 N.E. 384).

Obviously, prior to the extraction of ores there can be no "product" or "profit"; consequently, Montana has never taxed rent received by a lessor while the mine is in the exploratory stage.

In conclusion we would like to emphasize that the assessment and taxation of rent prior to the commencement of actual mining production was not intended by the 1864 Constitutional Delegates, or by the Nevada Supreme Court or the Nevada Legislature since that date. In 1864 the mining industry was in its infancy and it was generally felt that no taxes should be imposed until the mines were producing -- any other course of action would have greatly inhibited the development of an industry vital to the state's economy.

We do not feel that situations have changed -- to the contrary, at a time when our natural resources are being consumed at an alarming rate it is even more crucial today than in 1864 to permit the unobstructed development of the mining industry. It is our belief that a fully developed and producing mine will generate far more in revenue and will contribute

significantly more to the state's economy than the relatively small amount of revenue raised by taxing lessors of undeveloped mining claims.

Respectfully submitted,

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(Attachment 6)

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Paul W. May, Chairman
Assembly Taxation Committee
Legislative Building
Carson City, Nevada 89701

Dear Mr. May:

The history of the establishment and operation of the "in lieu" tax on the proceeds of mines is one of the thrilling episodes in the story of Nevada. William Morris Stewart in addition to writing the mining regulations in California and Nevada and later the Mining Law of the United States, conceived this just and equitable theory of taxation of mines which was and is so vital and important to their discovery and development.

Dr. Miller's recent discovery of the Marsh-Clemens-Bowman notes of the 1863 Constitutional Convention gives us the lucid and clear expositions of Stewart and his protagonist, John Wesley North. Succinctly stated, North wanted to tax the mines just like any other property because it was not the "poor miner" who was going to pay the tax, it was the big owner and frequently an absentee owner at that. Stewart's valid position was that there was no way on earth to equitably tax the labor and the expenditure based on sanguine hope.

Stewart was not successful and promptly closed his office and went out and defeated the 1863 Constitution; the next Constitution was readily passed in 1864 and the provision is as follows:

ARTICLE X
Taxation

"Section 1. The Legislature shall provide by law for a uniform and equal rate of assessment and taxation, and shall prescribe such regulations as shall secure a just valuation for taxation of

> all property, real, personal and possessory, except mines and mining claims, when not patented, the proceeds alone of which shall be assessed at not less than five hundred dollars ($500), except where one hundred dollars ($100) in labor has been actually performed on such patented mine during the year, in addition to the tax upon the net proceeds..."

Thus, under the Constitution the proceeds alone are taxable and it was left to the Legislature to determine how those proceeds should be arrived at, whether gross, adjusted gross or net and, of course, as we know the Legislature has arrived at a net proceeds tax which takes into consideration certain deductions.

Over the years various Governors and their tax commissions have rumbled about the mining companies getting away with murder and have tried various devices to enlarge the tax and on occasion have even violated the law and the Constitution.

Those of us who have specialized in mining matters have periodically had to negotiate fair settlements with the Tax Commission. Frankly, up until recently the prevalent strategy has been to keep the subject under cover so to speak, out of the courts and particularly out of the Legislature. For example, as I recall, I have only had to go to court once for U. S. Gypsum and I am happy to report that I won that case.

Since the early 1950s, relying on two Attorney Generals' opinions, #49 April 25, 1951 and #264 December 31, 1961, the Tax Commission has taxed rent payments indiscriminately whether the mines are in operation or not. In other words, the Attorney General concluded on the basis of some California, Kentucky and Minnesota cases that rent and royalty are synonymous.

There is a case pending on this question and I think the taxing policy based on the Attorney Generals' opinions will be held to be unconstitutional. However, I strongly feel that the case could be made moot if this Legislature would clarify the net proceeds law as we suggest.

The most serious attempt by the Tax Commission to violate the Constitution and flout the law came in 1972 according to my experience. The Tax Commission started assessing clients of mine even for sales contracts of mining property where the mine was not in operation. We refused to pay the assessment, demanded a hearing before the Tax Commission and then the 1973 Session came along. The Tax Commission got A.B. 642 introduced; most of you well remember it. It went sailing through and I caught it in the Senate and it was sent back to you and it was properly amended. Then the Tax Commission backed off, voided our assessment and eliminated the necessity for a hearing. But, they passed some regulations which were potentially troublesome.

Now they are back with A.B. 62 which again is unconstitutional and attempts to include as proceeds everything except a straight purchase without regard to whether the proceeds are from a mine in operation.

Further, there is a provision for out-of-state mining companies to pay for their audits.

A.B. 62 should be rejected and new clear definitions should be enacted. Attached hereto is a definition which comes from a firm of Certified Public Accountants.

The audit requirements it seems to me could be made consistent and simple. One answer would be to require every company operating in Nevada to maintain books and records within the State so that they will be available for audit on notice.

Respectfully submitted,

Leslie B. Gray

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"3. 'Royalty' of 'royalty payment' means a payment received for a right to minerals in place that entitles the owner to a specified fraction, in kind or value, of the total production from the property, free of the expense of development and operation and includes without limitation advance royalty payments or bonuses which are recoupable by the payor from the proceeds of production. The term 'royalties' does not apply to delay rental payments which are carrying charges on nonproductive property where they are made for the privilege, during the primary period of the lease, of deferring development of the property, nor to payments directly applicable to the purchase of a mine."