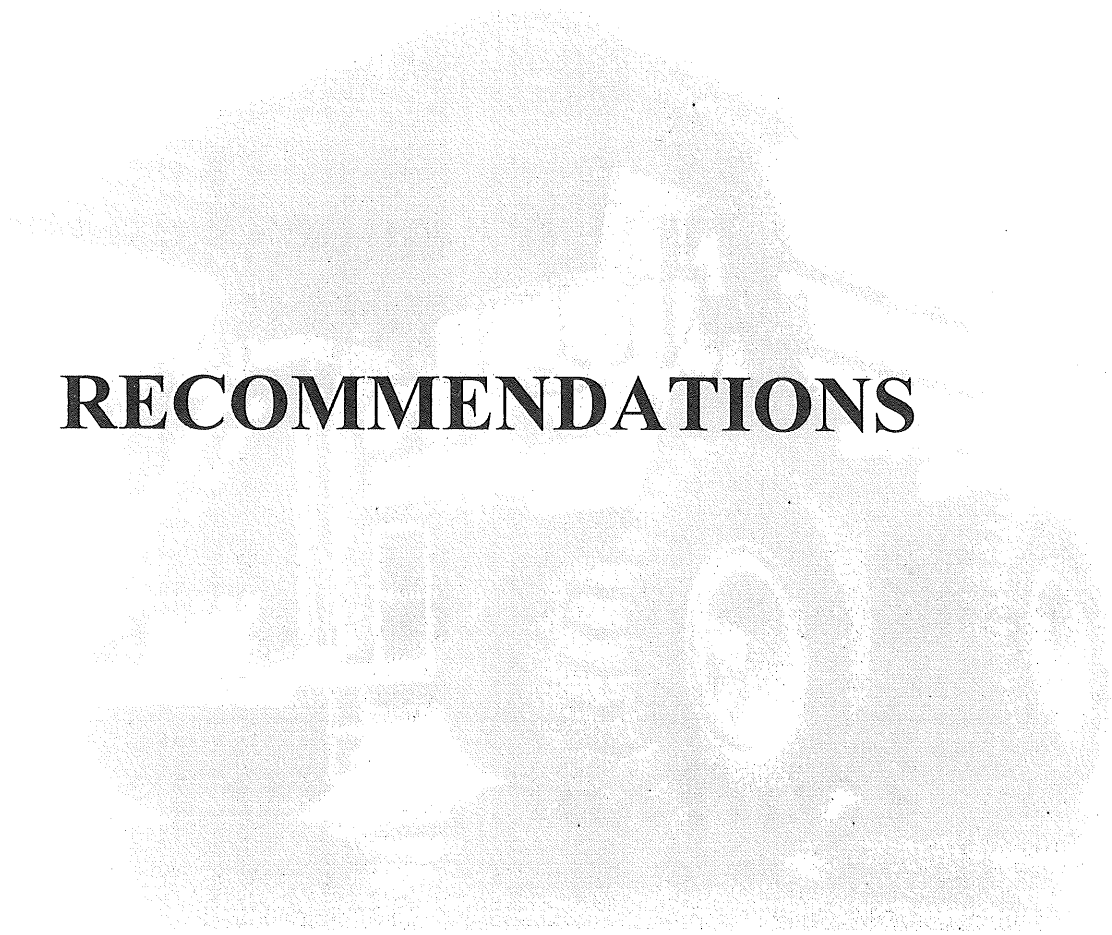
Iron Range Resources & Rehabilitation Board

Taconite Production Tax Committee



RECOMMENDATIONS

Submitted to:

Governor Arne Carlson
Members of the Minnesota Legislature

January 25, 1996

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CHAPTER 1

INTRODUCTION

The histories of the iron and taconite mining industries and Minnesota's Iron Range communities are inextricably linked; their future vitality is intertwined because the taconite industry plays a major role in the economy of northeastern Minnesota. Given this linkage, Governor Arne Carlson in 1993 directed the Iron Range Resources and Rehabilitation Board (IRRRB) to create the Governor's Task Force on Mining and Minerals to explore issues facing this important industry and make recommendations to the Governor and the Legislature on sound state policies relating to mining. The Task Force met in 1993, 1994 and 1995.

Among the issues discussed by this task force was the level of taxation the taconite industry faced. When it became clear in 1995 that the issue needed in-depth study, the Task Force unanimously recommended that "*the IRRRB Commissioner appoint a committee of industry, labor, local governmental officials, state agencies, and Iron Range legislators to examine and discuss why taconite production taxes*[1] *are needed and how they are used by local governments and the IRRRB, how these taxes impact the competitiveness of Minnesota taconite producers, and how these divergent factors should be weighed in devising mining tax policies*

[1] The taconite production tax is levied against each ton of taconite pellets produced in Minnesota. This production tax, which companies pay instead of paying local property taxes, amounts to $2.054 per ton of taconite. The proceeds from this tax, which totaled more than $82 million in 1995, are distributed to cities, townships, school districts, counties, local property taxpayers and the IRRRB according to a formula established in state law.

that are acceptable to both taxpayers and tax recipients." The Taconite Production Tax Committee was born of this recommendation, and this report constitutes the committee's response to its charge.

Committee membership and process

In order to ensure a thorough and balanced discussion, the Production Tax Committee membership included a broad cross-section of those impacted by the taconite industry and the tax policies applied to it.

The 15-member committee met throughout the fall to explore the issues facing the industry as well as local units of government in northeastern Minnesota. Expert testimony was provided by Minnesota Department of Revenue staff, local government officials, industry representatives and a financial analyst from a Canadian securities firm. In addition, committee members toured two taconite mining operations -- LTV Steel Mining Company and Hibbing Taconite Company -- to become better acquainted with taconite mining and processing and to become more familiar with the capital needs of plants of different ages.

These in-depth discussions helped the committee achieve one of its primary goals: To provide an open forum in which to learn about all aspects of the taconite production tax. The fiscal situation of local governments -- cities, townships, school districts and counties -- was outlined in detail, providing information about the pressures facing local governments and the role taconite taxes play in local financial decisions. The capital needs of the companies, as well as their challenges in remaining competitive, were reviewed. In addition, committee members studied the distribution of the production tax proceeds and the IRRRB budget.

Preview of this report

This report will provide a detailed summary of the information gathered by the committee, giving the reader a thorough understanding of the taconite production tax -- its impact on local governments and on the industry that pays it. Although other opportunities to discuss this complex tax may have occurred in the past, the broad membership of the committee offering this report presents a unique opportunity for decision makers to view the context of the production tax -- and the committee's recommendation -- in a more holistic light.

The report also will provide a clear explanation of the taconite production tax and its distribution formula.

Finally, based upon the context of the committee's discussion and the state taxing and distribution formulas, the committee will offer its consensus recommendations at the end of this report.

CHAPTER 2

ECONOMIC CONTEXT: TACONITE'S IMPACT

Taconite companies provide more than 6,000 high-paying jobs[2] in northeastern Minnesota, forming the backbone of the Iron Range economy even though the number of mining jobs has declined from a modern-day high of more than 16,000 in 1978. In addition, other spin-off industries that directly service the taconite companies supply a significant number of jobs. All told, the presence of the taconite companies means more than 17,000 jobs -- or about 11% of the total employment in the area. Historically, many Iron Range communities were formed by the workers in these mining activities, and many still rely upon the companies' employees as a core segment of their populations.

In addition to the number of people employed by the taconite and related industries, the taxes paid by the companies help support the local government infrastructure -- further linking the fortunes of local government with the fortunes of the taconite industry. Local units of government support a vital taconite industry as essential to their survival and the services they provide. Whether at the township, city, county or school district level, taconite production taxes make up a significant portion of the overall local budgets that provide such services as education,

[2] The Iron Mining Association reports that the Minnesota taconite industry payroll for 1995 was $332 million. The Minnesota Department of Revenue estimates that this gross payroll will result in approximately $14,490,000 in income tax paid to the State of Minnesota.

public works, public safety and other community needs.

Because this reliance on mining had, in the past, created a boom and bust cycle for communities dependent upon mining taxes, there has been a concerted effort to diversify the economy of the Iron Range. Helping non-taconite related industries expand or locate in the area can create a commercial and industrial property tax base that will be less volatile than the production tax, which can vary according to the wide fluctuations in the demand for taconite[3]. The IRRRB serves as a regional coordinator for this economic diversification effort, although local governments individually also invest significant effort and resources into economic development. Long-range planning also dictates that the Iron Range prepare for a time when the economically mineable taconite is depleted; a commercial and industrial business mix that will survive diminished taconite activity is the best insurance against a mass exodus of citizens from the Iron Range. Whether efforts are purely local or a partnership between the IRRRB and a local unit of government, these economic diversification attempts also focus on the creation of high-paying jobs that offer good benefits to workers. *In other words, economic development efforts are being invested in the very kind of jobs provided by the taconite companies.* In addition, the IRRRB has helped enhance the long-term viability of the taconite industry by providing $38 million[4] to the seven producers for plant and equipment improvements.

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[3] Taconite production taxes now are calculated using a three-year production average, which minimizes the fluctuations in revenue to local government and provides more predictability for taconite tax payers.

[4] Of this, $17.7 million was money rebated to the taconite companies through the Investment Tax Credit program in 1993-95. $14 million was distributed as $2 million grants to each company for plant and equipment improvements under the IRRRB Taconite Assistance Program in 1994-95. $6 million was loans to National Steel Pellet Company that helped it reopen in 1994 following its closure in 1993, and $500,000 was an energy conservation improvements grant to Eveleth Mines in 1994.

There has been significant success in creating new employment opportunities and retaining existing jobs in northeastern Minnesota; more than 2,000 jobs have been or shortly will be created based upon the economic diversification efforts of the IRRRB and its local government partners over the last two years. But the economic benefits provided by the taconite companies remain a major force in the overall economic health of the region.

CHAPTER 3

LOCAL UNITS OF GOVERNMENT: A QUEST FOR STABILITY AND CERTAINTY

Production taxes play an important role in the budgets of local units of government on the Iron Range, in large part because the revenues are so constant. Based upon the state's distribution formula, the amount of money distributed to local units of government remains relatively constant, unless there are wide swings in production tonnages from year to year that are not moderated by the effects of averaging. Similarly, the amount of money distributed to local government remains unchanged if the tax per ton is raised or lowered slightly.

This consistency, which relies upon consistent levels of production by the taconite companies, helps local units of government face a rising tide of increased costs from inflation, mandates and a demand for services, as well as a citizenry less comfortable with shouldering increased property taxes simply in order to maintain the current level of services. The impact of likely federal budget cuts, along with the anticipation of fewer state resources, also poses a problem of unknown significance. In northeastern Minnesota, a declining and aging population, as well as an aging infrastructure, create additional problems for local government officials.

The production tax is distributed according to a formula established in state law. The proceeds from this tax are distributed to local governments and spent just like property taxes levied on residential, commercial and industrial property. In addition, the production tax proceeds are used to off-set the property tax paid by individual homeowners. Because the circumstances of land ownership and other property values vary significantly among different local governments, determining the average contribution of production taxes to local budgets is difficult. However, among the local units of government that made presentations to the committee, production tax contributions ranged up to 22 percent of local government budgets[5].

The IRRRB, which is also a beneficiary of the production tax proceeds, absorbs reductions or increases in those proceeds. This would appear to provide the certainty and stability that local governments seek; however, because a significant portion[6] of the IRRRB's budget is set aside for grants to local units of government, not including schools, when reductions in the taconite production tax proceeds occur, the impact is felt by local units of government because fewer grant dollars are available. Without these grant proceeds, local units of government would have to pay for projects with local property tax dollars or forgo them entirely[7].

Municipalities

Cities on the Iron Range have seen a decline in population, in large part spurred by the downturn in the taconite industry in the early 1980s. This has affected both residential and commercial/industrial property tax bases. In addition, property values underwent a similar

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[5]The committee heard presentations from the City of Virginia; Independent School District No. 701 (Hibbing Public Schools); St. Louis County, and Lake County.

[6]In fiscal year 1995, the local government grants amounted to about $8 million or approximately 15 percent of the agency's budget.

[7]The City of Virginia estimates that eliminating any IRRRB grants for projects could result in a 50 percent increase in the local property tax levy.

decline during the mid-1980s. More recently, however, the real estate market has recovered to pre-existing levels. Increased mandates from the state and federal levels, as well as an aging infrastructure in need of increasing repairs and/or replacement, have increased costs for local governments. Like governments throughout the country, Iron Range municipalities have attempted to reduce costs. The City of Virginia has 15 percent fewer employees and 35 percent fewer managers on staff in 1995 than were employed seven years earlier. In addition, an increased interest in inter-community cooperation and collaboration to help reduce the cost of providing basic government services has re-surfaced on the Iron Range, in part spurred by training supported by the IRRRB and the Blandin Foundation.

School Districts

Because of declining enrollments and the desire to provide a quality education, Iron Range school districts have led the state in efforts to consolidate, including landmark legislation that created a framework for reorganization and consolidation. Five school districts have recently consolidated on the Iron Range, and discussions about consolidation are likely to continue in some fashion because unlike other school districts in Minnesota, such as those in the Twin Cities metropolitan area, Iron Range districts continue to see enrollment declines. The same problems plaguing other local governments -- increased federal and state mandates, inflation, an aging population, a declining property tax base and old buildings in need of repair -- beset school districts, as well. School districts face an additional problem, however; declining state aids[8].

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[8] While the state might be spending more on education overall, these increases are seen mostly in areas with growing school populations.

Under the state's school funding formula, most school districts receive money from the state as well as taxes levied against local property tax payers. Taconite taxes replace money that otherwise would come from state coffers or local levy.

Counties

Counties share many of the problems faced by municipalities and school districts, but their role in providing local services is somewhat unique. One county commissioner described his county as a contractor for state services. In St. Louis County, more than 35 percent of the county's budget goes to pay for state or federal mandates; in Lake County, where the overall budget is smaller, mandates account for 90 percent of the county's budget. In addition, the "get tough" approach to crime and punishment has increased counties' costs. And counties in northeastern Minnesota face higher costs for providing services to a population that is aging more rapidly than found in the rest of the state or nation. Significant public ownership of large tracts of land throughout northeastern Minnesota[9] limits the amount of taxable property in the counties' jurisdictions, as well.

Options and Opportunities

Faced with fewer opportunities to raise money and increased costs of providing services, local units of government have exercised a variety of options to balance their budgets They've reduced the level of services provided, although in the case of mandated services, this option is not acceptable. Many communities have increased their property tax levies, to the

[9] For example, in Cook County, 90 percent of the land is publicly owned; in Lake County, 82 percent of the land is publicly owned, and in St. Louis County, public entities own 63 percent of the land.

extent allowed by local voters and state law. And they've looked at more creative ways of balancing their books -- increasing local user fees, for example.

However, given the number of local governments throughout the Iron Range, the most likely opportunity for savings will come from inter-community cooperation and collaboration in providing services. In the past, this often has happened by default and not by design. And fears over losing local identity often have waylaid such partnership efforts. But recent efforts have been more thoughtful and reasoned; cities are reaching out to other cities to pool resources for recreational services and to cut administrative costs. The City of Virginia is working with St. Louis County to explore a partnership for providing law enforcement and/or public works. The IRRRB and the Blandin Foundation are in the process of conducting training sessions for community leaders living in nearby cities to encourage creative and cooperative approaches for community partnerships.

Whether cost-controlling efforts and community cooperation will provide the certainty and stability that local governments need into the future is unclear, particularly since the impact of expected federal and state budget cuts is as yet unknown.

CHAPTER 4

THE TACONITE INDUSTRY: SEARCHING FOR CERTAINTY, INVESTING IN THE FUTURE

Minnesota's seven active taconite mines and processing facilities[10] produce taconite pellets, a small round ball about the size of a marble made up of low-grade iron ore (taconite), a binder like bentonite and a small amount of silica. In 1995, the industry produced 45 million tons -- up from 23.4 million in 1982 -- a low point for the industry. These taconite pellets are transported by rail and boat to steelmaking facilities, primarily in the lower Great Lakes region.

The first mining companies on the Iron Range didn't mine taconite; they mined high-grade iron ore that didn't require the extensive processing demanded by the lower-grade taconite. But in the 1940s and 1950s, as natural, high-grade iron ore reserves became depleted and as means were developed to process taconite into a marketable commodity, taconite companies took the place of natural ore mines. Plants range in age from about 40 years old to about 20 years old, with older plants reflecting the higher costs per ton of production associated with aging and outdated equipment.

For the most part, Minnesota taconite companies are owned, in whole or in part, by

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[10]The seven mining and processing companies in Minnesota are: **Eveleth Mines** in Eveleth; **Hibbing Taconite Company** in Hibbing; **Inland Steel Mining Company** in Virginia; **LTV Steel Mining Company** in Hoyt Lakes; **National Steel Pellet Company** in Keewatin; **Northshore Mining Company** in Babbitt and Silver Bay, and **USX--Minntac** in Mt. Iron. One plant, Butler Taconite in Nashwauk, closed permanently in 1986.

integrated steelmaking companies -- corporations that own the raw material mining and processing facilities, as well as the steel mills that create a finished steel product. These integrated steel companies initially invested in the mining companies as a means of assuring supply and reducing the volatility of price paid for raw materials.

While Minnesota's Iron Range has supplied a tremendous amount of raw material to the nation's steelmaking plants in the past, taconite pellets now are facing stiff competition from many other suppliers of raw material: high-grade, natural iron ore from Brazil; scrap metal that is a better source of steel for some lower-cost steelmaking processes; and pellets from other mines located in Canada and Michigan. As the raw material options for steelmakers have increased, they have become less likely to turn automatically to their own taconite companies as a supplier; this is especially true during periods of decreased demand, which makes Minnesota taconite operations even more vulnerable during recessions in the steel industry. Consequently, taconite companies have focused on reducing their per-ton production costs to compete with these other sources.

In addition, the two relatively recent and very significant downturns in the steelmaking industry have forced the corporations to reexamine their business practices. Steel companies have focused on reducing debt[11] and reducing production costs to get the most out of existing assets. Capital investments in taconite companies have not kept up with requirements for capital improvement, while companies dedicate cash flow to reducing debt. In addition, because steel companies were perceived as "non-investment grade" when debt was high and the cost of

[11] Margaret Cornish-Kehoe, vice president and director of ScotiaMcLeod Inc., of Toronto, is a financial expert specializing in the steel industry. In her presentation to the committee, she indicated that reducing debt has as great an impact on earnings as reducing the production cost of steel.

production was relatively high as compared to European and Japanese producers, steel companies found it difficult to borrow capital except at punitive rates of interest. This situation persisted for much of the industry in the early to mid-1990s; however, some industry experts predict an improvement in the companies' operating profit per ton of steel in the latter part of 1995 and into 1996 and beyond. Adding to one analyst's prediction for an improved picture for the domestic steel industry is a downward trend in the amount of raw material imported, meaning more domestic raw material, like Minnesota taconite, will be used to meet domestic steelmaking needs[12]. Production levels likely will remain high throughout 1996, although downward pressure on steel prices and profits is expected because of new, increased steel production that does not rely on taconite pellets. What remains to be seen is whether and at what point integrated steel companies will be able to increase capital investments throughout their operations, including taconite companies, and what factors, including perceptions about tax climate, will influence those investment decisions.

Competition from without and within

As mentioned above, taconite companies supply raw materials to a steelmaking industry that can choose from among many sources of material. Product differences aside, the chief factor influencing a steel mill's choice of raw materials is price per ton[13]. Consequently, Minnesota taconite companies work very hard to reduce all components of their cost per ton of taconite --

[12] According to Cornish-Kehoe, domestic manufacturing of steel-containing products, including heavy equipment, machine tools and automobiles, has increased steadily in the 1990s -- increasing the domestic demand for raw materials.

[13] In 1994, the average cost per ton of taconite at the mine was $29.77. 1995 costs won't be available until May 1996.

labor, utilities, supplies, permits, transportation, royalties, taxes etc. Cost-reduction efforts work to trim pennies -- hopefully dollars -- from the per ton cost of taconite, a difficult task when many of the costs remain outside of the control of producers, including the declining quality of ore reserves and the increased cost of mining the ore. Minnesota taconite producers aren't alone in their efforts, however; their competition in Canada and Michigan, as well as scrap suppliers and Brazilian iron ore companies also work at being competitive.

Taxes

Because production taxes are a significant per ton cost, providing more certainty in the taxation process will improve taconite companies' long-term viability. Minnesota taconite companies see the production tax, currently at $2.054 cents per ton[14], as a cost that negatively affects their competitiveness, particularly compared to the tax situation in nearby Michigan and Canada[15]. In addition, a statutory provision known as the escalator dictates that the rate of the production tax will go up automatically each year based upon an index that reflects the performance of the economy as adjusted by inflation -- unless the Legislature votes to freeze the escalator each year[16].

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[14] Of the $2.054 per ton collected, $.154 is considered an Investment Tax Credit, which is set aside in a special account administered by the IRRRB. The funds in this account are used to help pay for capital improvements at each taconite plant if the improvements meet certain requirements.

[15] Calculating an exact comparison is difficult because of different tax structures in each taxing district. However, a rough estimate of the total tax burden paid per ton of ore indicates that the average tax burden in Michigan is 36 percent of the tax burden in Minnesota, and the average tax burden for Canadian plants is about 43 percent of the tax burden in Minnesota.

[16] The escalator has increased the taconite production tax twice since 1986, once in 1989 and again in 1991. The escalator has remained frozen for production years 1992-95.

Because taconite production taxes are levied instead of local property taxes, taconite companies also are concerned that they pay more than they would pay if they paid property taxes[17].

Taconite companies need to invest in new technology and replace aging equipment in order to reduce production costs, and to do so, they must turn to parent companies for capital. Given the financial picture painted by a steel industry expert, the competition for investment internally is also a challenge for taconite companies, which must demonstrate a greater need for capital investment and a greater rate of return than other company options. Taconite companies indicated that the uncertainty created by the escalator makes it more difficult for them to compete for corporate reinvestment in their facilities.

Capital reinvestment needs

Replacing worn or outdated equipment and implementing innovative technologies to boost production and/or lower costs at Minnesota's seven taconite companies will require an estimated $1.3 billion[18] investment over the next 10 years.

Integrated steel making companies, which have been trying to reduce debt[19] during the

[17] The Minnesota Department of Revenue estimates that if taconite companies paid property taxes, they would amount to about $1.81 per ton, although the companies maintain that their calculations indicate the amount would be closer to $1.67 per ton.

[18] Presentations by the seven taconite companies indicated the following capital requirements for the years 1996 through 2005: National Steel Pellet Company, $60 million; Eveleth Mines, $65 million; Inland Steel Mining Company, $71 million; Northshore Mining Company, $177 million; LTV Steel Mining Company, $210 million; Hibbing Taconite Company, $249 million; Minntac, $490 million.

[19] Integrated steel companies' debt includes significant pension obligations. Competitors whose processes rely on scrap metal tend to be younger companies and, therefore, don't have significant pension liabilities.

last several years and making more capital investments in steel facilities instead of the raw material end of the business, face increasing demand for capital investment throughout their operations. Minnesota's $38 million investment thus far in state taconite plants have provided a much-needed infusion of capital dollars, often serving as seed money for additional corporate investment. Capital needs run the gamut from replacing worn equipment to modernizing to installing new environmental controls. Consequently, in order to earn a place at the top of the corporate capital needs list, taconite companies must demonstrate how the investment ultimately will reduce production costs and result in a sound rate of return for investors.

Because the steel industry still is struggling to reduce its debt, attracting outside investors has been difficult. In addition, outside investors want to keep their profit and not have it reinvested into company operations. The fluctuating financial fortunes of the industry also have made Wall Street leery of investing.

If the positive picture painted by one analyst for the near-term is realized, integrated steel makers likely will have made progress in reducing corporate debt in a few years. If demand and revenues remain constant, this same analyst predicts companies likely will be more able to reinvest in all operations, including Minnesota taconite companies, providing those investments provide an adequate rate of return. However, many of those companies are facing immediate needs in order to keep production at current levels and costs; the ability to modernize and to keep reducing costs also requires a more immediate infusion of investment. Minnesota taconite companies indicate that a willingness by the state to consider providing more certainty in taxation policies and/or investing more resources into capital improvements within the plants would ensure a brighter future for the plants and the support they provide local communities.

CHAPTER 5

THE IRRRB

The IRRRB is a state agency created in 1941 as part of a legislative compromise on mining taxation. Currently, it receives virtually all of its funding from taconite production tax revenues, according to formula. Although its focus has varied somewhat over the last 55 years, there always has been an element of economic diversification in its mission. IRRRB has two major thrusts: diversification of the economy of the Iron Range through a wide variety of programs and because production taxes replace property taxes, community development activities.

In general, the IRRRB views its role as a regional focus for economic diversification. Because its service territory spans almost all of northeastern Minnesota, the IRRRB can play a unique role in creating partnerships with local units of government and in serving as a coordinator of economic development activities. This role is unique to IRRRB, and consequently, is the priority for spending agency dollars. The agency also takes very seriously its community development program, which leverages local and other contributions to pay for public projects that otherwise would be paid for with local property tax dollars. However, because this role could, if necessary, be assumed by local units of government, the community development grant budget has been the primary agency program cut when agency revenues have decreased. Likewise, increased revenues often are directed toward community development assistance.

Because of the distribution formula, IRRRB accounts are the last recipients of the taconite production taxes. After local governments -- school districts, townships, cities and counties -- have received their allotted amount of the proceeds, the remainder is divided up among IRRRB-managed accounts. The net effect of this is that when the amount of tax collected increases through an increased rate of taxation, the IRRRB receives the entire increase; when the amount of tax collected increases due to increased production the distribution to all tax recipients, including the IRRRB, increases proportionately. The converse also is true: when proceeds decline, either through a decline in production or a decrease in the rate of taxation, IRRRB revenue declines much more rapidly than revenue to local governments.

CHAPTER 6

RECOMMENDATIONS

Committee members jointly developed and unanimously agreed that these recommendations address the desires and concerns of both local government and the taconite industry by providing greater tax certainty and investment capital for their futures, which remain inextricably linked:

Production Tax Escalator

Eliminate the taconite production tax escalator, beginning in production year 1996.

Investment Tax Credit

Increase the Investment Tax Credit, which currently rebates 15.4 cents per ton of the $2.054 per ton taconite production tax to taconite producers for plant and equipment improvements, to a maximum of 31.4 cents per ton as follows:

- to 20.4 cents per ton, should taxable tonnage reach 40 million tons
- to 25.4 cents per ton, should taxable tonnage reach 41 million tons
- by an additional 1.5 cents per ton for each additional one million taxable tons, starting with 42 million taxable tons

This increase would remain in effect for 10 years beginning in production year 1996. Companies would be required to provide a 1:1 match to receive the increased investment tax credit. This match can be met by the aggregate investment in a plant each year and need not be project specific.

The committee further recommended that money to provide the increased investment tax credit come from production tax revenues that otherwise would flow directly to the Northeast Minnesota Economic Protection Trust Fund, commonly known as the 2002 Fund. Interest and earnings from the 2002 Fund are used by the IRRRB to fund economic development projects. The 2002 Fund currently has a balance of approximately $62 million, and this recommendation is designed so most of the money needed to pay for the increased investment tax credit would not exceed the monies derived from new production, therefore not substantially reducing[20] the current balance in the fund.

The committee respectfully submits these recommendations to the Governor and Legislature for their consideration.

[20]The Minnesota Department of Revenue estimates that the increased Investment Tax Credit will reduce the balance of the 2002 Fund by approximately $414,000 at 44.5 million tons and $831,000 at 45.5 million tons (See page 35). There are several ways that the taconite tax formula could be adjusted so that the balance of the fund would not be reduced at higher tonnages.

APPENDIX

Members of the IRRRB Taconite Production Tax Committee

Ann Glumac, (Chair) Deputy Commissioner, Iron Range Resources & Rehabilitation Board
Duluth

Bill Brice, Director, DNR Minerals
St. Paul

Carl D'Aquila, Businessman & Former Legislator
Hibbing

Nick Dragisich, City Administrator, City of Virginia
Chisholm

Jim Hoolihan, Businessman & Former Mayor of Grand Rapids
Grand Rapids

Robert Kind, Mayor of Silver Bay
Silver Bay

Richard Kirkes, Retired Mining Manager & Former Mayor of Bovey
Bovey

John Kokotovich, General Manager, Eveleth Mines
Hibbing

Barb Nosan, Assistant Vice President, First National Bank of Chisholm
Chisholm

Frank Ongaro, Executive Director, RAMS
Hibbing

Lee Ramsdell, Lake County Commissioner
Silver Bay

Steve Raukar, St. Louis County Commissioner
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TACONITE PRODUCTION TAX
(M.S. 298.24, M.S. 298.28)

The Taconite Production Tax is a severance tax paid on concentrates or pellets produced by the various taconite companies. It is paid "in lieu of" ad valorem taxes on taconite and lands containing taconite. With some exceptions, it also excludes land and structures used in the production of taconite from ad valorem taxes. (Special ad valorem taxes are discussed in detail on pages 43, 44 and 45).

The taconite production tax rate for concentrates produced in 1994 remained frozen at $2.054 per taxable ton. The tax is levied on "taxable tons" which are the average tonnage produced during the current and previous two production years. The taconite production tax rate for concentrates produced in 1990 was $1.975 per taxable ton. The 1991 tax rate was the 1990 rate escalated by the percentage increase in the Gross National Product Implicit Price Deflator from the fourth quarter of the second preceding year to the fourth quarter of the preceding year, which increased the rate to $2.054. Normally, the escalator takes effect each year unless the rate is frozen or changed by the legislature.

The rate was frozen by the 1992 legislature at $2.054 per ton for production years 1992 and 1993. The 1994 legislature continued the frozen rate at $2.054 per ton for production year 1994 payable 1995. After considerable study, discussion and input from numerous stakeholders, the 1995 legislature extended the rate freeze for production year 1995 payable 1996.

The revenues from the production tax are distributed by statutory formulas to various cities, townships, counties, and school districts within the taconite tax relief area (the area is comprised of the present taconite mining area plus areas where natural ore was formerly mined). Funds are also allocated to the Iron Range Resources and Rehabilitation Board (I.R.R.R.B.) which administers the Taconite Environmental Protection Fund and the Northeast Minnesota Economic Fund.

LEGISLATIVE CHANGES

Payment Dates and Method Changed. The 1993 legislature eliminated the 90 percent and 10 percent payment schedule. Beginning with the 1993 tax payable in 1994, there will be only one payment date, February 24, when 100 percent of the tax is due. The date that the Department of Revenue is required to notify each producer of their tax obligation has been changed from February 8 to February 15.

Taconite Economic Development Fund (M.S. 298.227). The Taconite Economic Development Fund was first created for production years 1992 and 1993 at a rate of 10.4-cents per taxable ton. The 1995 legislature extended the Taconite Economic Development Fund through the 1996 production year at the rate of 15.4-cents/ton established in 1993. Each producer's share can be spent for equipment and machinery or research and development in Minnesota on mining technology or taconite, iron, or steel production technology. A joint labor-management committee must agree on projects to be funded. Each producer has two potential sources of Taconite Economic Development Funds:

1. Acid or Flux Pellets

   The amount of the production tax that is credited to each producers share of the Taconite Economic Development Fund is 15.4-cents/ton. All producers qualify for this through production year 1996, as mentioned above.

2. Pellet Chips and Fines

   This provision remains the same as last year--an amount equal to 50 percent of the tax for pellet chips and fines not exceeding 5/16-inch in size will be allocated to each company's share of the Taconite Economic Development Fund. The total amount shall not exceed $700,000 for all companies. If the total claimed exceeds $700,000, each company's share will be prorated. The determination of this allocation is based on *current production year sales* of chips and fines and not the three-year average of production. However, sales of fine concentrate do qualify for this credit. Crushed pellets are not eligible for the chips and fines credit.

Thus, each company is eligible to receive 15.4-cents per taxable ton plus an additional amount based on current year sales of chips and fines.

A listing of the projects funded and current years distribution of the Taconite Economic Development Fund is shown in Figure 23 on page 26 in the I.R.R.R.B. section.

ECONOMIC DEVELOPMENT INCENTIVES

The 1995 legislature authorized the I.R.R.R.B. to loan up to $10 million from the Economic Fund (2002) for construction and equipping of direct-reduced iron plants. The amount is limited to $5 million per facility and the loan authority expires December 31, 1997. The plant must produce iron upgraded to a minimum of 75 percent Fe. This loan provision is also available to mineral producers subject to net proceeds tax (generally non-ferrous).

REDUCED TAX RATE FOR DRI

The 1995 legislature revised the reduced production tax rate for DRI which had been established in 1994. The first five years of a DRI plant's production are subject to the reduced rate under the new law. The reduced rate is 25 percent of the regular taconite production tax rate for the first 500,000 taxable tons for the production year. A 50 percent rate applies to production over 500,000 tons during the production year. If the taxpayer had no production in the two years prior to the current production year, the taxable tonnage would be 166,667 tons due to the three-year average provision. This tonnage would be taxed at the 25 percent rate.

Also, a provision has been added to avoid double taxation of DRI as both DRI and taconite concentrate. If an existing taconite producer sells concentrate to a separate company producing DRI in the state, this concentrate is not subject to the existing production tax, but will be taxed as DRI and the tax will be paid by the DRI producer. The property tax exemption for taconite producers will also apply to DRI.

FLUX PELLETS

Fluxed pellets have limestone or other basic flux additives combined with the iron concentrates before pelletizing. All of the companies have experimented with flux pellets. Two companies, Inland Steel and USX, are producing fluxed pellets. Eveleth Mines, National, and Northshore are producing a partially fluxed pellet containing a low percentage of limestone additive. Northshore also produces fluxed pellets and acid pellets. The remaining companies produce primarily acid pellets. M.S. 298.24, Subd. 1, clause (e) allows the weight of flux added to be subtracted from the weight of pellets for production tax purposes. All tables in the Minnesota Mining Tax Guide with production statistics use an equivalent or calculated weight for fluxed pellets. The taxable weight is the dry weight less the weight of the flux. The weight of the flux is determined by a metallurgical calculation based on the analyses of the finished pellet, the concentrate, and the flux stone. Beginning with 1988, a flux credit was allowed against production tax. Occupation tax is based on iron units and uses the full weight including flux. A reconciliation of both tonnages and the weight of the flux is shown on Figure 27.

PELLET WEIGHING

A survey of weighing procedures used has been completed. Dust and other environmental problems have been an increasing concern with all of the industry and the railroads. It appears that fluxed pellets have increased problems with dust. There has been a need to increase dust control water sprays at various points in the pellet processing and shipping operations. Therefore, due to these environmental concerns and basic fairness, the Department of Revenue changed from natural weight to dry weight for tax reporting purposes. This change was effective beginning with the 1990 production year. The years 1989 and 1988 were still reported on a natural basis for three-year average purposes.

DEFINITION OF TACONITE TAX RELIEF AREA

One common prerequisite exists for all taconite aids and grants--that is the recipient must be within the geographic confines of the taconite tax relief area. A taconite tax relief area is defined by statute (M.S. 273.134) as follows:

"Tax relief area" means the geographic area contained within the boundaries of a school district which contains a municipality which meets the following qualifications:

(1) It is a municipality in which the assessed valuation of unmined iron ore on May 1, 1941, was not less than 40 percent of the assessed valuation of all real property and in which, as of the applicable assessment date, the assessed valuation of unmined iron ore is not more than 60 percent of the assessed valuation of all real property, or

(2) It is a municipality in which, on January 1, 1977, or the applicable assessment date, there is a taconite concentrating plant or where taconite is mined or quarried or where there is located an electric generating plant which qualified as a taconite facility.

DISTRIBUTION OF FUNDS (M.S. 298.28)

Subd. 2 - Taconite Cities and Towns

A total of 2.5-cents per ton is allocated to cities and towns where taconite mining and concentrating occurs. Forty percent (1.0-cent/ton) of this fund goes to those cities and townships in which mining activity occurs. The remaining 60 percent (1.5-cents/ton) goes to those cities and townships in which the concentrating of the taconite occurs. (Note: This is done on a company-by-company basis).

If both mining and concentrating take place in a single taxing district, then the entire 2.5-cents is allocated there.

If mining occurs in more than one city or town, then the revenue (1.0-cent/ton) is divided based on either a percentage of taconite reserves or a four-year average of production. Most taconite mines have mining in two or more units.

If concentrating is split between two cities or towns, the revenue (1.5-cents/ton) is divided by the percentage of hours worked in each. The primary crusher is considered the first stage of concentration. The only current examples of this are Cyprus (Babbitt and Silver Bay) and Eveleth Mines (Eveleth, Fayal Township, and McDavitt Township). *Distribution detail in Figure 13.*

Subd. 3 - Taconite Municipal Aid Account

(a) - The Taconite Municipal Aid payment is made on September 15. Each city or township first receives the amount it was entitled to receive in 1975 from the occupation tax. This amount is then reduced according to the percentage aid guarantee provisions of M.S. 298.225. For example, if production levels mandate a 90 percent aid guarantee, then the occupation tax grandfather amount is also reduced to 90 percent. The remainder of the aid is distributed according to a complex formula using levies, valuation, population, and fiscal need factors.

The conditions necessary for a municipality to qualify for this aid are identical to the qualifications for the 66 percent taconite property tax relief listed under Subdivision 6 on this page. The statutory references governing Municipal Aid are M.S. 273.134, M.S. 298.28, Subd. 1, Clause 2, and M.S. 298.282. *Distribution detail is Figure 13.*

(b) & (c) - Additional money is allocated to cities and townships if more than 75 percent of the city's assessed valuation consisted of iron ore as of January 2, 1980, or if more than 75 percent of the township's assessed valuation consisted or iron ore as of January 2, 1982. The distribution is calculated using certified levies, net tax capacities, and population. Currently, only White Township and the city of Kinney qualify.

Subd. 4 - School Districts

(a) - $.275 per taxable ton distributed under (b) & (c) plus increase in paragraph (d).

(b) - School District $.055 Fund - A total of $.055 per taxable ton for each taconite company is allocated to school districts in which mining and concentrating occurs. If the mining and concentrating take place in separate districts, 40 percent is allocated to the location of mining and 60 percent to concentrating.

In addition, if the mining occurs in more than one school district, the 40 percent portion is further split based on either a four-year average of production or a percentage of taconite reserves. If the concentrating function of a company takes place in more than one school district, the 60 percent portion is further split according to hours worked in each district. *Distribution detail in Figure 14.*

4(c) - School $.22 Fund - All taconite companies pay $.22 per taxable ton into a fund which is split among the 15 school districts comprising the taconite relief area. Each school district receives the amount which it was entitled to receive in 1975 from the taconite occupation tax. This amount may be increased or reduced by the percentage aid guarantee provisions of M.S. 298.225. The remaining amount in the fund is distributed using an index based on pupil units and tax capacities. Generally, districts with larger tax capacities per pupil unit tend to receive a proportionately smaller amount of this fund. *Distribution detail in Figure 14.*

4(d) - Taconite Referendum Fund (T.R.F.) - Taconite school districts quality for an additional $175 per pupil unit over and above state aids by passing a special levy referendum equal to 1.8 percent of net tax capacity. The T.R.F. pays the difference between the local levy and $175 per pupil unit. The payment is made on July 15 each year. The fund receives money based on the theoretically escalated portion of the 22-cent school fund. If any money remains in the fund, it is distributed to the Environmental Protection Fund (two-thirds) and the Northeast Minnesota Economic Protection Trust (one-third). Note: A district receiving money from the T.R.F. shall reserve $25 per pupil unit (of the $175 authorized) for outcome-based learning programs approved by the Commissioner of Education. *Distribution detail in Figure 14.*

Subd. 5 - Counties

(a) - The allocation of 16.5-cents per taxable ton to taconite counties (subject to adjustment by M.S. 298.225) is to be distributed under Subd. 5(b) through (d). This 16.5-cents was subject to escalation prior to 1986. By 1986, the 13-cents amount in Subd. 5(b) had increased to 20.52508-cents and was frozen. The 3.5-cents amount for county road and bridge covered in Subd. 5(d) had increased to 5.52598-cents and was also frozen at that level. The amounts listed in (b) and (d) are the statutory amounts prior to escalation. *Distribution detail in Figure 16.*

(b) - Taconite Counties with Mining or Concentrating - Thirteen-cents per taxable ton is distributed to the county in which the taconite was mined or quarried or in which the concentrate is produced (split in same manner as taconite cities and towns), less any amount distributed in Subd. 5(c). *Distribution detail in Figure 16.*

(c) - Counties - Electric Power Plant - If an electric power plant owned by and providing the primary source of power for a taconite plant is located in a county other than the county in which the mining and concentrating processes are conducted, one-cent of the 13.0-cents per ton (for that company) shall be distributed to the county in which the power plant is located. (This one-cent is not escalated, but is subject to M.S. 298.225 adjustment). For 1994, this amounted to $94,265 or 1.3155-cents per taxable ton including the adjustment. The only company whose distribution is affected by this provision is LTV due to their power plant location at Taconite Harbor in Cook County. Their one-cent per ton distribution for the 1983 base year was based on 9,793,639 tons. This amount was carried forward from 1979 based on a previous guarantee. The current year M.S. 298.225 guarantee percentage is always applied.

$97,936 (1983 base) x 96.251378% = $94,265

(d) - Taconite Counties Road and Bridge - Each county receives a portion of the aid in the same manner as taconite cities and towns, to be deposited in the county road and bridge fund. The basic allocation is 3.5-cents per taxable ton subject to adjustment as per M.S. 298.225. *Distribution detail in Figure 16.*

Subd. 6 - Taconite Property Tax Relief

(a) - Taconite Property Tax Relief - A total of 15-cents per taxable ton is escalated by the Gross National Product Implicit Price Deflator and is allocated to the Taconite Property Tax Relief Account. The qualifications and distribution of taconite property tax relief are described in the following paragraphs. The escalation feature was frozen for 1991 and 1992. For the 1994 production year, the rate increased to 30.4760-cents per taxable ton.

The Taconite Homestead Credit reduces the tax paid by owners of certain properties located on the Iron Ranges. The properties receiving this credit are owner-occupied homes and owner-occupied farms. The tax on all of the land comprising the farm is used in determining the amount of credit for a farm. Prior to 1983, the credit on farms was limited to 240 acres.

If an owner-occupied home or farm is located in a city or town which contained at least 40 percent of its valuation as iron ore on May 1, 1941, or currently has a taconite mine, processing plant, or electric generating facility, the taconite credit is 66 percent of the tax on that property to a maximum of $294.40 for taxes payable in 1995. If the property is not located in such a city or town, but is located in a school district containing such a city or town, the taconite credit is 57 percent of the tax on the property to a maximum credit of $269.10 for taxes payable in 1995.

The taconite homestead credit cannot reduce the "effective tax rate" on each parcel of property below 95 percent of the "base year effective tax rate". "Effective tax rate" is the net tax divided by the market value, and the "base year effective tax rate" is the payable 1988 effective tax rate on a property with an identical market value to that of the property receiving the credit in the current year. The amount of the taconite homestead credit cannot be less than $10.00 per homestead. The total amount of taconite property tax relief paid in each county and school district is listed in Figure 9. An example of the calculation is shown on page 15.

The statutory references governing taconite property tax relief are contained in M.S. 273.134 to M.S. 273.136, and M.S. 298.28, Subd. 6. This is guaranteed by the Northeast Minnesota Economic Protection Fund as stated in M.S. 298.293. *Distribution detail in Figure 9.*

(b) - Electric Power Plant Aids From Property Tax Relief - For any electric power plant located in another county (as described in 5c), .1875-cents per taxable ton from the Taconite Property Tax Relief account shall be paid to the county. The amount was subject to escalation until frozen for the 1987 production year. The M.S. 298.225 guarantee also applies. For the 1994 production year, the total amount was .30261-cents per taxable ton (LTV's taxable tonnage). The frozen escalated rate is .296035-cents per taxable ton for Cook County subtracted from LTV's property tax relief distribution. The remaining amount ($471 for 1994) is provided by the M.S. 298.225 guarantee. The guaranteed amount for 1994 is determined by applying the 96.251378 percent guarantee by the $22,528 1983 distribution.

(c) - Electric Power Plant Aid from Property Tax Relief - This subdivision allocates .5625-cents per LTV's taxable tonnage to Cook County school district due to the LTV power plant in Cook County. Because of escalation (frozen in 1987), this amounted to .888104-cents per taxable ton (LTV tons) for 1994. This school aid is guaranteed at 50 percent or the variable rate, whichever is less. The 1983 base for the school was $67,586. For 1994, no guarantee applies and the distribution is calculated by multiplying the LTV taxable tons and the .888104-cents per ton escalated rate.

Subd. 7 - Iron Range Resources & Rehabilitation Board

An amount of three-cents per taxable ton escalated by the Gross National Product Implicit Price Deflator is allocated to this board. These funds are used by the I.R.R.R.B. for general operating expenses and community development grants.

Subd. 8 - Range Association of Municipalities & Schools

This .2-cent per taxable ton is paid to R.A.M.S. for the purpose of providing an area-wide approach to problems which demand coordinated and cooperative actions. All cities, towns, and schools in the taconite and iron ore mining area are included.

Subd. 9 - N.E. Minnesota Economic Protection Trust Fund

In addition to the amount provided in the remainder after all other distributions are completed, 1.5-cents per taxable ton is allocated to the Northeast Minnesota Economic Protection Trust Fund.

(a) - Taconite Economic Development Fund - This subdivision is explained in detail under 'Legislative Changes' on page 7.

Subd. 10 - Indexing

Provides indexing of the cents per ton allocation for Subd. 4(d), Subd. 6(a), Subd. 7 and 9. For the 1992 and 1993 distributions (1991 and 1992 production years), the amount distributed per ton was the same as in 1991.

For the 1994 distribution (1993 production year), the amount distributed was the distribution per ton for 1991 increased in the same proportion as the increase between the fourth quarter of 1989 and the fourth quarter of 1992 in the implicit price deflator. The index was increased in 1995 and shall be increased in 1996 and subsequent years in the same proportion as the increase in the implicit price deflator as provided in section 298.24, subd. 1.

Subd. 11 - Remainder

(a) - After all other aid distributions including school bond credits and payments, taconite railroad, Department of Revenue, and I.R.R.R.B. payments, the remainder shall be distributed two-thirds to the Taconite Environmental

Protection Fund and one-third to the N.E. Minnesota Economic Protection Trust Fund. The remainder includes interest earned on monies on deposit by the counties prior to final distribution. Beginning in 1989, the taconite railroad gross earnings tax was abolished and these railroads were made subject to property tax, the same as other railroads.

Prior to 1989, every taconite railroad paid a 3.75 percent gross earnings tax to the state. Taconite railroads are wholly owned by a mining company and are principally used for the transportation of taconite concentrates. They are not used to haul freight commercially as a common carrier.

(c) - Occupation Tax Grandfather Amount to I.R.R.R.B. - In 1978 and each year thereafter, there has been distributed to the I.R.R.R.B. the amount it received in 1977 from the distribution of the taconite and iron ore occupation taxes. Amount: $1,252,520.

ADDITIONAL PAYMENTS

Although the following payments are not included in M.S. 298.28 or its subdivisions, they are subtracted prior to dividing the remainder described in Subd. 11.

1. Department of Revenue - Minerals Tax Office

Beginning with the 1993 production year (payable 1994), $55,000 per year for two years was appropriated from production tax revenues to the Department of Revenue for costs and expenses incurred in the administration of the Taconite Production Tax. The 1995 legislature increased this appropriation to $75,000 per year (Chapter 254, Article 1, Section 16, Laws of Minnesota for 1995).

2. School Bond Credits and Payments

The legislature has authorized payment of school bonds from taconite revenues at various times. This has been done both with production tax credits for bonds paid by a mining company and direct payments. The first credits were authorized when whole new towns were built for the Erie and Reserve taconite plants in Hoyt Lakes and Silver Bay. Since that time, school bond payments have been authorized by the legislature for most Iron Range school districts. Taconite revenues have been authorized to fund 100, 90, or 80 percent of the bond payment, depending on the school district situation and year authorized. *Distribution detail in Figure 15.*

A) A $240,000 payment is made from the production tax to School District 710 for payment of school bonds. An amount equal to four-cents per ton of Eveleth Mines taxable tonnage is subtracted from money otherwise payable to the Northeast Minnesota Economic Protection Fund. Any remaining amount required to equal $240,000 shall be paid as provided by M.S. 298.225.

B) The 1982 legislature increased the taconite production tax credit to four-cents per taxable ton for school district bonds. However, a credit of seven-cents per ton is allowed for Independent School District 712, Mt. Iron-Buhl. The school bond credits are subtracted from the amount which would otherwise be distributed to the Northeastern Minnesota Economic Fund. These credits are for bond payments made by the companies and are not collected or distributed by the Department of Revenue. Currently, only Mt. Iron-Buhl is covered by the credit.

C) The 1988 legislature passed a provision that has the production tax pay a portion of the bonds issued by the following four school districts: 318 (Grand Rapids), 701 (Hibbing), 706 (Virginia), 708 (Tower), and 2142 (St. Louis County). Money for the payments are deducted, in equal shares, from the distributions made to the Taconite Environmental Protection Fund and the Northeast Minnesota Economic Protection Trust. *Distribution detail in Figure 15.*

D) The 1990 legislature authorized additional school bonds for eight school districts. These payments are made by the respective county auditors from production tax revenues. Money for the payments is deducted in equal shares from the environmental and economic protection funds. *Distribution detail in Figure 15.*

E) The 1992 legislature authorized three additional school bond issues. The three districts are Grand Rapids, Lake Superior, and Virginia. Lake Superior and Virginia have issued bonds but Grand Rapids has not been able to get voter approval on a new bond issue as of September 1, 1995.

AID GUARANTEE (M.S. 298.225)

The recipients of the taconite production tax as provided in M.S. 298.28, subdivisions 2 to 5, subdivision 6, paragraphs (b) and (c), subdivisions 7 and 8 are guaranteed to receive distributions equal to the amount distributed to them with respect to the 1983 production year, provided that production is not less than 42,000,000 taxable tons. If the production is less than 42,000,000 taxable tons, the amount distributed from the fund will be reduced proportionately by two percent per each 1,000,000 tons by which the production is less than 42,000,000 tons. For example, if the taxable tonnage (three-year average) is 39,800,000, then the proportionate reduction is 4.4 percent. This is calculated by multiplying two percent times 2.2 million tons. The 1994 guarantee percentage is 96.251378%. This aid guarantee is funded equally from the initial current year distributions to the Taconite Environmental Protection Fund and the Northeast Minnesota Economic Protection Fund. If the initial distributions are insufficient to fund the difference, the Commissioner of the I.R.R.R.B. shall make the payments of any remaining difference from the corpus of the Taconite Environmental Protection Fund and the corpus of the Northeast Minnesota Economic Protection Trust Fund in equal proportions, as directed by the Commissioner of Revenue. The aid payments covered by this variable guarantee are listed as follows:

AID GUARANTEE (M.S. 298.225)

(Continued)

1. 2.5-cents City and Town Fund.
2. 12.3-cents Taconite Municipal Aid.
3. 3-cents escalated to I.R.R.R.B.
4. .2-cents R.A.M.S.
5. .1875-cent power plant transfer from Taconite Property Tax Relief Account to Cook County.

The following funds are guaranteed at 75 percent or the variable guarantee, whichever is less:

1. 13.0-cents Taconite County Fund.
2. 3.5-cents Taconite County Road and Bridge Fund.

The following funds are guaranteed at 50 percent or the variable guarantee, whichever is less:

1. 22-cents School Fund.
2. 5.5-cents School District Fund.
3. Taconite Referendum Fund.
4. .5625-cent power plant transfer from Taconite Property Tax Relief Account to S.D. 166.

The Taconite Property Tax Relief is not covered by M.S. 298.225, but is guaranteed separately by the Economic Protection Fund, as stated in M.S. 298.293.

TACONITE PRODUCTION TAX DISTRIBUTION CALCULATION

The taconite mining companies make the production tax payments directly to six counties (Cook, Lake, St. Louis, Itasca, Crow Wing, and Aitkin) and the I.R.R.R.B. Each county auditor is responsible for making the taconite aid payments to the various jurisdictions within the county. St. Louis County was designated as fiscal agent for the taconite property tax relief account and issues taconite property tax relief checks to the other counties.

The Department of Revenue makes all computations regarding the amount to be paid by the companies and the aid payments due to cities, schools, townships and counties. Interest earnings on undistributed funds are remitted by the counties to the I.R.R.R.B.

The proceeds of the 1994 taconite production tax (payable 1995) are distributed by statute as follows (all figures are cents per taxable ton):

M.S. 298.28,			
Subd. 2	- Taconite Cities and Towns		2.5
Subd. 3	- Taconite Municipal Aid Account:		12.3
Subd. 4	- School Districts -		
	(b) Taconite schools (mining and/or concentrating in the district):	5.5	
	(c) School districts within the taconite relief area (distributed by formula):	22.0	
	Basic School District Total:		27.5
	(d) Taconite Referendum Fund:	(formula amount - see page 9)	
Subd. 5	- Counties -		
	(b) Taconite Counties:	13.0*	
	(c) (includes Electric Power Plant)		
	(d) Taconite Counties Road/Bridge:	3.5*	
	Counties Total:		16.5*
Subd. 6	- Taconite Property Tax Relief (includes .75-cents for Cook County and Cook County schools):		15.0**
Subd. 7	- I.R.R.R.B.:		3.0**
Subd. 8	- Range Association of Municipalities and Schools:		0.2
Subd. 9	- N.E. Minnesota Economic Protection Fund:		1.5**
Subd. 9a	- Taconite Economic Development Fund:		15.4
Subd. 10	- Indexing Provisions:		---
Subd. 11	- Distribution of Remainder:		---

* Beginning with the 1986 production year, the cents-per-ton distribution was frozen at an escalated rate of 20.52508-cents for the County Fund and 5.52599-cents for the County Road and Bridge Fund. However, the actual distribution may be larger due to M.S. 298.225.

** These funds are escalated using the Gross National Product Implicit Price Deflator. After escalation, the cents-per-ton for Taconite Property Tax Relief was 30.4760-cents, I.R.R.R.B. was 6.0952-cents, and the 1.5-cent N.E. Minnesota Economic Protection Fund was 3.0476-cents. *The full amount distributed, including escalation and M.S. 298.225 guarantees, is listed in Figure 11.*

Figure 7

NORTHEAST MINNESOTA ECONOMIC PROTECTION TRUST FUND AND ENVIRONMENTAL PROTECTION FUND

Period Ending	Economic Fund Balance	Environmental Protection Fund Balance
December 31, 1983	$28,487,283	
June 30, 1984	27,019,423	
September 30, 1985	28,859,669	
June 30, 1986	31,537,559	
June 30, 1987	31,186,041	
June 30, 1989	31,279,724	
June 30, 1990	36,679,552	$4,027,594
June 30, 1991	42,004,602	4,997,728
June 30, 1992	48,840,406	8,583,918
June 30, 1993	54,084,189	1,459,629
June 30, 1994	57,633,818	1,411,886
June 30, 1995	61,596,404	4,034,811

Economic Fund Major Withdrawals:

September 27, 1982	$ 2.5 million	I.R.R.R.B. Jobs Program
February 3, 1983	$ 5.0 million	I.R.R.R.B. Jobs Program
May 24, 1983	$10.0 million	I.R.R.R.B. Economic Development
February 25, 1984	$2.08 million	Aid guarantees to cities/schools (M.S. 298.225)*
February & May, 1987	$ .46 million	M.S. 298.225
September 26, 1989	$1.90 million	Property Tax Relief Guarantee**

* This aid guarantee formula was revised by the 1984 legislature so that further withdrawals should not be necessary except during serious depression of the iron ore industry.

** Funding for Taconite Property Tax Relief was reduced from 22-cents-per-ton to 12-cents-per-ton by the 1988 legislature. When this proved to be inadequate funding, it was increased by the legislature in the 1989 special session from12-cents to 15-cents-per-ton. This should eliminate withdrawals from the Northeast Minnesota Economic Fund for property tax relief in normal production years.

The Taconite Area Environmental Protection Fund (M.S. 298.223) and the Northeast Minnesota Economic Protection Trust Fund (M.S. 298.291 through 298.294) were established by the 1977 legislature. These two funds receive the remainder of the production tax revenues after all distributions provided under M.S. 298.28 and school bond payments are completed. A special allocation of 1.5-cents per ton for the economic fund is provided for in M.S. 298.28. The remainder is split with one-third going to the economic fund and two-thirds to the environmental protection fund.

The Taconite Environmental Protection Fund was "created for the purpose of reclaiming, restoring, and enhancing those areas of northeast Minnesota that are adversely affected by environmentally damaging operations involved in mining and producing taconite and iron ore concentrate." The scope of activities includes local economic development projects. The fund is administered by the I.R.R.R.B. Commissioner. Projects must be approved by the I.R.R.R.B. and the Governor.

The Northeast Minnesota Economic Protection Trust Fund is somewhat different in that only interest and dividends earned by the trust fund may be expended before January 1, 2002. Approval for expenditures from earnings is similar to the environmental fund. Expenditures from the principle of the trust fund may be made prior to 2002 only with authorization of the full legislature. This has been done on several occasions, as shown in Figure 7.

PRODUCTION TAX RATE HISTORY

The taconite production tax was enacted in 1941 at a rate of five cents per ton and included an index for iron content exceeding 55%. In 1969 the statutory base rate was increased and the first inflation index was added based on the wholesale price index (WPI). A series of increases occurred during the 1970's. In 1977 the index was charged to the steel mill products index (SMPI), and a new base rate of $1.25 was set. In 1986 the iron content index, first established in 1941, was eliminated. Also in 1986, the index was changed from the SMPI to the gross national product implicit price deflator (IPD). This change was made primarily due to industry objections to the SMPI. A new base rate of $1.90 was established in 1986 and remains in effect currently. The index has been allowed to take effect twice since 1986, once in 1989 and again in 1991. If the escalator were allowed to take effect for the 1996 production year, we are estimating an increase of three to four cents per ton based on current low inflation rates.

A new method of calculating the tax was introduced in the 1977 law. This law mandated that the tax be calculated on a three year average of tonnage for each company, or the current year, whichever was greater. The industry felt that this method was very unfair and it was repealed and replaced with the current straight three year average method in 1984. This repeal was preceded by a series of court cases over mining taxes which were resolved by Minnesota supreme court rulings and industry-legislative negotiations in 1984. The 1984 supreme court ruling upheld the constitutionality of the three year average or current year provision of the production tax calculation. However, the court directed the state to modify its' indexing calculation. This change resulted in a credit to the industry of $17.9 million and $5.5 million in interest. The entire amount was paid back through production tax credits to each company over five years.

PRODUCTION TAX RATE HISTORY & INDEX SUMMARY

PRODUCTION YEAR	STATUTORY BASE RATE	FE INDEX	INFLATION INDEX	TOTAL RATE
1941	5.0 - cents	.5 - cents	None	5.5 - cents
1969	11.5 - cents	.5 - cents	0 (WPI*)	12.0 - cents
1970	11.5 - cents	.5 - cents	0 (WPI)	12.0 - cents
1971	15.5 - cents	.5 - cents	.4 (WPI) cents	16.4 - cents
1972	18.5 - cents	.5 - cents	1.3 (WPI) cents	20.3 - cents
1973	20.5 - cents	1.0 - cents	2.8 (WPI) cents	24.3 - cents
1974	20.5 - cents	1.0 - cents	8.2 (WPI) cents	29.7 - cents
1975	60.5 - cents	1.0 - cents	13.4 (WPI) cents	74.9 - cents
1976	60.5 - cents	1.0 - cents	15.5 (WPI) cents	76.5 - cents
1977	125.0 - cents	4.5 - cents	0 (SMPI**) cents	129.5 - cents
1978	125.0 - cents	6.0 - cents	8.9 (SMPI) cents	139.9 - cents
1979	125.0 - cents	6.0 - cents	28.8 (SMPI) cents	159.8 - cents
1980	125.0 - cents	6.0 - cents	42.2 (SMPI) cents	173.3 - cents
1981	125.0 - cents	6.0 - cents	60.6 (SMPI) cents	191.6 - cents
1982	125.0 - cents	6.0 - cents	76.8 (SMPI) cents	207.8 - cents
1983	125.0 - cents	6.0 - cents	73.7 (SMPI) cents	204.7 - cents
1984	125.0 - cents	6.0 - cents	79.7 (SMPI) cents	210.7 - cents
1985	125.0 - cents	3.0 - cents	76.8 (SMPI) cents	204.8 - cents
1986	190.0 - cents	-0-	Frozen (IPD***)	190.0 - cents
1987	190.0 - cents	-0-	Frozen (IPD)	190.0 - cents
1988	190.0 - cents	-0-	Frozen (IPD)	190.0 - cents
1989	190.0 - cents	-0-	7.5 (IPD) cents	197.5 - cents
1990	190.0 - cents	-0-	♦7.5 (IPD) cents	197.5 - cents
1991	190.0 - cents	-0-	15.4 (IPD) cents	205.4 - cents
1992	190.0 - cents	-0-	♦15.4 (IPD) cents	205.4 - cents
1993	190.0 - cents	-0-	♦15.4 (IPD) cents	205.4 - cents
1994	190.0 - cents	-0-	♦15.4 (IPD) cents	205.4 - cents
1995	190.0 - cents	-0-	♦15.4 (IPD) cents	205.4 - cents

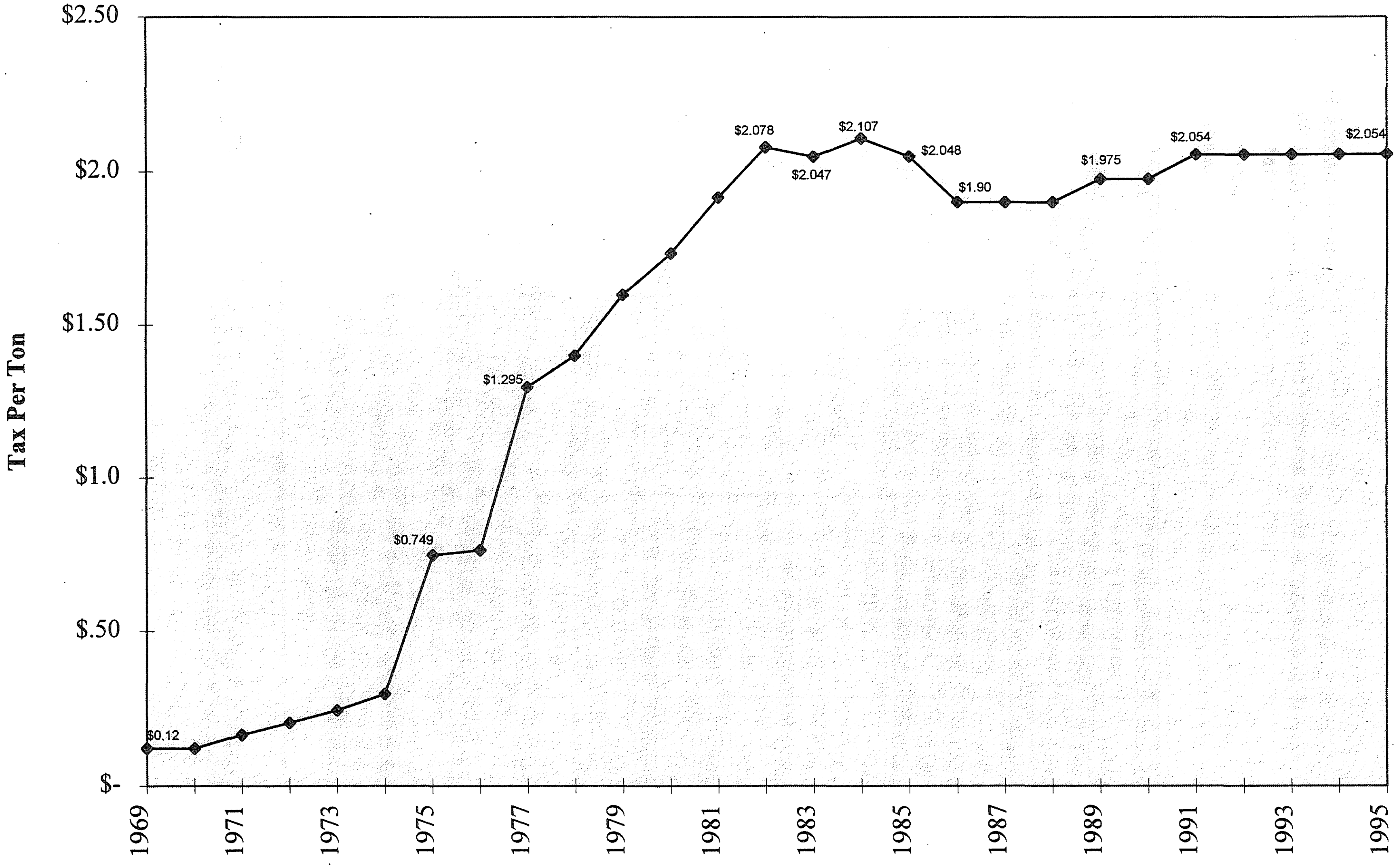
* Wholesale price index

** Steel mill products index

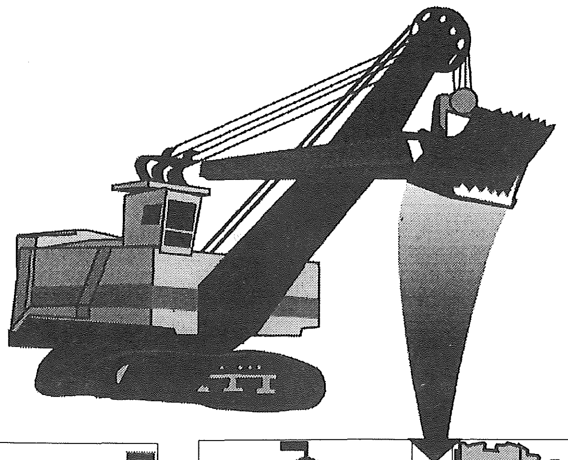
♦ *** Gross national product implicit price deflator

♦ In years following 1989 & 1991 where the inflation index is unchanged, it was frozen by legislative action

Production Tax Rate History



(Est. 1995 production payable in 1996)
DISTRIBUTION OF TACONITE PRODUCTION TAX



Total Taconite Production Tax

$86,645,102

Production Tax is $2.054 per taxable ton.

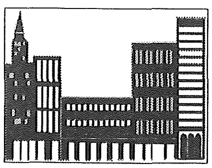
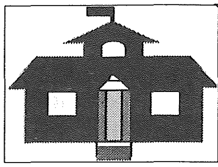
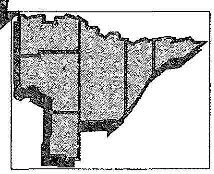
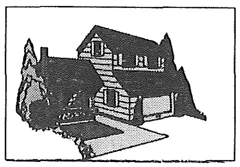
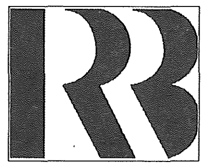
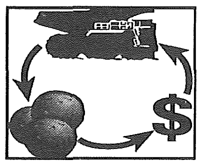
The three-year average taxable tonnage was 42,183,594

Less: School Bond Credits

-$928,006

Net Production Tax

$85,717,096

CITIES & TOWNSHIPS — $8,910,729
- City and Township Fund* — *$1,387,506*
- Taconite Municipal Aid* — *$6,932,081*
- Taconite Railroad — *$591,142*

SCHOOL DISTRICTS — $21,898,495
- School District $.055 Fund* — *$2,500,308*
- School $.22 Fund — *$9,686,019*
- Taconite Railroad — *$1,785,380***
- Taconite Referendum — *$4,923,657*
- School Bond Payments — *$3,003,131*

COUNTIES — $13,209,416
- Regular County Fund* — *$9,824,324*
- County Road & Bridge Fund* — *$2,600,715*
- Taconite Railroad — *$784,377*

PROPERTY TAX AND MISC. — $13,243,436
- Taconite Property Tax Relief — *$13,057,854*
- R.A.M.S.* — *$110,582*
- State of Minnesota — *$75,000*

I.R.R.R.B. — $21,280,927
- I.R.R.R.B. Fund* — *$2,822,766*
- I.R.R.R.B. Fixed Fund — *$1,252,520*
- Taconite Env. Protection Fund — *$12,560,818*
- N.E. Minnesota Economic Protection Fund — *$4,644,823*

TACONITE ECONOMIC DEVELOPMENT FUND — $7,174,093

Guarantee Fund
M.S. 298.225
M.S. 298.293

**35.2 cents-per-ton will be subtracted from STATE aids or levies a taconite school district would otherwise receive.

*Payments to the funds are guaranteed at a percentage level of the base year (1983) by M. S. 298.293 for property tax relief.

IMPACT OF INCREASED INVESTMENT TAX CREDIT

Estimated Taxable Tons (million)	N.E. Minnesota Economic Protection Trust Fund	Taconite Environmental Protection Fund	Investment Tax Credit	
			Cents/Ton	Total
39.5	$4,168,597	$11,028,328	15.4	$ 6,537,679
40.5	$2,490,739	$11,605,226	20.4	$ 8,740,352
41.5	$ 722,598	$12,189,053	25.4	$11,044,462
42.5	$ 354,774	$12,775,741	26.9	$11,980,584
43.5	$ 13,113	$13,409,694	28.4	$12,963,038
44.5	($414,287)	$13,977,908	29.9	$14,005,500
45.5	($830,914)	$14,619,914	31.4	$14,987,000