Fiscal Note

State of Alaska
2017 Legislative Session

Bill Version:	CSHB 111(FIN)
Fiscal Note Number:	3
(H) Publish Date:	4/9/2017

Identifier: HB111CS(FIN)-DOR-TAX-04-07-17
Title: OIL & GAS PRODUCTION TAX;PAYMENTS;CREDITS
Sponsor: RESOURCES
Requester: House Finance Committee

Department: Department of Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2018 Appropriation Requested	Included in Governor's FY2018 Request	Out-Year Cost Estimates				
OPERATING EXPENDITURES	**FY 2018**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**	**FY 2022**	**FY 2023**
Personal Services							
Travel							
Services							
Commodities							
Capital Outlay							
Grants & Benefits							
Miscellaneous							
Total Operating	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Fund Source (Operating Only)

None							
Total	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Positions

Full-time							
Part-time							
Temporary							

Change in Revenues

1250 UGF Rev (UGF)	20,000.0		85,000.0	90,000.0	100,000.0	145,000.0	190,000.0
Total	**20,000.0**	**0.0**	**85,000.0**	**90,000.0**	**100,000.0**	**145,000.0**	**190,000.0**

Estimated SUPPLEMENTAL (FY2017) cost: 0.0 *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY2018) cost: 1,200.0 *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? yes
If yes, by what date are the regulations to be adopted, amended or repealed? 01/01/18

Why this fiscal note differs from previous version:

Revised to reflect work draft House Finance committee substitute.

Prepared By:	Ken Alper, Director	Phone:	(907)465-8221
Division:	Tax Division	Date:	04/07/2017 01:00 PM
Approved By:	Jerry Burnett, Deputy Commissioner	Date:	04/07/17
Agency:	Department of Revenue		

REPORTED OUT OF HFC 04/08/2017

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2017 LEGISLATIVE SESSION

Analysis

Bill Background
This legislation would make multiple changes to Alaska's oil and gas production tax and tax credit statutes. Various credits have been added to statute since 2003, with state repurchase beginning in 2007. Through the end of FY 2016, about $8 billion in tax credits have been received by companies. This includes both credits used against tax liability and credits repurchased by the state; it also includes activity on both the North Slope and other areas of the state. A substantial number of companies rely on these credits to support and subsidize their Alaska operations. For work done in 2015, the producers earned credit certificates for up to 85% of the cost.

The Legislature passed HB247 in 2016. That bill was primarily focused on scaling back credits available in Cook Inlet. Those changes, combined with the sunset of most exploration credits that also occurred in 2016, reduces the state's estimates of future credit demand. Nevertheless, the volume of tax credit certificates eligible for state purchase continues to grow in part due to Governor Walker vetoing most of the FY2017 appropriation to the tax credit fund (AS 43.55.028). If annual appropriations continue according to the statutory formula, the current forecast indicates $1.6 billion in purchasable credits outstanding in 2026. Additionally, there have been several large discoveries recently announced on the North Slope; if any of these were sanctioned and built it could result in additional billions in credit liability that under current law could be payable far in advance of any additional tax or royalty revenue from the development.

With the changes made in this legislation, the state will cease offering transferrable or cashable tax credit certificates for work done on the North Slope. Instead, companies would be expected to carry forward their losses until such time as they owe a tax liability to the state, at which time they could be used to offset the company's oil and gas production taxes. Additionally, the state’s contribution towards many projects will be reduced. Additional provisions of the bill will increase the oil and gas production tax under certain circumstances.

Summary of Revenue Impact
The bill's fiscal impacts can be divided into two categories: increases to revenue (taxes), and reductions in the demand for tax credit repurchases (appropriations). The cover page table only includes the revenue items as it is impossible to predict future appropriations. Savings due to reductions in demand for future appropriations to purchase tax credits are noted in the summary table on page 4. The table shows the impact at forecasted oil prices. Additionally, the bar charts on page 5 examine the average total impact at a wide range of possible oil prices.

The initial revenue impact from this bill would be concentrated in changes to the base production tax and the per-taxable barrel credit. The tax rate is reduced from 35% to 25%, although a "bracket" of progressivity is added so that portion of production tax value greater than $60 per barrel would be taxed at 40%. At the same time, the sliding scale per-barrel credit of between $0 to $8 is repealed.

In general, this moves the "crossover point" between the gross minimum tax (unchanged in this version) and the net profits tax much lower- from roughly $75 per barrel to $55. The bill would result in a tax increase at oil prices between roughly $50 and $100 per barrel, and is roughly revenue neutral at higher prices.

Additionally, HB111 prevents certain credits from being used to reduce tax payments below the minimum tax, a concept colloquially known as "hardening the floor." This will have a smaller revenue impact that disappears in future years as the price of oil increases.

Also, a small indeterminate amount of additional revenue would come from the elimination of the "zero interest rate" provision after three years of production tax delinquency.

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STATE OF ALASKA **BILL NO.** HB111
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Analysis

Implementation Cost
The changes anticipated in this bill will require somewhat substantial reprogramming of the Tax Revenue Management System and Revenue Online tax portal. Based on the required changes after the passage of HB247 in 2016, we currently assume a one-time cost of about $1,200,000 to accomplish this. We do not anticipate any additional costs to administer the tax program. There will also be a need for substantial amendments to existing regulations to fully implement the changes.

Detail of Specific Provisions
1) Eliminates the 35% Carried Forward Annual Loss Credit (also known as "NOL") rate for the North Slope, effective 1/1/18. This change would eliminate reduce the future liability from this credit. Instead of the credit, taxpayers will be able to carry forward their excess lease expenditures to be used against future taxes. The value of carried forward expenditures begins to decrease by 10% per year if unused for seven years. Additionally, carried forward expenditures can only be used to offset revenues from the lease or property where they were originally incurred, a concept generally referred to as "ring fencing." This change would not impact the existing credit certificates, estimated at about $900 million that will be in company hands at the end of 2017 given no further action.

2) Hardens the floor, so no credits can be used to reduce payments below the minimum tax. An exception is made for the small producer credit

3) Production eligible for the gross value reduction (GVR) only pays a minimum tax based on 4% of their adjusted gross value, after subtraction of the GVR. This results in an effective 3.2% gross minimum tax on new oil.

4) The base tax rate for the North Slope is reduced from 35% to 25%; an additional 15% progressive surcharge is added to that portion of production tax value greater than $60 per barrel.

5) The sliding scale per-barrel credit on non-GVR oil is eliminated. This means that the calculated tax rate (25%, plus possible progressivity) and the effective tax rate will be the same.

6) The Gross Value at the Point of Production for a given property can’t go below zero. This would only impact a very high tariff (likely remote) field at very low prices, so those fields could not have negative wellhead value that could offset other tax liability.

7) Eliminates the zero interest rate for delinquent taxes that currently take effect after three years of delinquency. This provision was added in HB247 to incentivize DOR to accelerate the tax audit process. However, the larger concern is that it remains in effect for the entirety of any tax appeal or litigation, reducing any incentive on the part of companies to settle a tax issue.

8) The 30% Gross Value Reduction for high royalty fields on state land is eliminated. All GVR is limited to the 20% category.

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2017 LEGISLATIVE SESSION

BILL NO. HB111

Analysis

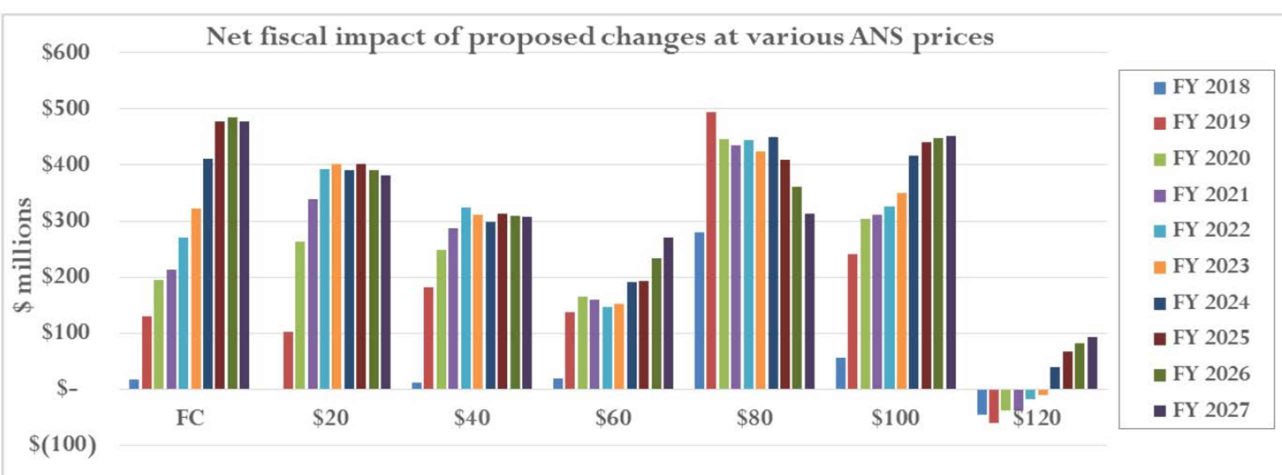
Provisions in CSHB 111 (FIN) \M and their Estimated Fiscal Impact based on Fall 2016 Forecast ($millions) - Fall 2016 FC PRICE

Revised 4-7-17 by Dept. of Revenue

Description of Provision	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
1. Effective 1/1/18, Operating loss credit eliminated for North Slope and replaced with carry-forward lease expenditures provision. A company may carry forward 100% of North Slope lease expenditures not deducted against tax, but can only use to offset gross value from the lease or property whre earned. After 7 years, carry-forward reduced by 10% of original value each year.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2. Only small producer credits can reduce tax below the minimum tax effective 1/1/18.	$20	$15	$0	$0	$0	$0	$0	-$10	-$25	-$5
3. Existing minimum tax rates retained, and GVR reduces basis for minimum tax, effective 1/1/18.	$0	$0	$0	$0	-$5	-$5	$0	$0	$0	$0
4. Effective 1/1/18, base tax rate for North Slope changed from 35% of PTV to 25%; an additional 15% progressive surcharge applies to that portion of PTV above $60 per barrel.	$0	-$10	-$10	-$15	-$20	-$20	-$35	-$45	-$60	-$70
5. Sliding scale per-taxable-barrel credits eliminated, effective 1/1/18.	$5	$210	$185	$250	$340	$405	$510	$610	$630	$620
6. Gross value at point of production (GVPP) cannot go below zero effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
7. Interest on delinquent taxes continues to accrue after 3 years, retroactive to 1/1/17.	Indeterminate - likely positive for state.									
8. Eliminate 30% GVR option effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Additional impact of implementing above provisions together vs standalone.	-$5	-$130	-$85	-$135	-$170	-$190	-$200	-$215	-$200	-$210
Total Revenue Impact	**$20**	**$85**	**$90**	**$100**	**$145**	**$190**	**$275**	**$340**	**$345**	**$335**
A. Budget impact of operating loss and carry-forward lease expenditures changes effective 1/1/18.	$0	$45	$105	$115	$125	$135	$135	$140	$140	$140
B. Budget impact of only small producer credits can reduce tax below minimum tax effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
C. Budget impact of minimum tax changes effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
D. Budget impact of North Slope tax rate changes effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
E. Budget impact of eliminating sliding scale per-taxable-barrel credits, effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
F. Budget impact of GVPP cannot go below zero effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
G. Budget impact of interest accrual changes, retroactive to 1/1/17.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
H. Budget impact of eliminating 30% GVR option effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Additional impact of implementing above provisions together vs standalone	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Total Budget Impact	**$0**	**$45**	**$105**	**$115**	**$125**	**$135**	**$135**	**$140**	**$140**	**$140**
Total Fiscal Impact - (does not include potential changes in investment)	**$20**	**$130**	**$195**	**$215**	**$270**	**$325**	**$410**	**$480**	**$485**	**$475**
Tax impact of carry-forward lease expenditure balances - current law	$14	$0	$0	$0	$0	$0	$0	$0	$0	$0
Tax impact of carry-forward lease expenditure balances - proposed	$90	$150	$225	$280	$335	$390	$455	$520	$580	$640
Change in year-end balance due to proposal	**$76**	**$150**	**$225**	**$280**	**$335**	**$390**	**$455**	**$520**	**$580**	**$640**

NOTE: The fiscal impact of this proposal is an estimate based on the Fall 2016 revenue forecast. **Estimates shown here are draft / preliminary based on our interpretation of possible changes, and do not include any changes in company behavior as a result of this proposal. We reserve the right to make modifications to estimates for any forthcoming fiscal notes.**

Net Fiscal Impact of CSHB111(FIN) \M at Various Prices



(Revised 1/11/17 OMB/LFD)