

STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

POUCH S - JUNEAU 99811

May 14, 1976

The Honorable Kathryn Poland
Chairman
Senate Resources Committee
Alaska State Legislature
State Capitol Building
Juneau, Alaska

Re: Senate Bill No. 699

Dear Senator Poland:

Senate Bill No. 699, an Act relating to the exemptions under the oil and gas reserves ad valorem tax, was introduced in the Senate on March 12, 1976 and was referred to the Senate Resources and Finance Committees.

For the records of the Senate Resources Committee, I am enclosing a copy of testimony given by Thomas K. Williams, Director, Petroleum Revenue Division, Department of Revenue, Anchorage, Alaska before the Senate Resources Committee on May 12, 1976 along with a copy of a memorandum from Mr. Williams to Frederick F. Boetsch, Deputy Commissioner, Department of Revenue concerning Senate Bill No. 699.

If you or any members of the Senate Resources Committee have any further questions on the testimony given on May 12, 1976 or on the material submitted, please telephone the writer at 465-2397 and I will contact Mr. Williams in Anchorage for further information.

Very truly yours,

R. D. Stevenson
Special Assistant

cc: The Honorable Bill Ray
Chairman
Senate Finance Committee

Thomas K. Williams
Director, Petroleum Revenue Division
Department of Revenue
Anchorage, Alaska

1776-A TRIBUTE FROM OUR STATE TO OUR NATION-1976"



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MEMORANDUM

State of Alaska

TO: R. D. Stevenson
Special Assistant
Department of Revenue

DATE: May 12, 1976

FILE NO:

TELEPHONE NO:

FROM: Thomas K. Williams *TKW*
Director
Petroleum Revenue Division

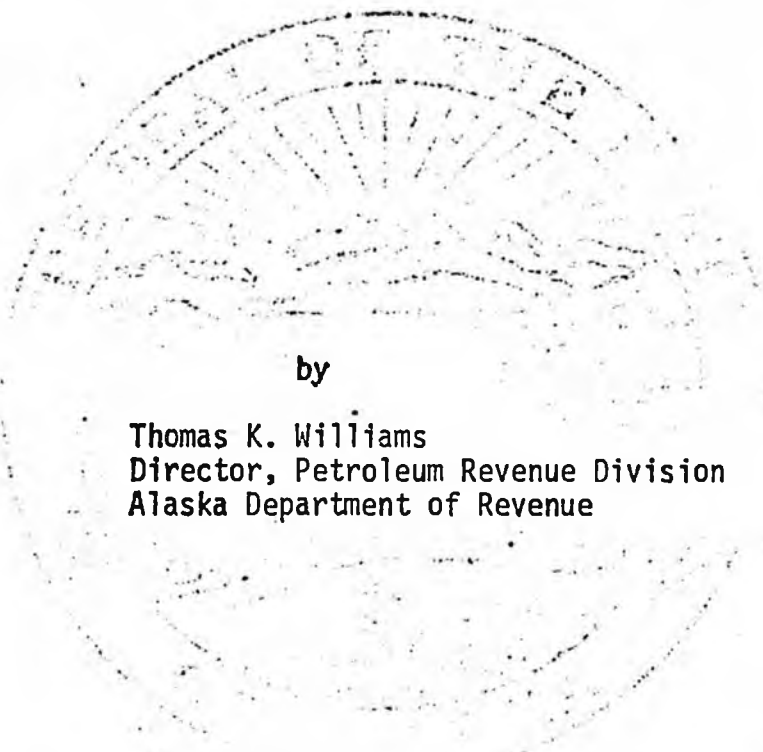
SUBJECT: SB 699

In response to your earlier request for a review of SB 699, please find attached a copy of my memorandum of April 29, 1976 to Frederick P. Boetsch and a copy of my testimony of May 12, 1976 to the Senate Resources Committee regarding this Bill.

Attachments

TKW:tw

TESTIMONY
BEFORE
THE SENATE RESOURCES COMMITTEE
CONCERNING
SENATE BILL 699



by

Thomas K. Williams
Director, Petroleum Revenue Division
Alaska Department of Revenue

May 12, 1976

Madame Chairman, Members of the Committee:

Thank you for the opportunity to testify to you today about Senate Bill 699. For the record let me first state that my name is Thomas K. Williams and that I am the director of the Petroleum Revenue Division, Alaska Department of Revenue.

SB 699 seeks to exempt from reserves tax all oil or gas reserves committed to a public utility regulated by the Alaska Public Utilities Commission. It has been prompted by Alaska Gas and Service Company (AGAS), the gas utility serving Anchorage, as a measure to "protect" the utility from the effects of the reserves tax. I have discussed these effects several times with representatives of AGAS. Frankly, this Bill is an over-reaction to an exaggerated problem, and I am whole-heartedly opposed to it.

I have been told by both AGAS and members of the Public Utilities Commission that the Commission will allow AGAS and other utilities (such as the one for the City of Kenai) to pass their full reserves tax costs on to their customers through rate increases. Thus the utility will not itself absorb any of the actual tax. Its only problem, if it may be called that, will be the minor bookkeeping necessary to keep track of the credit against production tax that accrues from reserves tax payments. The cost of the production tax is already largely passed through to the gas customer (all but the first one percent), so AGAS would be monitoring this credit in order to know when to seek a rate increase to reflect the rise in production tax from half to its full amount when the credit from the reserves tax payments is depleted.

Moreover, the cost passed through to the consumer will be very small. We estimate that a net reserves tax of approximately \$1,077,000 will be paid this year for all taxable gas reserves in the Kenai gas field, the source of the gas for AGAS and the Kenai utility. Assuming the reserves

tax will be passed on to the utilities in proportion to the percentage of taxable gas reserves of the field that are committed to them respectively, then 23.92% of the net reserves tax (or \$257,600) would pass through to AGAS and thence to Anchorage consumers. Similarly, 1.43% of the tax (or \$15,400) would be passed on to consumers in the City of Kenai. The contract for AGAS's supply has a "take or pay" provision for 26.28 million Mcf of gas annually through 1985. Assuming this volume is delivered to AGAS, the cost of the 1976 reserves tax is only 0.98 cent per Mcf. The average residential user in Anchorage buys 200 to 230 Mcf per year, so the annual cost during the two-year life of the reserves tax would be \$1.96 to \$2.25. The cost to Kenai gas users would be 3.21 cents per Mcf.

By contrast it should be noted that AGAS has been authorized by the Public Utilities Commission over the last two years to raise its rates by more than 20-1/2 cents per Mcf, and it has sought but been denied even greater increases. Compared to these, the reserves tax is a small cost. And of course, Alaska residents (not temporaries) would eventually recover even these modest costs of the reserves tax through lower utility rates during the time the accrued credit is applied against production taxes.

Since all gas not committed to utilities goes Outside (either as LNG or fertilizer), the Bill could subject the reserves tax to constitutional challenge either as discriminating against interstate and foreign commerce or as violating the Equal Protection Clause.

Inasmuch as the "problem" involved is largely illusory and the reserves tax is indispensable to the State's financial solvency in Fiscal Year 1977, it is clear to me that any benefit that SB 699 may have to offer is greatly outweighed by the risks it carries. Therefore, I am opposed to this Bill and urge the Legislature not to seek its enactment.

Thank you.

MEMORANDUM

State of Alaska

TO: Frederick P. Boetsch
Deputy Commissioner, Taxation
Department of Revenue

DATE: April 29, 1976

FILE NO:

TELEPHONE NO:

FROM: Thomas K. Williams
Director
Petroleum Revenue Division

SUBJECT: SB 699
(amending the reserves tax)

SB 699 would exempt from reserves tax all gas reserves committed for purchase by a utility. It has been introduced at the request of the Anchorage gas utility to "protect" the utility from the effects of the tax. Frankly, this bill is an overreaction to an exaggerated problem.

It is my understanding that the Public Utilities Commission will allow the utilities to pass the reserves tax cost through to their customers. Thus the utility will not itself absorb any of the tax.

The cost passed through to the consumer will be very small. We estimate a net reserves tax of approximately \$1,077,000 will be paid this year for all taxable gas reserves in the Kenai gas field (the source of gas for the Anchorage and Kenai gas utilities). Assuming the reserves tax will be passed on to the utility in proportion to the percentage of taxable gas reserves of the field that are committed to the utility, 23.92% of the tax (or \$257,600) would pass through to Anchorage gas consumers and 1.43% (or \$15,400) to Kenai gas consumers. The Anchorage utility's contract has a "take or pay" provision for 26.28 million Mcf of gas annually through 1985. Assuming this volume is delivered to the utility, the annual cost of the 1976 reserves tax that is passed on to Anchorage gas users is 0.98 cent per Mcf. The average residential user in Anchorage buys 200 to 230 Mcf per year, so the annual cost during the 2 year life of the tax would be \$1.96 to \$2.25. About 480,000 Mcf a year are sold to the City of Kenai's utility, so the passed-through reserves tax is a cost of 3.21 cents per Mcf (\$6.42 to \$7.38 annually) to Kenai users.

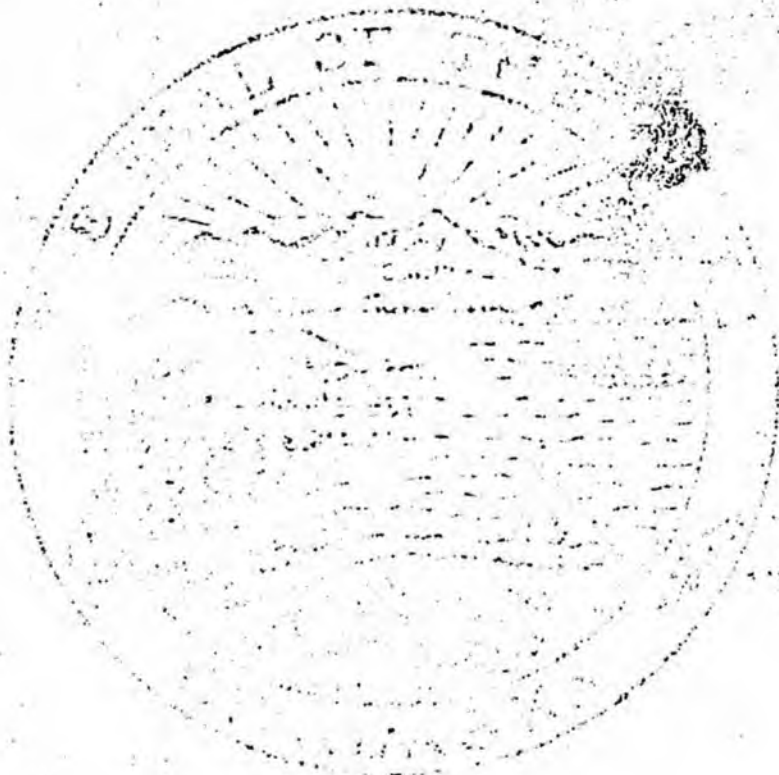
By contrast it should be noted that the Anchorage gas utility has been authorized to raise its rates by over 20 cents per Mcf over the last two years (\$40 to \$46 annually to the residential user in Anchorage), and it has sought but been denied even greater increases. Compared to these the reserves tax cost is slight. And of course Alaska residents would recover even the modest cost of the reserves tax because of the credit against future years' production tax which is also passed through.

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Since all gas not committed to utilities goes Outside (either as LNG or fertilizer), the bill could subject the reserves tax to constitutional challenge either as discriminating against interstate and foreign commerce or as violating the Equal Protection clause. Since the "problem" from taxing the reserves committed to utilities is largely illusory and since the reserves tax is indispensable to the State's solvency in FY77, it seems clear to me that any benefit SB 699 may have to offer is greatly outweighed by the risks it carries.

TKW:dh



Introduced: 3/12/76
Referred: Resources and
Finance

1 IN THE SENATE

BY THE RULES COMMITTEE
BY REQUEST

2 SENATE BILL NO. 699

3 IN THE LEGISLATURE OF THE STATE OF ALASKA

4 NINTH LEGISLATURE - SECOND SESSION

5 A BILL

6 For an Act entitled: "An Act relating to the exemptions under the oil and
7 gas reserves ad valorem tax."

8 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

9 * Section 1. AS 43.58.020 is amended by adding a new paragraph to read:
10 (5) any oil or gas reserves committed to or produced for use
11 or resale by public utilities which are regulated by the Alaska Public
12 Utilities Commission.
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