

SCR

58

STATE OF ALASKA  
OFFICE OF THE GOVERNOR  
JUNEAU

January 12, 1982

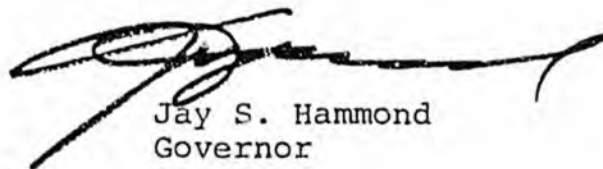
The Honorable Jalmar Kerttula  
President of the Senate  
Alaska State Legislature  
Pouch V  
Juneau, Alaska 99811

Dear Mr. President:

Under the authority of art. III, sec. 18, of the Alaska Constitution, I am transmitting a resolution which proposes a constitutional amendment regarding contributions to the permanent fund. The amendment would add proceeds from severance or production taxes to the list of revenue sources.

While the tax presently imposed under AS 43.55 is often referred to as a "severance tax," it is not clear whether the Alaska Supreme Court would find that it is a severance tax. See Liberati v. Bristol Bay Borough, 584 P.2d 1115 (Alaska 1978). I have therefore included both production and severance tax proceeds in the proposed amendment.

Sincerely,



Jay S. Hammond  
Governor

# STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

## DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

POUCH 5  
JUNEAU, ALASKA 99811

February 1, 1982

The Honorable Bob Mulcahy, Chairman  
Senate Labor and Commerce Committee  
Pouch V  
Juneau, AK 99811

Re: Senate Joint Resolution No. 58

Dear Senator Mulcahy:

At the present time 25 percent of all mineral lease rentals, royalties and royalty sale proceeds are explicitly dedicated under the State Constitution to the Permanent Fund. The Constitution also allows the Legislature by statute to increase this percentage, which it has done for the royalty revenues from the Beaufort Sea leases and for bonus bids received for oil and gas lease sales held after 1979. In addition, the Legislature may make special appropriations to the Permanent Fund, as it has done the past two sessions.

The problem with the dedication of 50 percent of future bonuses and royalties from the Beaufort Sea and other new oil and gas production is that it is statutory in origin. That is, what one Legislature enacts another Legislature may repeal. Thus, while it appears that 50 percent of those one-time-only revenues will be going into the Permanent Fund, it remains possible that future Legislatures could change this or repeal it altogether, in which case the 25 percent minimum under the Constitution would again apply.

At present these constitutionally mandated contributions represent about 10 percent of the State's total revenues derived from oil and gas development. This is because the State's royalties are slightly less than half of the total petroleum revenues; the balance is from taxes on the oil and gas industry. By far the largest of these taxes is the State's Oil and Gas Properties Production Tax (AS 43.55), which is generally referred to as the "severance tax" even though it calls itself a "production tax" in its title.

The difference between a severance tax and a production tax is nearly metaphysical. Both are taxes imposed on the activity of extracting and removing a valuable resource from the ground. However, a

Senator Bob Mulcahy (Re SJR 58)

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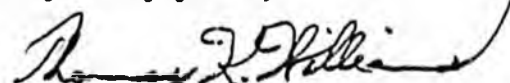
severance tax, strictly speaking, is imposed on the actual act of severing the mineral from the ground in its natural condition as it emerges or is severed. A production tax is imposed on the reduction of the resource to actual possession in a condition of marketability, which may or may not be the same as its natural condition when the mineral is severed. In the case of oil and gas, the processes of cleaning and dehydration, of separating oil from any water and gases in it, of separating the gas from any condensable liquids in it, etc. are all conducted as part of the "production" process. Thus, the comparatively slight amounts of oil or gas that are consumed, used or lost in the course of these "production" operations would not be counted in determining the taxable volume of the oil or gas for purposes of a "production" tax. In contrast, such oil and gas would be included in determining the taxable volumes of each under a "severance" tax.

Happily, for the sake of keeping things straight, our Oil and Gas Properties Production Tax really is a "production" tax, as opposed to a "severance" tax. However, as I indicated, the distinction between these types of taxes is relatively minor for most purposes.

Senate Joint Resolution No. 58 refers both to production taxes and to severance taxes because of the similarity between these kinds of taxes. The clear intent of the Resolution is to amend the Constitution so that the Permanent Fund will receive at least one-quarter of the one-time-only tax revenue collected by the State from the activity of extracting and removing mineral resources from the ground, regardless whether the Legislature retains the present "production"-type tax structure or changes over someday to a "severance"-type tax structure. It might also develop that the "production"-tax approach is retained for oil and gas, but that future taxes someday enacted for other kinds of mineral extraction would be of the "severance"-tax type. By referring to both kinds of tax, the Resolution will ensure that at least a quarter of the revenues from both kinds of extraction-based taxes will be dedicated to the Permanent Fund.

I hope this will assist you in your consideration of SJR 58. Please do not hesitate to contact me if you have any further questions on this matter.

Very truly yours,



Thomas K. Williams  
Commissioner of Revenue

TKW:tw

cc: Governor Hammond