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Offered: 4/9/86
Referred: Finance

Original sponsor: Fuller

1 IN THE HOUSE

BY THE COMMUNITY AND
REGIONAL AFFAIRS COMMITTEE

2

CS FOR HOUSE BILL NO. 546 (C&RA)

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

4

FOURTEENTH LEGISLATURE - SECOND SESSION

5

A BILL

6

For an Act entitled: "An Act relating to the capital and the taxation of

7

Native corporations."

8

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

9

* Section 1. AS 10.05.005(a) is amended to read:

10

(a) A corporation organized under 43 U.S.C. 1601 - 1628 (Alaska

11

Native Claims Settlement Act), except a village corporation which may

12

be incorporated under either this chapter or AS 10.20, shall be incor-

13

porated under and is subject to this chapter, except

14

(1) each corporation shall issue without further considera-

15

tion the number of shares of common stock necessary to comply with the

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requirements of the Alaska Native Claims Settlement Act and all stock

17

so issued is considered fully paid and nonassessable when issued;

18

(2) unless otherwise provided in the articles of incorpora-

19

tion approved by the secretary of the interior,

20

(A) the capital is considered the consideration for

21

the initial issuance of shares; and

22

(B) the capital of a corporation organized under 43

23

U.S.C. 1601 - 1628 includes

24

(i) the land or interests in it conveyed to the

25

corporation by the United States under the federal Act,

26

except that which is required to be conveyed under 43 U.S.C.

27

1613(c)(1), (3), and (4), entered at its fair value to the

28

corporation upon receiving the conveyance of it; and

29

(ii) the money, when received under 43 U.S.C.

1 1605, 1606(i), and 1608, that [WHICH] is retained by the
2 corporation and that [WHICH] is not immediately distributed
3 or required to be distributed under 43 U.S.C. 1606(j).

4 * Sec. 2. AS 43.20.031 is amended by adding a new subsection to read:

5 (j) The department shall apply the exception contained in sec.
6 60(b)(5) of P.L. 98-369 (Deficit Reduction Act of 1984) to a consoli-
7 dated return filed by a Native corporation under this chapter. In
8 this subsection, "Native corporation" means a corporation organized
9 under 43 U.S.C. 1601 - 1628 (Alaska Native Claims Settlement Act).

Introduced: 2/5/86
Referred: Community & Regional
Affairs and Finance

1 IN THE HOUSE

BY FULLER

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14 (1) each corporation shall issue without further considera-
15 tion the number of shares of common stock necessary to comply with the
16 requirements of the Alaska Native Claims Settlement Act and all stock
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18 (2) unless otherwise provided in the articles of incorpora-
19 tion approved by the secretary of the interior,

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21 the initial issuance of shares; and

22 (B) the capital of a corporation organized under 43
23 U.S.C. 1601 - 1628 includes

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25 corporation by the United States under the federal Act,
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5 (j) The department shall apply the exception contained in sec.
6 60(b)(5) of P.L. 98-369 (Tax Reform Act of 1984) to a consolidated
7 return filed by a Native corporation under this chapter. In this
8 subsection, "Native corporation" means a corporation organized under
9 43 U.S.C. 1601 - 1628 (Alaska Native Claims Settlement Act).

Comply w/1984 tax law.

HB 546

I appreciate the opportunity to appear before the committee today. I'd like to briefly go through the provisions of HB 546 and then have you hear the testimony of ^{Janie Lusk} AFN and Mr. Beattie of Peat, Marwick, who will be able to answer any questions you may have about the intricacies of federal tax law.

Section 1

The first section of the bill amends state law to define the 7(i) revenues received by Native Regional Corporations as contributions to a corporation's capital. The reason for this change is to ensure that the intent of ANCSA to equally distribute the earnings from resource development revenues among all Alaska Native Corporations is met; under current law this is not possible due to manner in which the depletion allowance for resource extraction is computed.

Section 2 *can take losses against profit*

Section 2 has been added to the legislation to make state law consistent with federal law. Because state tax regulations reference the internal revenue code, it may not be technically necessary to include this provision, but we have done so on the advise of Mr. Beattie of Peat Marwick.

Thank you.

Jack Fuller



Peat, Marwick, Mitchell & Co.
Certified Public Accountants
Alaska Mutual Bank Building
601 West 5th Avenue, Suite 700
Anchorage, Alaska 99501

March 22, 1986

MAR 31 RECD

Representative Jack Fuller
Pouch V
Juneau, Alaska 99611

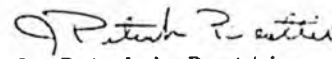
Dear Representative Fuller:

Attached is a memorandum regarding the explanation behind the proposed changes to the corporate statutes and the revenue statutes for Alaska native corporations. Hopefully, this will be of help to you as you progress on the bill. Please call me if you have any questions.

Thank you for your help in this matter.

Very truly yours,

PEAT, MARWICK, MITCHELL & CO.


J. Patrick Beattie, Partner

JPB:SKH

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date 3/24/86

REQUEST

Bill/Resolution No: HB 546
Title: Taxation of Native Corporations

Sponsor: Fuller
Requestor: (H) C & RA
Date of Request: March 24, 1986

FISCAL DETAIL

Agency Affected: Department of Revenue
BRU: Audit

Components:
Audit Division

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 86	FY 87	FY 88	FY 89	FY 90	FY 91
OPERATING						
100 PERSONAL SERVICES	-0-	-0-	-0-	-0-	-0-	-0-
200 TRAVEL	-0-	-0-	-0-	-0-	-0-	-0-
300 CONTRACTUAL	-0-	-0-	-0-	-0-	-0-	-0-
400 SUPPLIES	-0-	-0-	-0-	-0-	-0-	-0-
500 EQUIPMENT	-0-	-0-	-0-	-0-	-0-	-0-
600 LANDS & STRUCTURES	-0-	-0-	-0-	-0-	-0-	-0-
700 GRANTS, CLAIMS	-0-	-0-	-0-	-0-	-0-	-0-
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TOTAL	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS:

FULL-TIME	-0-	-0-	-0-	-0-	-0-	-0-
PART-TIME	-0-	-0-	-0-	-0-	-0-	-0-
TEMPORARY	-0-	-0-	-0-	-0-	-0-	-0-

ANALYSIS: Please see attached.

Prepared By: Steven E. Kettel
Division: Audit Division

Phone: 465-2343
Date: March 24, 1986

Approved by Commissioner: [Signature]
Agency: Revenue

Date: 3/25/86

Distribution (by Agency preparing fiscal note):

- Legislative Finance
- Legislative Sponsor
- Requestor
- Office of Management and Budget
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Fiscal Note
HB 546

Analysis:

This bill has two provisions affecting Native corporations organized under the Alaska Native Claims Settlement Act. (ANCSA).

- I. Section I amends AS 10.05.005(a) to allow Native corporations to treat as a contribution to capital all distributions made to it under section 1606(i) of ANCSA. These distributions, commonly referred to as "(7)(i)" distributions are currently required to be reported in each recipient corporation's income for tax purposes. This legislation will therefore change the character of the distribution.

It is not possible to estimate the revenue impact this bill will have. Revenue loss would depend upon the Regional and Village corporations' overall profitability and, of course, upon the continued availability of distributable income from the sale of non-renewable resources from Native lands.

- II. Section II of the bill gives Native corporations special treatment under Alaska tax law, identical to that bestowed upon them at the federal level. As Alaska corporate tax law currently adopts the special federal provisions which this bill attempts to recognize, section II of the bill is entirely unnecessary. The intent of this section is apparently to leave no doubt that the special privilege allowed by federal income tax law is also allowed at the State level.

IRC Section 1504(a) was amended in 1984 to tighten up the rules which allow corporations with large net operating losses to, in effect "sell" those tax losses to profitable non-Native corporations. The amendment specifically exempts Native corporations organized under ANCSA from the provision, thereby allowing them to continue to utilize their net tax losses in business ventures with profitable corporations.

Although it is not possible to estimate the impact this federal provision has on Alaska state revenues, several inferences can be made:

1. Native corporations will more quickly utilize their losses and become subject to Alaska tax;
2. Non-native corporations acquiring these losses will benefit by paying less federal and state income tax, thus freeing up more capital for additional investment in the state;
3. Corporations organized and doing business outside Alaska may also acquire the net operating losses to shelter their federal taxable income. If they are not doing business in Alaska, no revenue impact would result.

Jack Fuller Testimony

I appreciate the opportunity to appear before the committee today. I'd like to briefly go through the provisions of HB 546 and then have you hear the testimony of AFN and Mr. Beattie of Peat, Marwick, who will be able to answer any questions you may have about the intricacies of federal tax law.

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Peat, Marwick, Mitchell & Co.
Certified Public Accountants
Alaska Mutual Bank Building
601 West 5th Avenue, Suite 700
Anchorage, Alaska 99501

March 22, 1986

MAR 31 RECD

Representative Jack Fuller
Pouch V
Juneau, Alaska 99611

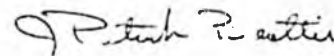
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Thank you for your help in this matter.

Very truly yours,

PEAT, MARWICK, MITCHELL & CO.


J. Patrick Beattie, Partner

JPB:SKH

March 22, 1986

Memorandum for Record:

Alaska Native Legislation

A House bill has been proposed by Representative Jack Fuller regarding two items relating to the taxation of native corporations. The purpose of this memorandum is to provide an explanation for those items and a discussion behind the purpose of the legislation.

The first item proposed is the change to revenue statute AS 43.20.031 which recognizes the Federal consolidated exception allowable to Alaska native corporations. The purpose behind this amendment is to ensure that Alaska taxation follows Federal with regard to native consolidated loss transactions. The exceptions provided in the Federal legislation allow Alaska native corporations to file consolidated returns under the rules in existence prior to the changes of the Tax Reform Act of 1984. The revenue statutes for Alaska already indicate that they recognize Federal consolidated filings and the purpose behind the legislation is to merely emphasize the fact that the State will also recognize the Federal exception.

The net effect of the recognition and the transactions, which are anticipated to be entered into by native corporations in the current year, should be minimal to Alaska taxation. The reason for this is the fact that the majority of income that would be sheltered for Federal purposes would, in all probability, come from outside the State of Alaska and not have been subject to taxation otherwise. The utilization of this income to offset the Alaska loss carryforwards will have the effect of accelerating revenue payments to the State of Alaska once the losses are utilized.

The second piece of legislation is a bit more complicated than the first part. However, the second part merely is a reversion back to the law for corporate structure that existed prior to 1981. This is the capital formation provision that treated Section 7(i) receipts by a native corporation as contributed capital. The provision was changed in 1981 because of a concern that native corporations could not make distributions of 7(i) to their shareholders since it was considered, for State law purposes, to be contributed capital. If this is still a concern, it is recommended that it be addressed by simply allowing native corporations to distribute contributed capital to the extent of 7(i).

The rationalization behind the desired change is founded in the overall intent of ANCSA. When the historical land claim settlement was reached, the Federal government recognized in Section 21(c) of the Act the need to provide for an exemption from taxation on the overall settlement. To the extent moneys and land were received by native corporations, they were not subject to any Federal or State taxation. The mechanics of this were to provide a basis allowance equal to fair market value on the receipt of any land. The problem then came with regard to the provisions enacted by Section 7(i) of the Act which provided for a revenue sharing allocation among the various corporations, giving recognition to the fact that there could be substantial variances in the value of resources received in a particular region.

Memorandum for Record
Alaska Native Legislation
March 22, 1986
2

The overall intent, as indicated in the basis provision, was to allow for the receipt of land and the conversion of its resources to be exempt from taxation. While this is a fairly straight-forward concept, the accounting problems which surfaced as a result of the revenue sharing provision created substantial difficulties. A regional corporation which receives land and extracts subsurface estate is obligated to share the subsurface estate with other regions. If the receipt of the subsurface estate by the other regions under Section 7(i) were taxable, it would defeat the intent of the overall settlement itself. However, the tax rules and regulations regarding depletion did not directly allow for a receiving corporation to be entitled to an outright basis deduction. Therefore, in order to implement the intent of ANCSA, the easiest method appears to be having the amounts received under Section 7(i) as contributed capital and thus eliminate the need for complex calculations and substantial disagreements.

Accordingly, it was recommended that the statutes be revised back to their previous form so that for State law purposes, amounts received under Section 7(i) will be considered contributed capital and exempt in accordance with the intent of ANCSA. As native corporations currently are paying extremely little amounts of taxation to the State due to their net operating loss carryovers, this provision is not anticipated to have a substantial revenue effect, if any, to the State.

J. P. Smith

TELEPHONE CONVERSATION WITH PAT BEATTIE, BSNC
MARCH 14, 1986

Present: John Halterman
Bob Berry
Pat Norman

BEATTIE: We have Bob, Pat and John there, right?

HALTERMAN: That is correct.

BEATTIE: Okay, I am in the office here in Anchorage and I also have Mike Stone with me. Mike is a tax partner, like myself, and our specialty is working with the Native Corporations both regional and village. I felt it would be helpful to have Mike in here as well.

To start off in addressing, I think there is two provisions of the bill and let's separate them and dispense with the easy one first, as far as the rationalization part, and that is the consolidation provision.

BERRY: I was hoping they were both going to be easy.

BEATTIE: Well, they are fine as far as I am concerned.

The consolidation provision is something that technically may not even be needed. It is just a clarification because of changes we are doing to the internal revenue code at the federal level, to make sure there is no miss communication with regards to the State's application of federal law. For federal purposes we have already achieved a change in the Deficit Reduction Act of '84, which allows Alaska Native corporations to file under the old consolidated rules. We have a draft of technical report language that is being submitted in the Tax Reform Bill of '85, in Washington. That will help further clarify that consolidation provision, and what is being proposed for the State is simply to recognize what ever is recognized for federal purposes. In other words, to follow it. There is an argument that you don't even have to do that because that is what the State statutes say, but just to make sure there is no confusion on it, and that Native companies which are allowed file consolidated tax returns and utilize their net operating loss position for federal purposes, will also be allowed to do it for state tax returns.

HALTERMAN: Practically, as I understand what that means, is that if you have five subsidiaries and four of them are operating at a profit and one of them is operating at a loss you can use that loss to shelter the profits by filing a single return.

Is that basically it?

BEATTIE: That is basically it, the standard consolidation provision. What makes it different, is for federal purposes now, and it is also for state, is that the requirements for ownership of those subsidiaries have changed. But they have changed for corporations other than Native corporations. Native Corporations are subject to the old rules under the internal revenue code.

HALTERMAN: Now, there is a statutory time limit is there not, for being able to transfer the net operation losses?

BEATTIE: Yes, it is tied into the enablement issue of the stock under 7(h).

HALTERMAN: So, 1991 is the last year, tax year, that they will be able to use this.

BEATTIE: That is correct.

HALTERMAN: I see.

BEATTIE: So, that in a nut shell is really kind of the sole purpose behind the consolidation provision being requested for the State. To just make sure it is in line with the federal, which is consistent with all other applications of state law, at least with regard to taxation. They simply reference the internal revenue code and use that as a source for authority.

HALTERMAN: Let me ask you kind of an ancillary question then, Pat, and go over this again. The sale of the net operating losses, now have any village or regional corporation in the State actually sold those losses to date?

BEATTIE: Yes.

HALTERMAN: I see, and these were to domestic in state Alaska corporations?

BEATTIE: Some, yes.

HALTERMAN: So, it is a mixture, and there is a viable market for selling your net operating losses?

BEATTIE: That is correct. There certainly is.

BERRY: Do I need to understand that? Because I don't. I mean the question of selling losses. This is Bob Berry.

BEATTIE: Okay, yeah, Bob, it is a misnomer to say selling losses. Although, from a practicality aspect that is what it is. The utilization of the consolidate filing allows the Native

corporation which has operating loss carry overs and can not issue any of its own stock to acquire an ownership interest in another corporation which is profitable, and to use their losses to observe the income of that other corporation.

BERRY: Okay, that I understand a little better than just the term selling losses. John mentioned this before. Maybe a week or so ago, I said don't tell me now if I don't need to know. So when it came up again, that is a little more helpful.

HALTERMAN: I think what you need to know is that other corporate entities can benefit from this provision besides Alaska Native regional and village corporations. Is that correct?

BEATTIE: That is correct. It is not restricted within Alaska.

HALTERMAN: And also that not only out of state but domestic Alaskan corporations have benefited by this provision to the extent then, freeing up their own capital for additional investment and business purposes in the state of Alaska.

BEATTIE: That is correct.

HALTERMAN: So, that is the positive side to it. Right?

BEATTIE: Then from the point of view of the other corporations outside the state of Alaska the issue with regard to revenue is relatively moot because the profit that is earned outside the state of Alaska, which is being absorbed for federal income tax purposes by the Native corporations, would never have been subject to tax in Alaska anyway.

HALTERMAN: Pat (N), do you have any questions on that? Okay, let's go on to 7, (i) then.

BEATTIE: 7(i), is a much more difficult concept. Maybe I shouldn't preface it that way. Maybe it isn't. But, it has always been a difficult one to rattle with, and it is something that I think is a typical result of ANCSA. That ANCSA was not extremely well thought out in its accounting applications, okay, and the reason for that is that the purpose behind ANCSA was that the Native corporation would receive their land, and in receiving their land would not be subject to taxation on them, and this was the essential provision under Section 21(c) of ANCSA, which provided that companies would receive a basis on their land equal to fair market value on the date that they received it. Okay, and that fair market value related to not only the surface estate of the land but also the subsurface. Well, that was fine because if you forget about 7(i). Okay, in its normal context what that means is a company is formed under this federal act ANCSA which allows it to receive land, and the

disposition of that land, be it the subsurface or the surface interest, would not give rise to taxation. In other words, that they would not be subject to tax on the receipt of their land or the disposition of it. That was the entire fair market value basis concept, and it works very well if you look at just one corporation, and you forget about 7(i). However, 7(i) provision, which I am sure you gentlemen are more aware than even myself, was a provision stated, which recognized the discrepancies in the values of the land received by different regional corporations, and provided the mechanism for sharing which is relatively unique in tax law, so that the subsurface estates received by various corporations would be shared with all the other corporations. Well, that net policy as translated doesn't give rise to the same type of tax deductions that you would normally get because there is no basis in resource revenue received by other corporations under 7(i). The only one entitled to the basis, technically is the land owning corporation itself, the regional corporation. So, the purpose behind requesting this reinstatement of the corporate statute, that was already there, is to eliminate the problem of 7(i) essentially being taxed, when it was in our minds never intended to be taxed, because it could have been offset by depletion deduction. The accounting concept of getting those depletion deductions over to where the revenue is actually being received, is something that is unworkable under federal law because it is a concept that never really has arisen before the 7(i) concept, and there may be many ways to address the problem. But, in our minds, the easiest way, which prevents all sorts of accounting nightmares, is to simply provide for a method that the 7(i) itself is considered a contribution of capital, which is no more different then when regional corporations and village corporation originally received their land as part of their capitalization.

BERRY: Would you tell me in what sense of the word are you, what sense are using basis? I don't understand that. You are talking about assigning of basis to fair market value?

BEATTIE: Yes, that is Section 21(c) of the Native Claims Settlement Act.

HALTERMAN: What basis is, Pat, is an initial evaluation of properties, is what you are saying?

BEATTIE: Yes, and it was amended by the d(2) legislation that says that; let's say if you are Sealaska, if you are a Southeast village corporation, you have got an easier time of it for evaluation purposes because you select land, and you can do a timber cruise, and you can say this is what the land is worth, and this is amount of timber on it, and this is fair market value. Okay, but if you are an Arctic slope type

corporation or if you have a subsurface estate that you really don't know what is down there, then you run into problems. How do you value it? The d(2) legislation addressed that also. They said that basis would be fair market value on either the date of receipt or the date that property is first commercially developed, if that is greater. So, going back to the concept of establishing that basis, you would, say that you select an acre of land in 1971, when you are formed, and that land has an speculative value because it is up on the north slope, and it is a hundred dollars, and 1986 you find out that there is a substantial oil reserve under that land. Then when you drill and establish that reserve, in as far as how much oil is there, and then start to take it out, you are entitled to higher basis at that point in time. In other words, fair market value on date of first commercial development, and this is the principle behind the taxation provision of ANCSA, which essentially says that a Native corporation should not be taxed on the receipt or conversion of their land.

HALTERMAN: And the net affect of that is reducing your capital gain. Is that right?

BEATTIE: Reducing your basis, that is correct. In other words, it would be cost depletion to the Native corporation that owns the land. But to any one else it would be nothing. Unless we had the 7(i) provision in there.

HALTERMAN: Okay. Now, I guess, I had to step out of the room for a minute, but, then did you explain how the proposal here by defining the contributions as, the 7(i) payments as contributions to capital, extends that benefit and the concept of equality and distribution of assets to other recipients of the funds.

BEATTIE: I think so. If you step back, and say that if you could collapse all the corporations, because that is essentially what 7(i) does, I mean it shares everything. If you could collapse all the corporations, they would receive resource revenue, and they would be entitled to a cost depletion deduction, which is consistent with the basis intent of ANCSA, which says they should not be paying tax on this. Well, if you extend the corporation and say; well, okay accountants, tell us what our depletion deduction is. Tell us because we know that we are suppose to have recovery of basis in this. It is a very difficult thing to do and establish and approve because they don't actually have an interest in the land; they have an interest in the proceeds. So, what this provision does, is it eliminates a lot of employment for accountants. It essentially says; we are not going to get into the recipients of depletion on a regional recipients basis or on a village basis. We are simply going to say that the receipt of this amount under

7(i) consistent with the overall intent of ANCSA is itself a contribution of capitals of the corporation. It is something that you are entitled to receive as result of your formation under ANCSA.

HALTERMAN:

Do you have any questions on that? Okay, I guess the next outstanding, I guess the only outstanding remaining issue then, Pat, is what effect do these changes have on current or future state tax revenues?

BEATTIE:

And how does the Social Security Administration relate to the deficit on the United States? Your question is a very difficult one because of a couple of things. Number one; I would throw the question back at you or to the Department of Revenue: How much in taxes are you currently collecting from Native corporations? I am making the assumption that the amount of taxes being collected from Native corporations is currently relatively low. Because a lot of them have had problems. How much in revenues is there a loss? On a practical basis probably very little. On a gross numbers basis it may look like an awfully lot because there is a lot of 7(i) payments that are made. Okay, but it doesn't change the fact that the revenues being reported, the net revenues being reported by the Native corporations are for the most part relatively small. I think that is a correct statement to make. I make that statement knowing the clients that we have with regards to the villages and the amount of losses that they have had and the tax returns that we have filed. I think it is a safe statement to extrapolate that and say, that there are not a whole lot of taxes that are paid. I haven't really answered your question because it is a very difficult question to answer, and to come up with, I guess, what would be a meaningful projection of reduction of state revenues, and I also have to admit that you might have to get more complicated and tie this into the Native corporations ability to use the consolidation provision mentioned earlier in disposing of some of their losses, so that they do become a tax paying entity in Alaska. Which they are not currently.

HALTERMAN:

And, also, I think you have to optimistically look at the future, the time when they will be profitable enterprises and to the extent that they are profitable and tax paying and then to the extent that the 7(i) distributions are not counted as profits, there is a lost.

BEATTIE:

That is correct, and it's a little bit of a catch 22, because the consolidation provision may well have the effect of accelerating taxation in Alaska that wouldn't otherwise take place. In other words, my example before when I said the lower forty-eight companies that would participate in these transaction, whose income would not otherwise be subject to tax in Alaska, all of a sudden now will be taking down losses that are Alaska losses and

making income in, future income to be made in Alaska subject to taxation that would not otherwise be subject to taxation. That is part of the pluses behind the consolidation provision, is that it accelerates that, and hopefully is a benefit to the revenue picture in Alaska. But, then once you have made that assumption, okay, and that is a big hurdle and assumption to be made; that not only the technology exists to get the federal law changed and to implement transactions that are a benefit to Native corporations, but once that is done, then at that point they will be taxable on their earnings, and then you are talking about different types of dollars if you will, with regard to the 7(i) provision. But, one and the other is part and parcel to it.

HALTERMAN: Well, I don't have any other questions right now. Do you have any other questions, Bob?

BERRY: No, I don't think so.

HALTERMAN: Sure, go a head, Pat.

NORMAN: The corporations file consolidated statements now and after 1991 that ends and how

BEATTIE: I am sorry I can't hear you. Could you repeat that, please?

HALTERMAN: Just a minute.

NORMAN: Corporations are required to, or we file consolidated statements right now until 1991. After that date, then what happens to how we file?

BEATTIE: As it stands right now, assuming the alienability issue is resolved and the stock becomes tradable, then the consolidations are terminated, and the reason for that is the fact that in discussing the need for the consolidated provision with the Internal Revenue Service in Washington D.C. and IRS National, one of the major reasons why we were able to get the provision, was the fact that Native corporations themselves can not have a stock issued to raise capital. So, this is an alternative form of raising capital. No more different than the popular money market preferreds that are currently being utilized by savings and loans, in the saving and loan industry to absorb their losses. So, that once 1991 comes and this restriction on the ability to raise capital by issuing stock lapses, then the need or the benefit for the consolidated filing arguably should not be there, because it was there essentially to supplement the problems of the restriction provided by 7(h).

HALTERMAN: Okay, Pat, I think we have all the answers to the questions we have now, but I think we may have some more questions. Now, you are going to Washington next week? What is your availability here in the near term?

BEATTIE: I am in the office today and definitely Monday and Tuesday next week. I am not sure about the end of next week. It hasn't been decided yet.

BERRY: Will you be available to testify by teleconference from Anchorage on this bill when it has a hearing?

BEATTIE: Yes.

BERRY: Okay, that would be good. It is probably almost, it is probably real important for people to understand the bill that you be available.

BEATTIE: That is fine. It is my pleasure. It is unfortunate because, I guess, in my mind it is a very technical issue with out question, but in reality, what we are trying to do at least on the 7(i) issue is simply put. the law back to where it was prior.

HALTERMAN: Right, and I guess, Pat, the one other question that I ask in listening to your response, I have heard a political response to it is: Why was it changed in the first place?

BEATTIE: The reason it was changed in the first place was the thought that by having 7(i) considered as contributing capital it would restrict the corporation ability to pay dividends. That there would be something, and I am a little bit out of my bailiwick here because it is a legal question, I have gotten away from tax, but I think the concept was that a corporation can not pay dividends for State purposes out of its capital. It has to come out of surplus. So, by 7(i) being considered contributing capital it restricted their ability to pay dividends. I don't believe that situation still exists, and if it does, I would recommend that included with the change then we simply have a corporate statute change that says, that Native corporations are entitled to make dividend distributions or distributions out of their contributing capital to the extent of 7(i), if that is a problem.

HALTERMAN: That leads me to hopefully the last questions. That is; now, am I correct in understanding that if in fact a corporate entity makes a dividend distribution from its capital base, then, it by definition is reducing that base and that can have an affect on loan agreements and other business transaction and so forth?

BEATTIE: I suppose so, but I am not aware of that being a major problem.

HALTERMAN: I see. Well, listen, Pat, we appreciate it very much and we will be back in touch, and of course, you know, as far as when the committee schedules the bill as long as you are near a telephone if you are in Tierra del Fruego we can have you testify that is no problem.

BEATTIE: Okay, that is great.

HALTERMAN: Alright, thank you very much.

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"(IV) at least 25 percent of the total indebtedness of the corporation is extinguished by transfers pursuant to such plan."

26 USC 108 note.

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if it had been included in the amendments made by subsections (e) and (f) of section 806 of the Tax Reform Act of 1976.

26 USC 368, 382, 383.

(b) EFFECTIVE DATE.—

26 USC 108 note.

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendment made by subsection (a) shall apply to transfers after the date of the enactment of this Act in taxable years ending after such date.

(2) TRANSITIONAL RULE.—The amendment made by subsection (a) shall not apply to the transfer by a corporation of its stock in exchange for debt of the corporation after the date of the enactment of this Act if such transfer is—

(A) pursuant to a written contract requiring such transfer which was binding on the corporation at all times on June 7, 1984, and at all times after such date but only if the transfer takes place before January 1, 1985, and only if the transferee held the debt at all times on June 7, 1984, or

(B) pursuant to the exercise of an option to exchange debt for stock but only if such option was in effect at all times on June 7, 1984, and at all times after such date and only if at all times on June 7, 1984, the option and the debt were held by the same person.

(3) CERTAIN TRANSFERS TO CONTROLLING SHAREHOLDER.—The amendment made by subsection (a) shall not apply to any transfer before January 1, 1985, by a corporation of its stock in exchange for debt of such corporation if—

(A) such transfer is to another corporation which at all times on June 7, 1984, owned 75 percent or more of the total value of the stock of the corporation making such transfer, and

(B) immediately after such transfer, the transferee corporation owns 80 percent or more of the total value of the stock of the transferor corporation.

(4) CERTAIN TRANSFER PURSUANT TO DEBT RESTRUCTURE AGREEMENT.—The amendment made by subsection (a) shall not apply to the transfer by a corporation of its stock in exchange for debt of the corporation after the date of the enactment of this Act and before January 1, 1985, if—

(A) such transfer is covered by a debt restructure agreement entered into by the corporation during November 1983, and

(B) such agreement was specified in a registration statement filed with the Securities and Exchange Commission by the corporation on March 7, 1984.

SEC. 64 AFFILIATED GROUP DEFINED.

→ (a) IN GENERAL.—Subsection (a) of section 1504 (defining affiliated group) is amended to read as follows:

26 USC 1504.

"(a) AFFILIATED GROUP DEFINED.—For purposes of this subtitle—

"(1) IN GENERAL.—The term 'affiliated group' means—

"(A) 1 or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation, but only if—

“(B)(i) the common parent owns directly stock meeting the requirements of paragraph (2) in at least 1 of the other includible corporations, and

“(ii) stock meeting the requirements of paragraph (2) in each of the includible corporations (except the common parent) is owned directly by 1 or more of the other includible corporations.

“(2) 80-PERCENT VOTING AND VALUE TEST.—The ownership of stock of any corporation meets the requirements of this paragraph if it—

“(A) possesses at least 80 percent of the total voting power of the stock of such corporation, and

“(B) has a value equal to at least 80 percent of the total value of the stock of such corporation.

“(3) 5 YEARS MUST ELAPSE BEFORE RECONSOLIDATION.—

“(A) IN GENERAL.—If—

“(i) a corporation is included (or required to be included) in a consolidated return filed by an affiliated group for a taxable year which includes any period after December 31, 1984, and

“(ii) such corporation ceases to be a member of such group in a taxable year beginning after December 31, 1984,

with respect to periods after such cessation, such corporation (and any successor of such corporation) may not be included in any consolidated return filed by the affiliated group (or by another affiliated group with the same common parent or a successor of such common parent) before the 61st month beginning after its first taxable year in which it ceased to be a member of such affiliated group.

“(B) SECRETARY MAY WAIVE APPLICATION OF SUBPARAGRAPH (A).—The Secretary may waive the application of subparagraph (A) to any corporation for any period subject to such conditions as the Secretary may prescribe.

“(4) STOCK NOT TO INCLUDE CERTAIN PREFERRED STOCK.—For purposes of this subsection, the term ‘stock’ does not include any stock which—

“(A) is not entitled to vote,

“(B) is limited and preferred as to dividends and does not participate in corporate growth to any significant extent,

“(C) has redemption and liquidation rights which do not exceed the paid-in capital or par value represented by such stock (except for a reasonable redemption premium in excess of such paid-in capital or par value), and

“(D) is not convertible into another class of stock.

“(5) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including (but not limited to) regulations—

“(A) which treat warrants, obligations convertible into stock, and other similar interests as stock, and stock as not stock,

“(B) which treat options to acquire or sell stock as having been exercised,

“(C) which provide that the requirements of paragraph (2)(B) shall be treated as met if the affiliated group, in

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SEC. 61. PROVISION

(a) ADJUSTMENT

reliance on a good faith determination of value, treated such requirements as met,

"(D) which disregard an inadvertent ceasing to meet the requirements of paragraph (2)(B) by reason of changes in relative values of different classes of stock,

"(E) which provide that transfers of stock within the group shall not be taken into account in determining whether a corporation ceases to be a member of an affiliated group, and

"(F) which disregard changes in voting power to the extent such changes are disproportionate to related changes in value."

(b) EFFECTIVE DATE.—

26 USC 15-4
note.

(1) **IN GENERAL.**—Except as otherwise provided in this subsection, the amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1984.

(2) **SPECIAL RULE FOR CORPORATIONS AFFILIATED ON JUNE 22, 1984.**—In the case of a corporation which on June 22, 1984, is a member of an affiliated group which files a consolidated return for such corporation's taxable year which includes June 22, 1984, for purposes of determining whether such corporation continues to be a member of such group for taxable years beginning before January 1, 1988, the amendment made by subsection (a) shall not apply.

(3) **SPECIAL RULE NOT TO APPLY TO SELL-DOWNS AFTER JUNE 22, 1984.**—If—

(A) the requirements of subsection (b)(2) are satisfied with respect to a corporation,

(B) more than a de minimis amount of the stock of such corporation is sold or exchanged (including in a redemption), or issued (other than in the ordinary course of business) after June 22, 1984, and

(C) the requirements of the amendment made by subsection (a) are not satisfied after such sale, exchange, or issuance, then the amendments made by subsection (a) shall apply for purposes of determining whether such corporation continues to be a member of such group.

(4) **EXCEPTION FOR CERTAIN SELL-DOWNS.**—Subsection (b)(2) (and not subsection (b)(3)) will apply to a corporation if such corporation issues or sells stock after June 22, 1984, pursuant to a registration statement filed with the Securities and Exchange Commission on or before June 22, 1984, but only if the requirements of the amendment made by subsection (a) (substituting "more than 50 percent" for "at least 80 percent" in paragraph (2)(B) of section 1504(a) of the Internal Revenue Code of 1954) are satisfied immediately after such issuance or sale and at all times thereafter until the first day of the first taxable year beginning after December 31, 1987.

Ante, p. 577.

→ (5) **NATIVE CORPORATIONS.**—The amendments made by subsection (a) shall not apply to any Native Corporation established under the Alaska Native Claims Settlement Act (43 U.S.C. 1601 et seq.) during any taxable year beginning before 1992 or any part thereof in which such Corporation is subject to the provisions of section 7(h)(1) of such Act (43 U.S.C. 1606 (h)(1)).

SEC. 61. PROVISIONS RELATING TO EARNINGS AND PROFITS.

(a) ADJUSTMENTS TO EARNINGS AND PROFITS.—

LEGISLATIVE AFFAIRS DIVISION
POLICE Y-STATE CLERK

the benefit of the Natives who elected to be enrolled therein, and they may establish a Regional Corporation pursuant to this Act.

(d) Five incorporators within each region, named by the Native association in the region, shall incorporate under the laws of Alaska a Regional Corporation to conduct business for profit, which shall be eligible for the benefits of this Act so long as it is organized and functions in accordance with this Act. The articles of incorporation shall include provisions necessary to carry out the terms of this Act.

(e) The original articles of incorporation and bylaws shall be approved by the Secretary before they are filed, and they shall be submitted for approval within eighteen months after the date of enactment of this Act. The articles of incorporation may not be amended during the Regional Corporation's first five years without the approval of the Secretary. The Secretary may withhold approval under this section if in his judgment inequities among Native individuals or groups of Native individuals would be created.

(f) The management of the Regional Corporation shall be vested in a board of directors, all of whom, with the exception of the initial board, shall be stockholders over the age of eighteen. The number, terms, and method of election of members of the board of directors shall be fixed in the articles of incorporation or bylaws of the Regional Corporation.

(g) The Regional Corporation shall be authorized to issue such number of shares of common stock, divided into such classes of shares as may be specified in the articles of incorporation to reflect the provisions of this Act, as may be needed to issue one hundred shares of stock to each Native enrolled in the region pursuant to section 5.

(h) (1) Except as otherwise provided in paragraph (2) of this subsection, stock issued pursuant to subsection (g) shall carry a right to vote in elections for the board of directors and on such other questions as properly may be presented to stockholders, shall permit the holder to receive dividends or other distributions from the Regional Corporation, and shall vest in the holder all rights of a stockholder in a business corporation organized under the laws of the State of Alaska, except that for a period of twenty years after the date of enactment of this Act the stock, inchoate rights thereto, and any dividends paid or distributions made with respect thereto may not be sold, pledged, subjected to a lien or judgment execution, assigned in present or future, or otherwise alienated: Provided, That such limitation shall not apply to transfers of stock pursuant to a court decree of separation, divorce or child support or by stockholder who is a member of a professional organization, association, or board which limits the ability of that stockholder to practice his profession because of holding stock issued under this Act.

(2) Upon the death of any stockholder, ownership of such stock shall be transferred in accordance with his last will and testament or under the applicable laws of intestacy, except that (A) during the twenty-year period after the date of enactment of this Act such stock shall carry

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voting rights only if the holder thereof through inheritance also is a Native, and (B), in the event the deceased stockholder fails to dispose of his stock by will and has no heirs under the applicable laws of intestacy, such stock shall escheat to the Regional Corporation.

(3)(A) On December 18, 1991, all stock previously issued shall be deemed to be canceled, and shares of stock of the appropriate class shall be issued to each stockholder share for share subject only to such restrictions as may be provided by the articles of incorporation of the corporation, or agreements between corporations and individual shareholders.

(B) If adopted by December 18, 1991, restrictions provided by amendment to the articles of incorporation may include, in addition to any other legally permissible restrictions —

(i) the denial of voting rights to any holder of stock who is not a Native, or a descendant of a Native, and

(ii) the granting to the corporation, or to the corporation and a stockholder's immediate family, on reasonable terms, the first right to purchase a stockholder's stock (whether issued before or after the adoption of the restriction) prior to the sale or transfer of such stock (other than a transfer by inheritance) to any other party, including a transfer in satisfaction of a lien, writ of attachment, judgment execution, pledge, or other encumbrance.

(C) Notwithstanding any provision of Alaska law to the contrary —

(i) any amendment to the articles of incorporation of a regional corporation to provide for any of the restrictions specified in clause (i) or (ii) subparagraph (B) shall be approved if such amendment receives the affirmative vote of the holders of a majority of the outstanding shares entitled to be voted of the corporation, and

(ii) any amendment to the articles of incorporation of a Native Corporation which would grant voting rights to stockholders who were previously denied such voting rights shall be approved only if such amendment receives, in addition to any affirmative vote otherwise required, a like affirmative vote of the holders of shares entitled to be voted under the provisions of the articles of incorporation.

→ (i) Seventy per centum of all revenues received by each Regional Corporation from the timber resources and subsurface estate patented to it pursuant to this Act shall be divided annually by the Regional Corporation among all twelve Regional Corporations organized pursuant to this section according to the number of Natives enrolled in each region pursuant to section 5. The provisions of this subsection shall not apply to the thirteenth Regional Corporation if organized pursuant to subsection (c) hereof.

(j) During the five years following the enactment of this Act, not less than 10% of all corporate funds received by each of the twelve Regional Corporations under section 6 (Alaska Native Fund), and under subsection (i) (revenues from the timber resources and subsurface estate

patented to it pursuant to this Act), and all other net income, shall be distributed among the stockholders of the twelve Regional Corporations. Not less than 45% of funds from such sources during the first five-year period, and 50% thereafter, shall be distributed among the Village Corporations in the region and the class of stockholders who are not residents of those villages, as provided in subsection to it. In the case of the thirteenth Regional Corporation, if organized, not less than 50% of all corporate funds received under section 6 shall be distributed to the stockholders.

(k) Funds distributed among the Village Corporations shall be divided among them according to the ratio that the number of shares of stock registered on the books of the Regional Corporation in the names of residents of each village bears to the number of shares of stock registered in the names of residents in all villages.

(l) Funds distributed to a Village Corporation may be withheld until the village has submitted a plan for the use of the money that is satisfactory to the Regional Corporation. The Regional Corporation may require a village plan to provide for joint ventures with other villages, and for joint financing of projects undertaken by the Regional Corporation that will benefit the region generally. In the event of disagreement over the provisions of the plan, the issues in disagreement shall be submitted to arbitration, as shall be provided for in the articles of incorporation of the Regional Corporation.

(m) When funds are distributed among Village Corporations in a region, an amount computed as follows shall be distributed as dividends to the class of stockholders who are not residents of those villages: The amount distributed as dividends shall bear the same ratio to the amount distributed among the Village Corporations that the number of shares of stock registered on the books of the Regional Corporation in the names of nonresidents of villages bears to the number of shares of stock registered in the names of village residents: Provided, That an equitable portion of the amount distributed as dividends may be withheld and combined with Village Corporation funds to finance projects that will benefit the region generally.

(n) The Regional Corporation may undertake on behalf of one or more of the Village Corporations in the region any project authorized and financed by them.

(o) The accounts of the Regional Corporation shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants or independent licensed public accountants, certified or licensed by a regulatory authority of the State or the United States. The audits shall be conducted at the place or places where the accounts of the Regional Corporation are normally kept. All books, accounts, financial records, reports, files, and other papers, things, or property belonging to or in use by the Regional Corporation and necessary to facilitate the audits shall be available to

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Regional Corporations shall be organized in the number of shares of stock equal to the number of shares of stock of the Regional Corporation in the event of a liquidation.

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the person or persons conducting the audits; and full facilities for verifying transactions with the balances or securities held by depositories, fiscal agent, and custodians shall be afforded to such person or persons. Each audit report or a fair and reasonably detailed summary thereof shall be transmitted to each stockholder, to the Secretary of the Interior and to the Committees on Interior and Insular Affairs of the Senate and the House of Representatives.

(p) In the event of any conflict between the provisions of this section and the laws of the State of Alaska, the provisions of this section shall prevail.

(q) Two or more Regional Corporations may contract with the same business management group for investment services and advice regarding the investment of corporate funds. (Amended December 2 1980, P.L. 96-487 Title XIV § 1401(c), 94 Stat. 2492)

Revisor's notes. — The phrase "as provided in subsection to it" at the end of the second sentence of subsection (j) also appeared in the original version of this Act; it probably should refer to subsections (k), (l), and (m).

Cross references. — For corporations organized under this act, see AS 10.05.005; for the intestate share of a surviving spouse in stock of corporations organized under this act, see AS 13.11.012; for inheritance of stock of corporations organized under this act, see AS 13.16.705; for transfers of stock of corporations organized

under this act pursuant to a court decree of separation, divorce or child support, see AS 22.10.020; for contracts between corporations organized under this act and the Department of Natural Resources for management of land, see AS 38.95.050; for the issuance to a minor of stock or membership in a corporation organized under this act, see AS 45.60.016.

Effect of amendments. — The 1980 amendment, in subsection (h), added language beginning "or by stockholder who is a member" at the end of paragraph (1), and rewrote paragraph (3).

NOTES TO DECISIONS

- I. General Consideration.
 - A. Intent.
 - B. Jurisdiction.
- II. Boundaries.
- III. Stock.
 - A. Alienation.
 - B. Intestate Disposition.
- IV. Subsurface Estate.
- V. Division of Revenues.
 - A. "All Revenues."
 - B. Revenue Subject to Division.
 - C. Evidentiary and Procedural Issues.
- VI. Distribution of Funds.
- VII. Projects to Benefit Region.

I. GENERAL CONSIDERATION.

Applicability to villages holding fee land. — Neither subsection (l) nor subsection (m) seems applicable to the villages holding fee land since the regional corporation has no authority to control activities in those villages and the natives are not entitled to receive distributions

from the fund or stock. *Doyon, Ltd. v. Bristol Bay Native Corp.*, 569 F.2d 491 (9th Cir.), cert. denied, 439 U.S. 954, 99 S. Ct. 352, 58 L. Ed. 2d 345 (1978).

Construction of "Natives enrolled". — See *Doyon, Ltd. v. Bristol Bay Native Corp.*, 565 F.2d 491 (9th Cir.), cert. denied, 439 U.S. 954, 99 S. Ct. 352, 58 L. Ed. 2d 345 (1978).



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James O. Smith
Signature of Camera Operator

7/25/89
Date