

HOUSE
COMMITTEE REPORT

(11)

Date referred: 4/9/86

FURTHER REFERRALS:

DATE: 4-15-86

The FINANCE Committee has considered HB 546
"An Act relating to the taxation of Native corporations."

and recommends:

- do pass
- do not pass
- do pass with attached amendment(s)
- no recommendation
- replace with CS HB 546 (CIRA) same title
- new title

and recommends no recommendation

further referral to the _____ Committee

- and attaches:
- letter of intent
 - first fiscal note
 - new fiscal note
 - zero fiscal note

SIGNING DO PASS:

Albert B. Lohs

[Signature]

[Signature]

Ronald J. [Signature]

SIGNING OTHER RECOMMENDATIONS:

Mike [Signature] No Rec.

[Signature] No Rec.

[Signature] NO REC.

[Signature] No Recommendation

[Signature] No Rec.

[Signature] No Rec.

Albert B. Lohs
Chairman

STATE OF ALASKA 1986 LEGISLATIVE SESSION
FISCAL NOTE

Revision Date 3/24/86

REQUEST
Bill/Resolution No: ^{OS} HB 546 (C+RA)
Title: Taxation of Native Corporations

FISCAL DETAIL
Agency Affected: Department of Revenue
BRU: Audit

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

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-
800 MISCELLANEOUS	-0-	-0-	-0-	-0-	-0-	-0-
TOTAL OPERATING	-0-	-0-	-0-	-0-	-0-	-0-
CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
REVENUE	-0-	-0-	-0-	-0-	-0-	-0-

FUNDING: (Thousands of Dollars)

GENERAL FUND	-0-	-0-	-0-	-0-	-0-	-0-
FEDERAL FUNDS	-0-	-0-	-0-	-0-	-0-	-0-
OTHER	-0-	-0-	-0-	-0-	-0-	-0-
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
- Impacted Agency(ies)

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
16 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).

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.

CS HB 546 (C+RA)

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 ~~the~~ in which the depletion allowance for resource extraction is computed.

Native corporations which own the resources and retain 30% of the income therefrom are able to shelter this income from taxation through the use of a depletion allowance. However, the corporate recipients of the remaining 70%, because they are not owners of the resources, are not eligible for the same favorable tax treatment; this subverts the concept of equality upon which the 7(i) provision of ANCSA is based. By defining these payments as contributions to capital, rather than income, balance is restored.

Section 2

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 advice of Mr. Beattie of Peat Marwick.

The provision allows Native corporations to file consolidated tax returns for their subsidiary businesses. Since 1928 American corporations have been able to file consolidated tax returns for their subsidiaries, thus sheltering the earnings of their profitable subsidiaries with the losses of their poor performers; the losses generated were able to be "sold " to other profitable concerns in order to reduce the purchasers' tax liability.

This practice increased dramatically in 1981 with the passage of more liberal depreciation requirements. In 1984 Congress substantially limited this practice through the creation of more onerous ownership requirements for subsidiaries whose losses companies claimed for tax purposes. Alaska Native corporations were exempted from this provision due to their inability to sell stock to generate additional capital.



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.

A handwritten signature in cursive script that reads "J. Patrick Beattie".

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.

Sec. 2 of the bill

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.

Sec. 1 of the bill

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. Patrick Beatty

Offered: 4/9/86
Referred: Finance

Original sponsor: Fuller

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

1 IN THE HOUSE

BY FULLER

2

HOUSE BILL NO. 546

3

IN THE LEGISLATURE OF THE STATE OF ALASKA

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FOURTEENTH LEGISLATURE - SECOND SESSION

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A BILL

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