HB

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CS FOR HOUSE BILL NO. 328(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-SEVENTH LEGISLATURE - SECOND SESSION

BY THE HOUSE RESOURCES COMMITTEE

Offered:
Referred:

Sponsor(s): REPRESENTATIVES SEATON, Gardner

A BILL

FOR AN ACT ENTITLED

"An Act relating to the oil and gas corporate income tax; relating to the credits against the oil and gas corporate income tax; making conforming amendments; and providing for an effective date."

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

*** Section 1.** AS 21.96.070(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under more than one provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the

meaning given in AS 43.20.073.

* **Sec. 2.** AS 21.96.070(d), as amended by sec. 7, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under more than one provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $150,000.

* **Sec. 3.** AS 21.96.075(c) is amended to read:

(c) A contribution claimed by a taxpayer as a credit under this section may not

(1) be the basis for a credit claimed under more than one provision of this title;

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073; or

(3) be claimed as a credit unless the contribution qualifies for the credit under (d) of this section.

* **Sec. 4.** AS 21.96.075(c), as amended by sec. 10, ch. 92, SLA 2010, is amended to read:

(c) A contribution claimed by a taxpayer as a credit under this section may not

(1) be the basis for a credit claimed under more than one provision of this title;

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $150,000; or

(3) be claimed as a credit unless the contribution qualifies for the credit

under (d) of this section.

* **Sec. 5.** AS 29.60.599(1) is amended to read:

(1) "barrel," when used with reference to oil, **means the quantity of oil contained in 42 United States gallons of 231 cubic inches each, measured at a temperature of 60 degrees Fahrenheit and an absolute pressure of 14.65 pounds a square inch** [HAS THE MEANING GIVEN IN AS 43.20.072];

* **Sec. 6.** AS 41.09.010(b) is amended to read:

(b) An exploration incentive credit extended under (a) of this section may be applied against

(1) a payment or obligation against which a credit authorized by AS 38.05.180(i) may be claimed;

(2) taxes payable under AS 43.20 **or AS 43.21, as applicable**; and

(3) oil and gas bonus payments due the state under AS 38.05.180(f).

* **Sec. 7.** AS 43.20.011 is amended by adding a new subsection to read:

(g) For purposes of calculating the tax under (e) of this section, the taxable income of a corporation engaged in the production or transportation of crude oil or natural gas shall be determined in accordance with AS 43.21.

* **Sec. 8.** AS 43.20.014(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title;

(2) also be allowed as a deduction under 26 U.S.C. 170 against the tax imposed by this chapter; and

(3) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

* **Sec. 9.** AS 43.20.014(d), as amended by sec. 18, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title;

(2) also be allowed as a deduction under 26 U.S.C. 170 against the tax imposed by this chapter; and

(3) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $150,000.

* **Sec. 10.** AS 43.20.073(f) is amended to read:

(f) This section does not apply to taxpayers subject to **AS 43.21** [AS 43.20.072 ENGAGED IN

(1) THE PRODUCTION OF OIL OR GAS FROM A LEASE OR PROPERTY IN THE STATE; OR

(2) THE TRANSPORTATION OF OIL OR GAS BY REGULATED PIPELINE IN THE STATE].

* **Sec. 11.** AS 43.21 is amended by adding new sections to read:

Article 1. Determination of Taxable Income.

Sec. 43.21.200. Application. This chapter applies to every corporation doing business in the state that derives income from the production of oil or gas from a lease or property in the state or from the pipeline transportation of oil or gas in the state. The tax calculated under this chapter is measured by the total taxable income of the corporation during the tax period as defined by AS 43.21.210 - 43.21.250 and is calculated at the rates established under AS 43.20.011(e).

Sec. 43.21.210. Internal Revenue Code adopted by reference. (a) 26 U.S.C. 1 - 1399 and 6001 - 7872 (Internal Revenue Code), as amended, are adopted by reference as a part of this chapter. These portions of the Internal Revenue Code have full force and effect under this chapter unless excepted to or modified by other provisions of this chapter.

(b) When portions of the Internal Revenue Code incorporated by reference as provided in (a) of this section refer to rules and regulations adopted by the United

States Commissioner of Internal Revenue, or hereafter adopted, those portions shall be regarded as regulations adopted by the department under and in accord with the provisions of this chapter, unless and until the department adopts specific regulations in place of those portions conformable with this chapter.

Sec. 43.21.220. Determination of taxable income from oil and gas production. (a) The taxable income of a corporation from the production of oil and gas from a lease or property in the state is the corporation's net income as calculated in accordance with this section.

(b) Gross income of a corporation from oil and gas production is the sum of the gross value at the point of production of oil or gas produced from a lease or property in the state, any gain or loss resulting from the sale of a lease, and any gain or loss resulting from the sale of property used in the production of oil and gas in the state. The department shall by regulation determine a uniform method of establishing the gross value at the point of production. For the purpose of determining the gross value at the point of production under this subsection, the department shall use AS 43.55.150 for the determination of transportation costs.

(c) Net income from oil and gas production shall be determined by deducting from gross income the following:

(1) royalties paid in kind or in value;

(2) taxes imposed under AS 43.55 that are actually paid or incurred by the corporation on the production from a lease or property in the state;

(3) taxes imposed under AS 29.45.080 - 29.45.090 and AS 43.56 that are actually paid or incurred by the corporation on property used directly in the production of oil or gas from a lease or property in the state, including property used in production, gathering, treatment, or preparation of the oil or gas for pipeline transportation, but only if those property tax payments were due and payable only after the date of commercial production from the lease or property with which the property was associated;

(4) the direct costs incurred by or for the corporation in operating the lease or property, including the direct costs of producing, gathering, treating, or preparing the oil or gas for pipeline transportation, but net of any payments received

for those activities and not including any indirect cost or overhead expense;

(5) depreciation, under 26 U.S.C. 167 (Internal Revenue Code) or another reasonable method as the department may by regulation establish, on property used directly in the production, gathering, treatment, or preparation of the oil or gas for pipeline transportation, including amortization of capitalized interest for investments in that property at a rate not to exceed the average cost to the taxpayer of borrowed capital during the year in which the interest is capitalized; for purposes of this paragraph, property capitalized under AS 43.20 shall maintain its adjusted basis, less any depreciation taken under AS 43.20 and any amount attributable to that property received as a credit under this title;

(6) the amortization of lease acquisition payments and taxes paid or incurred under AS 29.45.080, 29.45.090, or AS 43.56, including capitalized interest, for or on producing properties before the commencement of commercial production from the lease or property for which the property is being used;

(7) interest expense of the corporation, not capitalized during construction, that was paid or incurred in connection with property in the state; however, the interest expense may not exceed that portion of the total interest paid by the consolidated business of which the corporation is a part, determined by multiplying the total interest by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business; in this paragraph, "total interest paid by the consolidated business" does not include interest expense arising from intercompany obligations within the consolidated business except to the extent that the interest expense reflects a pass-through of interest on a third-party borrowing by the parent or other member of the consolidated business with the purpose, expressed at the time of the third-party borrowing, of financing Alaska business activity of the taxpayer corporation;

(8) expenses incurred by the corporation after December 31, 2012, of unsuccessful exploration of oil or gas in the state, including the acquisition costs of abandoned properties, dry hole costs, and the costs of geologic and geophysical

exploration related to those abandoned properties;

(9) general overhead or administrative expense incurred by the corporation attributable to deriving income from the production of oil or gas from a lease or property in the state to the extent that the general overhead or administrative expense does not exceed that portion of the total general overhead or administrative expense incurred by the consolidated business of which the corporation is a part, determined by multiplying the total general overhead or administrative expense by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business;

(10) the amount of income from the production of oil and gas from a lease or property that is divided among the regional Native corporations under 43 U.S.C. 1606(i) (sec. 7(i), Alaska Native Claims Settlement Act, P.L. 92-203);

(11) net operating loss carry forward amounts accrued from taxes paid under AS 43.20 or AS 43.21 for expenditures related to the production of oil or gas from a lease or property in the state or from pipeline transportation of oil or gas in the state, except that a net operating loss amount that resulted from an expenditure that was also the basis of a credit under this title may not be deducted under this paragraph.

(d) Deductions from gross income under this section may not include expenses previously deducted on a return filed under AS 43.20.

(e) If a corporation subject to this chapter shares the production or proceeds of the production from a lease or property through a working interest, royalty interest, overriding royalty interest, production payment, net profit interest, joint venture, or other agreement, the taxpayer shall allocate the deductions from gross income between the corporation and the persons with whom the corporation has the agreement in accordance with the terms of the agreement.

Sec. 43.21.230. Determination of income from oil and gas pipeline transportation. (a) Except as provided in (c) of this section, taxable income attributable to the transportation of oil in a pipeline engaged in interstate commerce in this state is the amount reported or that would be required to be reported to the Federal

Energy Regulatory Commission or its successors as net operating income, less those portions of interest and general overhead or administrative expense attributable to the pipeline transportation of oil in the state, except that taxable income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general overhead or administrative expense attributable to pipeline transportation of oil in the state.

(b) Except as provided in (c) of this section, taxable income attributable to the transportation of natural gas in a pipeline engaged in interstate commerce in this state is the amount reported or that would be required to be reported to the Federal Energy Regulatory Commission as net operating income, less that portion of interest and general overhead or administrative expense attributable to pipeline transportation in the state, except that the taxable income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general overhead or administrative expense attributable to pipeline transportation of natural gas in the state.

(c) Taxable income attributable to the transportation of oil or natural gas in this state of a corporation not under the jurisdiction of the Federal Energy Regulatory Commission, or of a corporation under the jurisdiction of the Federal Energy Regulatory Commission but not reporting the operation of pipelines in the state separately from the operation of pipelines elsewhere, shall be based on an amount equal to the amount that would have been reported to the Federal Energy Regulatory Commission under (a) of this section in the case of oil pipelines, or under (b) of this section, in the case of natural gas pipelines, had the corporation been, in fact, under the jurisdiction of the Federal Energy Regulatory Commission for the taxable year and required to report on the operation of pipelines in the state separately from the operation of pipelines elsewhere.

Sec. 43.21.240. Determination of income from activities other than oil and gas production or pipeline transportation. (a) Taxable income of a corporation subject to this chapter from activities in this state other than the production of oil or gas from a lease or property in the state or the pipeline transportation of oil or gas in the state shall be determined in accordance with the method established in art. IV of

AS 43.19.010 and in AS 43.20.071, as modified by (b) - (d) of this section.

(b) The total taxable income of a consolidated business is its entire income less the portion of that entire income attributable to worldwide production and pipeline transportation of oil and gas. In this subsection, for a member of a consolidated business who is

(1) required to file under the Internal Revenue Code, "entire income" means the taxpayer's taxable income as the term is used in AS 43.20.011 - 43.20.065;

(2) not required to file under the Internal Revenue Code, "entire income" means an income determination prepared in accordance with generally accepted accounting principles, except that a taxpayer may elect to report income as the income would be determined under (1) of this subsection.

(c) The numerator and denominator of the property factor, of the payroll factor, and of the sales factor shall be calculated without reference to that portion of property, payroll, or sales directly related to the production of oil or gas from a lease of property in the state or the pipeline transportation of oil or gas in the state.

(d) The value attributed to vessels transporting Alaska oil or gas of a consolidated business that are not owned or effectively owned by the consolidated business shall be excluded from the property factor.

Sec. 43.21.250. Applicability of tax to a consolidated business. The provisions of this chapter apply to a consolidated business whether or not the taxpayer is the parent or controlling corporation.

Article 2. Calculation of Tax; Returns.

Sec. 43.21.300. Calculation of tax. (a) The amount of the tax payable on the taxable income of a corporation subject to tax under this chapter shall be determined using the tax rates in AS 43.20.011(e).

(b) For purposes of this chapter, the department may combine taxable income of corporations subject to tax under this chapter who are part of the same consolidated business.

(c) If the methods of allocation and apportionment provided in this chapter do not fairly represent the extent of a corporation's business activity in the state, the corporation may petition for or the department may require, in respect to all or any

part of the corporation's business activity, if reasonable, the employment of any method authorized under art. IV, sec. 18, AS 43.19.010 (Multistate Tax Compact), to carry out an equitable allocation and apportionment of the corporation's income. The commissioner shall include in the annual report required in AS 43.21.410 a report on all relief granted under this subsection, including, for each case, a statement of the changes in tax liability resulting from the granting of relief, the tax years involved, and a description of the method of determining taxable income that was substituted for the methods provided in this chapter.

Sec. 43.21.310. Income tax education credit. (a) A taxpayer is allowed as a credit against the tax due under this chapter for cash contributions accepted

(1) for direct instruction, research, and educational support purposes, including library and museum acquisitions, and contributions to endowment, by an Alaska university foundation or by a nonprofit, public or private, Alaska two-year or four-year college accredited by a regional accreditation association;

(2) for secondary school level vocational education courses, programs, and facilities by a school district in the state;

(3) for vocational education courses, programs, and facilities by a state-operated vocational technical education and training school;

(4) for a facility or an annual intercollegiate sports tournament by a nonprofit, public or private, Alaska two-year or four-year college accredited by a regional accreditation association;

(5) for Alaska Native cultural or heritage programs and educational support, including mentoring and tutoring, provided by a nonprofit agency for public school staff and for students who are in grades kindergarten through 12 in the state; and

(6) for education, research, rehabilitation, and facilities by an institution that is located in the state and that qualifies as a coastal ecosystem learning center under the Coastal America Partnership established by the federal government.

(b) The amount of the credit is

(1) 50 percent of contributions of not more than $100,000;

(2) 100 percent of the next $200,000 of contributions; and

(3) 50 percent of the amount of contributions that exceed $300,000.

(c) Each public college and university shall include in its annual operating budget request contributions received and how the contributions were used.

(d) A contribution claimed as a credit under this section may not

(1) be claimed as a credit under another provision of this title;

(2) also be allowed as a deduction under 26 U.S.C. 170 against the tax imposed by this chapter; and

(3) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

(e) The credit under this section may not reduce a person's tax liability under this chapter to below zero for any tax year. An unused credit or portion of a credit not used under this section for a tax year may not be sold, traded, transferred, or applied in a subsequent tax year.

(f) In this section,

(1) "school district" means a borough school district, a city school district, a regional educational attendance area, or a state boarding school;

(2) "vocational education" means organized educational activities that offer a sequence of courses that provides individuals with the academic and technical knowledge and skills the individuals need to prepare for further education and for careers other than careers requiring a baccalaureate, master's, or doctoral degree.

Sec. 43.21.320. Credits. In addition to the credit allowed under AS 43.21.310, a credit under AS 43.20.043, 43.20.044, or 43.20.046 may also be applied against the tax levied under this chapter, unless a credit for the same expenditure has been taken against a tax levied under AS 43.20 or AS 43.55.

Sec. 43.21.330. Returns and payment of taxes. (a) A corporation subject to tax under this chapter and required to make a return under the Internal Revenue Code

shall, within 30 days after the federal return is required to be filed, submit a return setting out

(1) the amount of tax due under this chapter, less credits claimed against the tax; and

(2) other information the department may require to carry out the purposes of this chapter.

(b) The return shall be made under oath or shall contain a written declaration that it is made under penalty of perjury and shall be made on a form prescribed by the department.

(c) On request by the department, a taxpayer shall furnish to the department a true and correct copy of each annual tax return the taxpayer has filed with the United States Internal Revenue Service. Every taxpayer shall notify the department in writing of any modification of the taxpayer's federal income tax return and of a recomputation of tax or determination of deficiency. A full statement of the facts must accompany this notice. The notice shall be filed within 60 days after the final determination of the modification, recomputation, or deficiency, and the taxpayer shall pay the additional tax or penalty under this chapter. For purposes of this section, a determination shall be considered to be final at the time an amended federal return is filed or a notice of deficiency or an assessment is mailed to the taxpayer by the Internal Revenue Service, except that in no event shall a determination be considered final for purposes of this section until the taxpayer has exhausted the taxpayer's rights of appeal under federal law.

(d) The total amount of tax imposed by this chapter is due and payable to the department at the same time and in the same manner as the tax payable to the United States Internal Revenue Service, including quarterly estimated tax prepayments, except that a taxpayer with an estimated tax liability of less than $1,000,000 for the year is not required to make quarterly prepayments of the estimated tax.

(e) A tax due under this section is payable even if the assessment is under appeal or the validity, enforceability, or application of this chapter or any provision of this chapter is challenged before the department or in the courts.

(f) An unpaid amount of an installment payment required under (d) of this

section that is not paid when due shall be treated as an underpayment under 26 U.S.C. 6655 (Internal Revenue Code) and shall accrue interest at a rate appropriate for the state prescribed in regulation.

Article 3. Administrative Matters.

Sec. 43.21.400. Regulations. The department shall adopt regulations in accordance with AS 44.62 (Administrative Procedure Act) to implement this chapter. In the adoption of regulations under this section, the department shall use the 1981 regulations adopted under former provisions of this chapter as guidance. Regulations adopted under this section must include methods for accounting for

(1) intercompany transactions in a fair and equitable manner and to prevent purposeful tax evasion or manipulation of income or deductions, including transactions for costs incurred by a party outside of the state that are related to oil or gas production from a lease or property in the state or to pipeline transportation of oil or gas in the state; and

(2) transactions between parent and subsidiary companies.

Sec. 43.21.410. Public reporting. (a) The commissioner shall compile and transmit to the legislature an annual report of state revenue and the implementation of taxation policies under this chapter. The report must include total aggregate income tax paid by corporations subject to this chapter and aggregate income and deductions by category, classified so as to prevent the identification of particular returns or reports.

(b) The legislative auditor shall notify the legislature on or before the first day of each regular session that the annual report reviewing the actions of the department in administering this chapter is available.

Sec. 43.21.420. Information disclosure. Notwithstanding AS 43.05.320, the department shall disclose to a legislator, on request, information collected from a taxpayer to the extent that

(1) the taxpayer is a publicly traded company;

(2) the information has been filed in a quarterly, annual, or other periodic report to the United States Securities Exchange Commission; and

(3) the information has been made public by the United States

Securities Exchange Commission.

Sec. 43.21.499. Definitions. Unless the context requires otherwise, the definitions contained in AS 43.55.900 are applicable to this chapter. In addition, in this chapter,

(1) "consolidated business" means a corporation or group of corporations having more than 50 percent common ownership, direct or indirect, or a group of corporations in which there is common control, either direct or indirect, as evidenced by an arrangement, contract, or agreement;

(2) "Internal Revenue Code" has the meaning given in AS 43.20.340.

* **Sec. 12.** AS 43.21.310(a), added by sec. 11 of this Act, is amended to read:

(a) A taxpayer is allowed as a credit against the tax due under this chapter for cash contributions accepted

(1) for direct instruction, research, and educational support purposes, including library and museum acquisitions, and contributions to endowment, by an Alaska university foundation or by a nonprofit, public or private, Alaska two-year or four-year college accredited by a regional accreditation association;

(2) for secondary school level vocational education courses **and** [,] programs [, AND FACILITIES] by a school district in the state;

(3) [FOR VOCATIONAL EDUCATION COURSES, PROGRAMS, AND FACILITIES] by a state-operated vocational technical education and training school [;

(4) FOR A FACILITY OR AN ANNUAL INTERCOLLEGIATE SPORTS TOURNAMENT BY A NONPROFIT, PUBLIC OR PRIVATE, ALASKA TWO-YEAR OR FOUR-YEAR COLLEGE ACCREDITED BY A REGIONAL ACCREDITATION ASSOCIATION;

(5) FOR ALASKA NATIVE CULTURAL OR HERITAGE PROGRAMS AND EDUCATIONAL SUPPORT, INCLUDING MENTORING AND TUTORING, PROVIDED BY A NONPROFIT AGENCY FOR PUBLIC SCHOOL STAFF AND FOR STUDENTS WHO ARE IN GRADES KINDERGARTEN THROUGH 12 IN THE STATE; AND

(6) FOR EDUCATION, RESEARCH, REHABILITATION, AND

FACILITIES BY AN INSTITUTION THAT IS LOCATED IN THE STATE AND THAT QUALIFIES AS A COASTAL ECOSYSTEM LEARNING CENTER UNDER THE COASTAL AMERICA PARTNERSHIP ESTABLISHED BY THE FEDERAL GOVERNMENT].

* **Sec. 13.** AS 43.21.310(b), added by sec. 11 of this Act, is amended to read:

(b) The amount of the credit is

(1) 50 percent of contributions of not more than $100,000; **and**

(2) 100 percent of the next **$100,000** [$200,000] of contributions [; AND

(3) 50 PERCENT OF THE AMOUNT OF CONTRIBUTIONS THAT EXCEED $300,000].

* **Sec. 14.** AS 43.21.310(d), added by sec. 11 of this Act, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be claimed as a credit under another provision of this title;

(2) also be allowed as a deduction under 26 U.S.C. 170 against the tax imposed by this chapter; and

(3) when combined with credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, AS 43.55.019, AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding **$150,000** [$5,000,000; IF THE TAXPAYER IS A MEMBER OF AN AFFILIATED GROUP, THEN THE TOTAL AMOUNT OF CREDITS MAY NOT EXCEED $5,000,000 FOR THE AFFILIATED GROUP; IN THIS PARAGRAPH, "AFFILIATED GROUP" HAS THE MEANING GIVEN IN 43.20.073].

* **Sec. 15.** AS 43.55.019(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an

affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

* **Sec. 16.** AS 43.55.019(d), as amended by sec. 25, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.56.018, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $150,000.

* **Sec. 17.** AS 43.56.018(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

* **Sec. 18.** AS 43.56.018(d), as amended by sec. 32, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.65.018, AS 43.75.018, or AS 43.77.045, result in the total amount of credits exceeding $150,000.

* **Sec. 19.** AS 43.65.018(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.75.018, or AS 43.77.045, result in the total amount of the credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

* **Sec. 20.** AS 43.65.018(d), as amended by sec. 39, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, or AS 43.77.045, result in the total amount of the credits exceeding $150,000.

* **Sec. 21.** AS 43.75.018(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, or AS 43.77.045, result in the total amount of the credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

* **Sec. 22.** AS 43.75.018(d), as amended by sec. 46, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, or AS 43.77.045, result in the total amount of the credits exceeding $150,000.

*** Sec. 23.** AS 43.77.045(d) is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, or AS 43.75.018, result in the total amount of the credits exceeding $5,000,000; if the taxpayer is a member of an affiliated group, then the total amount of credits may not exceed $5,000,000 for the affiliated group; in this paragraph, "affiliated group" has the meaning given in AS 43.20.073.

*** Sec. 24.** AS 43.77.045(d), as amended by sec. 53, ch. 92, SLA 2010, is amended to read:

(d) A contribution claimed as a credit under this section may not

(1) be the basis for a credit claimed under another provision of this title; and

(2) when combined with contributions that are the basis for credits taken during the taxpayer's tax year under AS 21.96.070, 21.96.075, AS 43.20.014, **AS 43.21.310,** AS 43.55.019, AS 43.56.018, AS 43.65.018, or AS 43.75.018, result in the total amount of the credits exceeding $150,000.

*** Sec. 25.** AS 43.82.210(a) is amended to read:

(a) If the commissioner approves an application and proposed project plan under AS 43.82.140, the commissioner may develop proposed terms for inclusion in a contract under AS 43.82.020 for periodic payment in lieu of one or more of the following taxes that otherwise would be imposed by the state or a municipality on the qualified sponsor or member of a qualified sponsor group as a consequence of

participating in an approved qualified project:

(1) oil and gas production taxes and oil surcharges under AS 43.55;

(2) oil and gas exploration, production, and pipeline transportation property taxes under AS 43.56;

(3) **oil and gas corporate income tax under AS 43.21;** [REPEALED]

(4) Alaska net income tax under AS 43.20;

(5) municipal sales and use tax under AS 29.45.650 - 29.45.710;

(6) municipal property tax under AS 29.45.010 - 29.45.250 or 29.45.550 - 29.45.600;

(7) municipal special assessments under AS 29.46;

(8) a comparable tax or levy imposed by the state or a municipality after June 18, 1998;

(9) other state or municipal taxes or categories of taxes identified by the commissioner.

*** Sec. 26.** AS 43.20.072 is repealed.

*** Sec. 27.** The uncodified law of the State of Alaska is amended by adding a new section to read:

APPLICABILITY. AS 43.21, added by sec. 11 of this Act, applies to taxable income earned or received after December 31, 2012.

*** Sec. 28.** The uncodified law of the State of Alaska is amended by adding a new section to read:

REGULATIONS. (a) The Department of Revenue may adopt regulations necessary to implement AS 43.21, added by sec. 11 of this Act. The regulations take effect under AS 44.62 (Administrative Procedure Act), but not before the effective date of the law implemented by regulation.

(b) The Department of Revenue shall provide by regulation for a transition for a corporation subject to tax under AS 43.20 before December 31, 2012, to avoid double taxation of the same income or double deduction of the same expense of the corporation as a result of becoming subject to tax under AS 43.21, added by sec. 11 of this Act.

(c) The Department of Revenue may adopt regulations necessary to provide a five-year transition period for the adoption of applicable depreciation schedules.

* **Sec. 29.** Sections 2, 4, 9, 12 - 14, 16, 18, 20, 22, and 24 of this Act take effect on the effective date specified in sec. 57, ch. 92 SLA 2010, as amended by sec. 15, ch. 7 FSSLA 2011, and as may be further amended.

* **Sec. 30.** Section 28 of this Act takes effect immediately under AS 01.10.070(c).

* **Sec. 31.** Except as provided in secs. 29 and 30 of this Act, this Act takes effect January 1, 2013.

27-LS1142\I
Nauman
3/27/12

CS FOR HOUSE BILL NO. 328(RES)

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-SEVENTH LEGISLATURE - SECOND SESSION

BY THE HOUSE RESOURCES COMMITTEE

Offered:
Referred:

Sponsor(s): REPRESENTATIVES SEATON, Gardner

A BILL

FOR AN ACT ENTITLED

"An Act relating to the oil and gas corporate income tax; relating to the credits against the oil and gas corporate income tax; making conforming amendments; and providing for an effective date."

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

*** Section 1.** AS 29.60.599(1) is amended to read:

(1) "barrel," when used with reference to oil, **means the quantity of oil contained in 42 United States gallons of 231 cubic inches each, measured at a temperature of 60 degrees Fahrenheit and an absolute pressure of 14.65 pounds a square inch** [HAS THE MEANING GIVEN IN AS 43.20.072];

*** Sec. 2.** AS 41.09.010(b) is amended to read:

(b) An exploration incentive credit extended under (a) of this section may be applied against

(1) a payment or obligation against which a credit authorized by AS 38.05.180(i) may be claimed;

(2) taxes payable under AS 43.20 **or AS 43.21, as applicable**; and

(3) oil and gas bonus payments due the state under AS 38.05.180(f).

*** Sec. 3.** AS 43.20.011 is amended by adding a new subsection to read:

(g) For purposes of calculating the tax under (e) of this section, the taxable income of a corporation engaged in the production or transportation of crude oil or natural gas shall be determined in accordance with AS 43.21.

*** Sec. 4.** AS 43.20.073(f) is amended to read:

(f) This section does not apply to taxpayers subject to **AS 43.21** [AS 43.20.072 ENGAGED IN

(1) THE PRODUCTION OF OIL OR GAS FROM A LEASE OR PROPERTY IN THE STATE; OR

(2) THE TRANSPORTATION OF OIL OR GAS BY REGULATED PIPELINE IN THE STATE].

*** Sec. 5.** AS 43.21 is amended by adding new sections to read:

Article 1. Determination of Taxable Income.

Sec. 43.21.200. Application. This chapter applies to every corporation doing business in the state that derives income from the production of oil or gas from a lease or property in the state or from the pipeline transportation of oil or gas in the state. The tax calculated under this chapter is measured by the total taxable income of the corporation during the tax period as defined by AS 43.21.210 - 43.21.240 and is calculated at the rates established under AS 43.20.011(e).

Sec. 43.21.210. Determination of taxable income from oil and gas production. (a) The taxable income of a corporation from the production of oil and gas from a lease or property in the state is the corporation's net income as calculated in accordance with this section.

(b) Gross income of a corporation from oil and gas production is the sum of the gross value at the point of production of oil or gas produced from a lease or property in the state, any gain or loss resulting from the sale of a lease, and any gain or loss resulting from the sale of property used in the production of oil and gas in the state. The department shall by regulation determine a uniform method of establishing the gross value at the point of production. For the purpose of determining the gross

value at the point of production under this subsection, the department shall use AS 43.55.150 for the determination of transportation costs.

(c) Net income from oil and gas production shall be determined by deducting from gross income the following:

(1) royalties paid in kind or in value;

(2) taxes imposed under AS 43.55 that are actually paid or incurred by the corporation on the production from a lease or property in the state;

(3) taxes imposed under AS 29.45.080 - 29.45.090 and AS 43.56 that are actually paid or incurred by the corporation on property used directly in the production of oil or gas from a lease or property in the state, including property used in production, gathering, treatment, or preparation of the oil or gas for pipeline transportation, but only if those property tax payments were due and payable only after the date of commercial production from the lease or property with which the property was associated;

(4) the direct costs incurred by or for the corporation in operating the lease or property, including the direct costs of producing, gathering, treating, or preparing the oil or gas for pipeline transportation, but net of any payments received for those activities and not including any indirect cost or overhead expense;

(5) depreciation, under 26 U.S.C. 167 (Internal Revenue Code) or another reasonable method as the department may by regulation establish, on property required to be capitalized under 26 U.S.C. (Internal Revenue Code) and used directly in the production, gathering, treatment, or preparation of the oil or gas for pipeline transportation, including amortization of capitalized interest for investments in that property at a rate not to exceed the average cost to the taxpayer of borrowed capital during the year in which the interest is capitalized;

(6) the amortization of lease acquisition payments and taxes paid or incurred under AS 29.45.080, 29.45.090, or AS 43.56, including capitalized interest, for or on producing properties before the commencement of commercial production from the lease or property for which the property is being used;

(7) interest expense of the corporation, not capitalized during construction, that was paid or incurred in connection with property in the state;

however, the interest expense may not exceed that portion of the total interest paid by the consolidated business of which the corporation is a part, determined by multiplying the total interest by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business; in this paragraph, "total interest paid by the consolidated business" does not include interest expense arising from intercompany obligations within the consolidated business except to the extent that the interest expense reflects a pass-through of interest on a third-party borrowing by the parent or other member of the consolidated business with the purpose, expressed at the time of the third-party borrowing, of financing Alaska business activity of the taxpayer corporation;

(8) expenses incurred by the corporation after December 31, 2012, of unsuccessful exploration of oil or gas in the state, including the acquisition costs of abandoned properties, dry hole costs, and the costs of geologic and geophysical exploration related to those abandoned properties;

(9) general overhead or administrative expense incurred by the corporation attributable to deriving income from the production of oil or gas from a lease or property in the state to the extent that the general overhead or administrative expense does not exceed that portion of the total general overhead or administrative expense incurred by the consolidated business of which the corporation is a part, determined by multiplying the total general overhead or administrative expense by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business;

(10) the amount of income from the production of oil and gas from a lease or property that is divided among the regional Native corporations under 43 U.S.C. 1606(i) (sec. 7(i), Alaska Native Claims Settlement Act, P.L. 92-203).

(d) Deductions from gross income under this section may not include expenses previously deducted on a return filed under AS 43.20.

(e) If a corporation subject to this chapter shares the production or proceeds of the production from a lease or property through a working interest, royalty interest, overriding royalty interest, production payment, net profit interest, joint venture, or other agreement, the taxpayer shall allocate the deductions from gross income between the corporation and the persons with whom the corporation has the agreement in accordance with the terms of the agreement.

Sec. 43.21.220. Determination of income from oil and gas pipeline transportation. (a) Except as provided in (c) of this section, taxable income attributable to the transportation of oil in a pipeline engaged in interstate commerce in this state is the amount reported or that would be required to be reported to the Federal Energy Regulatory Commission or its successors as net operating income, less those portions of interest and general overhead or administrative expense attributable to the pipeline transportation of oil in the state, except that taxable income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general overhead or administrative expense attributable to pipeline transportation of oil in the state.

(b) Except as provided in (c) of this section, taxable income attributable to the transportation of natural gas in a pipeline engaged in interstate commerce in this state is the amount reported or that would be required to be reported to the Federal Energy Regulatory Commission as net operating income, less that portion of interest and general overhead or administrative expense attributable to pipeline transportation in the state, except that the taxable income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general overhead or administrative expense attributable to pipeline transportation of natural gas in the state.

(c) Taxable income attributable to the transportation of oil or natural gas in this state of a corporation not under the jurisdiction of the Federal Energy Regulatory Commission, or of a corporation under the jurisdiction of the Federal Energy Regulatory Commission but not reporting the operation of pipelines in the state separately from the operation of pipelines elsewhere, shall be based on an amount equal to the amount that would have been reported to the Federal Energy Regulatory

Commission under (a) of this section in the case of oil pipelines, or under (b) of this section, in the case of natural gas pipelines, had the corporation been, in fact, under the jurisdiction of the Federal Energy Regulatory Commission for the taxable year and required to report on the operation of pipelines in the state separately from the operation of pipelines elsewhere.

Sec. 43.21.230. Determination of income from activities other than oil and gas production or pipeline transportation. (a) Taxable income of a corporation subject to this chapter from activities in this state other than the production of oil or gas from a lease or property in the state or the pipeline transportation of oil or gas in the state shall be determined in accordance with the method established in art. IV of AS 43.19.010 and in AS 43.20.071, as modified by (b) - (d) of this section.

(b) The total taxable income of a consolidated business is its entire income less the portion of that entire income attributable to worldwide production and pipeline transportation of oil and gas. In this subsection, for a member of a consolidated business who is

(1) required to file under the Internal Revenue Code, "entire income" means the taxpayer's taxable income as the term is used in AS 43.20.011 - 43.20.065;

(2) not required to file under the Internal Revenue Code, "entire income" means an income determination prepared in accordance with generally accepted accounting principles, except that a taxpayer may elect to report income as the income would be determined under (1) of this subsection.

(c) The numerator and denominator of the property factor, of the payroll factor, and of the sales factor shall be calculated without reference to that portion of property, payroll, or sales directly related to the production of oil or gas from a lease of property in the state or the pipeline transportation of oil or gas in the state.

(d) The value attributed to vessels transporting Alaska oil or gas of a consolidated business that are not owned or effectively owned by the consolidated business shall be excluded from the property factor.

Sec. 43.21.240. Applicability of tax to a consolidated business. The provisions of this chapter apply to a consolidated business whether or not the taxpayer is the parent or controlling corporation.

Article 2. Calculation of Tax; Returns.

Sec. 43.21.300. Calculation of tax. (a) The amount of the tax payable on the taxable income of a corporation subject to tax under this chapter shall be determined using the tax rates in AS 43.20.011(e).

(b) For purposes of this chapter, the department may combine taxable income of corporations subject to tax under this chapter who are part of the same consolidated business.

(c) If the methods of allocation and apportionment provided in this chapter do not fairly represent the extent of a corporation's business activity in the state, the corporation may petition for or the department may require, in respect to all or any part of the corporation's business activity, if reasonable, the employment of any method authorized under art. IV, sec. 18, AS 43.19.010 (Multistate Tax Compact), to carry out an equitable allocation and apportionment of the corporation's income. The commissioner shall include in the annual report required in AS 43.21.410 a report on all relief granted under this subsection, including, for each case, a statement of the changes in tax liability resulting from the granting of relief, the tax years involved, and a description of the method of determining taxable income that was substituted for the methods provided in this chapter.

Sec. 43.21.320. Credits. A credit under AS 43.20.043, 43.20.044, or 43.20.046 may also be applied against the tax levied under this chapter, unless a credit for the same expenditure has been taken against a tax levied under AS 43.20 or AS 43.55.

Sec. 43.21.330. Returns and payment of taxes. (a) A corporation subject to tax under this chapter and required to make a return under the Internal Revenue Code shall, within 30 days after the federal return is required to be filed, submit a return setting out

(1) the amount of tax due under this chapter, less credits claimed against the tax; and

(2) other information the department may require to carry out the purposes of this chapter.

(b) The return shall be made under oath or shall contain a written declaration that it is made under penalty of perjury and shall be made on a form prescribed by the

department.

(c) The total amount of tax imposed by this chapter is due and payable to the department at the same time and in the same manner as the tax payable to the United States Internal Revenue Service, including quarterly estimated tax prepayments, except that a taxpayer with an estimated tax liability of less than $1,000,000 for the year is not required to make quarterly prepayments of the estimated tax.

(d) A tax due under this section is payable even if the assessment is under appeal or the validity, enforceability, or application of this chapter or any provision of this chapter is challenged before the department or in the courts.

(e) An unpaid amount of an installment payment required under (c) of this section that is not paid when due bears interest (1) at the rate provided for an underpayment under 26 U.S.C. 6621 (Internal Revenue Code), as amended, compounded daily, from the date the installment payment is due until March 31 following the calendar year of production; and (2) as provided for a delinquent tax under AS 43.05.225 after that March 31. Interest accrued under (1) of this subsection that remains unpaid after that March 31 is treated as an addition to tax that bears interest under (2) of this subsection.

(f) Notwithstanding any contrary provision of AS 43.05.280,

(1) an overpayment of an installment payment required under (c) of this section bears interest at the rate provided for an overpayment under 26 U.S.C. 6621 (Internal Revenue Code), as amended, compounded daily, from the later of the date the installment payment is due or the date the overpayment is made, until the earlier of

(A) the date the overpayment is refunded or applied to an underpayment; or

(B) March 31 following the calendar year of production;

(2) except as provided under (1) of this subsection, interest with respect to an overpayment is allowed only on any net overpayment of the payments required under (c) of this section that remains after the later of March 31 following the calendar year of production or the date that the statement required is filed;

(3) interest is allowed under (2) of this subsection only from a date that

is 90 days after the later of March 31 following the calendar year of production or the date that the statement required is filed; interest is not allowed if the overpayment was refunded within the 90-day period;

(4) interest under (2) and (3) of this section is paid at the rate and in the manner provided in AS 43.05.225(1).

(g) Notwithstanding any contrary provision of AS 43.05.225 or (e) or (f) of this section, if the amount of a tax payment, including an installment payment, due under (c) of this section is affected by the retroactive application of a regulation adopted under this chapter, the department shall determine whether the retroactive application of the regulation caused an underpayment or an overpayment of the amount due and adjust the interest due on the affected payment as follows:

(1) if an underpayment of the amount due occurred, the department shall waive interest that would otherwise accrue for the underpayment before the first day of the second month following the month in which the regulation became effective, if

(A) the department determines that the producer's underpayment resulted because the regulation was not in effect when the payment was due; and

(B) the producer demonstrates that it made a good faith estimate of its tax obligation in light of the regulations then in effect when the payment was due and paid the estimated tax;

(2) if an overpayment of the amount due occurred and the department determines that the producer's overpayment resulted because the regulation was not in effect when the payment was due, the obligation for a refund for the overpayment does not begin to accrue interest earlier than the following, as applicable:

(A) except as otherwise provided under (B) of this paragraph, the first day of the second month following the month in which the regulation became effective;

(B) 90 days after an amended statement and an application to request a refund of production tax paid is filed, if the overpayment was for a period for which an amended statement was required to be filed before the

regulation became effective.

Article 3. Administrative Matters.

Sec. 43.21.400. Regulations. The department shall adopt regulations in accordance with AS 44.62 (Administrative Procedure Act) as appropriate to administer and enforce this chapter.

Sec. 43.21.410. Public reporting. (a) The commissioner shall compile and transmit to the legislature an annual report of state revenue and the implementation of taxation policies under this chapter. The report must include total aggregate income tax paid by corporations subject to this chapter and aggregate income and deductions by category, classified so as to prevent the identification of particular returns or reports.

(b) The legislative auditor shall notify the legislature on or before the first day of each regular session that the annual report reviewing the actions of the department in administering this chapter is available.

Sec. 43.21.420. Information disclosure. Notwithstanding AS 43.05.320, the department shall disclose to a legislator, on request, information collected from a taxpayer to the extent that

(1) the taxpayer is a publicly traded company;

(2) the information has been filed in a quarterly, annual, or other periodic report to the United States Securities Exchange Commission; and

(3) the information has been made public by the United States Securities Exchange Commission.

Sec. 43.21.499. Definitions. Unless the context requires otherwise, the definitions contained in AS 43.55.900 are applicable to this chapter. In addition, in this chapter,

(1) "consolidated business" means a corporation or group of corporations having more than 50 percent common ownership, direct or indirect, or a group of corporations in which there is common control, either direct or indirect, as evidenced by an arrangement, contract, or agreement;

(2) "Internal Revenue Code" has the meaning given in AS 43.20.340.

* **Sec. 6.** AS 43.82.210(a) is amended to read:

(a) If the commissioner approves an application and proposed project plan under AS 43.82.140, the commissioner may develop proposed terms for inclusion in a contract under AS 43.82.020 for periodic payment in lieu of one or more of the following taxes that otherwise would be imposed by the state or a municipality on the qualified sponsor or member of a qualified sponsor group as a consequence of participating in an approved qualified project:

(1) oil and gas production taxes and oil surcharges under AS 43.55;

(2) oil and gas exploration, production, and pipeline transportation property taxes under AS 43.56;

(3) **oil and gas corporate income tax under AS 43.21;** [REPEALED]

(4) Alaska net income tax under AS 43.20;

(5) municipal sales and use tax under AS 29.45.650 - 29.45.710;

(6) municipal property tax under AS 29.45.010 - 29.45.250 or 29.45.550 - 29.45.600;

(7) municipal special assessments under AS 29.46;

(8) a comparable tax or levy imposed by the state or a municipality after June 18, 1998;

(9) other state or municipal taxes or categories of taxes identified by the commissioner.

* **Sec. 7.** AS 43.20.072 is repealed.

* **Sec. 8.** The uncodified law of the State of Alaska is amended by adding a new section to read:

APPLICABILITY. AS 43.21, added by sec. 5 of this Act, applies to taxable income earned or received after December 31, 2012.

* **Sec. 9.** The uncodified law of the State of Alaska is amended by adding a new section to read:

REGULATIONS. (a) The Department of Revenue may adopt regulations necessary to implement AS 43.21, added by sec. 5 of this Act. The regulations take effect under AS 44.62 (Administrative Procedure Act), but not before the effective date of the law implemented by regulation.

(b) The Department of Revenue shall provide by regulation for a transition for a

corporation subject to tax under AS 43.20 before December 31, 2012, to avoid double taxation of the same income or double deduction of the same expense of the corporation as a result of becoming subject to tax under AS 43.21, added by sec. 5 of this Act.

(c) The Department of Revenue may adopt regulations necessary to provide a five-year transition period for the adoption of applicable depreciation schedules.

*** Sec. 10.** Section 9 of this Act takes effect immediately under AS 01.10.070(c).

*** Sec. 11.** Except as provided in sec. 10 of this Act, this Act takes effect January 1, 2013.

HB 328 CS Work-draft Version I changes from Version B (Corrected)

Prepared by the office of Representative Seaton

- Adds gains and losses from the sale of leases or properties used in the production of oil and gas to the calculation of gross income for determining taxable income. (Page 2, lines 28 and 29)

- Deletes the requirement that the Department of Revenue calculate a taxpayer's net income. Under version I a company is required to calculate its own tax liability. The Department was concerned with the administrative burden of calculating a taxpayer's tax liability. (Page 3 line 3, page 5 line 4 and page 5 line 30)

- Requires depreciation under current Internal Revenue Code in the calculation of a taxpayer's net income. Deletes the requirement that for the depreciation of property, taxpayers use the Internal Revenue Code depreciation schedule from 1981. (Page 3, line 19)

- Deletes requirement that depreciation be calculated on a percentage depletion basis. The Department was concerned that percentage depletion was not a customary depreciation method, and that it allows recovery in excess of cost. Replaces percentage depletion with depreciation under current Internal Revenue Code. (Page 3, line 19)

- Requires that property must be capitalized for purposes of deducting depreciation in determining net income. Previous language did not specifically require capitalization of property. (Page 3, line 21)

- Requires quarterly estimated payments as is current practice. However, taxpayers with an estimated liability of less than one million dollars for the year may file annually. Inserts section imposing interest on underpayment and overpayment of quarterly installments. (Page 8 and Page 9)

- Allows a five-year transition period for taxpayers to align to the current Internal Revenue code depreciation schedule from the 1981 schedule which is currently in effect. (Page 12, lines 4 and 5)

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

(907) 465-3867 or 465-2450
FAX (907) 465-2029
Mail Stop 3101

State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM February 24, 2012

SUBJECT: Sectional Summary for HB 328 (Work Order No. 27-LS1142\B)

TO: Representative Paul Seaton
Attn: Louie Flora

FROM: Emily Nauman
Legislative Counsel

You have requested a sectional summary of the above-described bill.

As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents. If you would like an interpretation of the bill as it may apply to a particular set of circumstances, please advise.

Section 1 amends the definition of "barrel" in AS 29.60.599; substituting it with the text that will be lost with the repeal of AS 43.20.072.

Section 2 extends the exploration incentive credit provided by AS 41.09.010 to AS 43.21.

Section 3 directs corporations engaged in production or transportation of crude oil or natural gas to determine net income under AS 43.21.

Section 4 substitutes a descriptive list exempting oil and gas companies from the affiliated group reporting requirements of AS 43.20.073(f) with a reference exempting taxpayers subject to AS 43.21.

Section 5 adds AS 43.21, the former Oil and Gas Corporate Income Tax that was repealed in 1982. Credits applicable to income taxes paid under AS 43.20 are extended to AS 43.21 in AS 43.21.320, with exception of the education tax credit, which is not extended to income taxes calculated under AS 43.21. A requirement that legislators have access to information provided by corporations to the SEC has been added at AS 43.21.420. Additionally, minor changes have been made, including updating dates, cross references, and language.

Section 6 extends periodic payment provisions for stranded gas development projects to taxes paid under AS 43.21.

Section 7 repeals AS 43.20.072, the previous oil and gas tax provisions.

Section 8 states that AS 43.21 applies only to taxable income earned or received after December 31, 2012.

Section 9 directs the Department of Revenue to develop regulations to effect AS 43.21 and to develop transitional regulations.

Section 10 gives an immediate effective date to sec. 9, allowing the department to proceed with development of regulations immediately.

Section 11 gives the effective date for the remainder of the bill as January 1, 2013.

ELN:plm
12-127.plm

FISCAL NOTE

STATE OF ALASKA cost ≠ codes
2012 LEGISLATIVE SESSION

Bill Version: **HB 328**
Fiscal Note Number: 1
Publish Date:

Identifier (file name): HB328-DOR-TAX-02-27-12
Title: Oil and Gas Corporate Taxes
Sponsor: Representatives Seaton and Gardner
Requester: (H) RES

Dept. Affected: Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

	FY13 Appropriation Requested	Included in Governor's FY13 Request	Out-Year Cost Estimates				
OPERATING EXPENDITURES	**FY13**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18**
Personal Services			246.6	493.2	493.2	493.2	493.2
Travel				25.0	25.0	25.0	25.0
Services			2.3	4.7	4.7	4.7	4.7
Commodities							
Capital Outlay			5.0				
Grants, Benefits							
Miscellaneous							
TOTAL OPERATING	**0.0**	**0.0**	**253.9**	**522.9**	**522.9**	**522.9**	**522.9**

FUND SOURCE				(Thousands of Dollars)				
1002	Federal Receipts							
1003	GF Match							
1004	GF			253.9	522.9	522.9	522.9	522.9
1005	GF/Prgm (DGF)							
1037	GF/MH (UGF)							
1178	temp code (UGF)							
TOTAL		**0.0**	**0.0**	**253.9**	**522.9**	**522.9**	**522.9**	**522.9**

POSITIONS							
Full-time			4	4	4	4	4
Part-time							
Temporary							

CHANGE IN REVENUES	**0.0**	**0.0**	***	***	***	***	***

Estimated SUPPLEMENTAL (FY12) operating costs _____ *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY13) costs _____ *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Why this fiscal note differs from previous version (if initial version, please note as such)

Initial fiscal note.

Prepared by: Johanna Bales, Deputy Director — Phone (907) 269-6628
Division: Tax — Date/Time 2/27/2012 3:30 p.m.
Approved by: Jerry Burnett, Director Administrative Services — Date 2/28/2012
Department of Revenue

(Revised 8/17/2011 OMB)

FISCAL NOTE

STATE OF ALASKA **BILL NO.** HB 328
2012 LEGISLATIVE SESSION

Analysis

Bill Language:
This bill would repeal the current corporate income tax on oil and gas corporations under AS 43.20.072 (worldwide combination and apportionment) and replace it with a corporate income tax based on separate accounting. Current oil and gas corporate income tax is based on a formula where total worldwide income of a corporation's unitary group is apportioned to Alaska based on the amount of property, extraction and sales attributable to Alaska. This bill would require Alaska oil and gas corporations to calculate income tax for their oil and gas producing and transportation companies based on income earned solely in Alaska. If oil and gas companies are also engaged in activities other than oil and gas production and transportation, this bill would require those companies to calculate and pay tax on those other activities based on worldwide combination and apportionment. This bill would require oil and gas corporations to file a return by April 15 each year providing information the department needs to calculate each corporation's taxable income and income tax. This bill requires the department to calculate each corporation's income tax and send an assessment by August 15 each year to each company subject to the tax. Corporations must then pay the amount of tax as calculated by the department by September 30 of each year. This bill also requires the department to prepare a report each year showing the aggregate amount of income and deductions by category reported by all oil and gas corporate income tax taxpayers. The department would also be required to disclose specific information about a taxpayer if the taxpayer is a publicly traded company and if the information was included in a report filed with the US Securities Exchange Commission (SEC) and the SEC publicly disclosed the information.

Revenues:
The department does not have enough information to accurately and fully estimate the change in oil and gas corporate income tax as a result of this legislation. Preliminary estimates show that under separate accounting, oil and gas corporations would have paid approximately $250 million more during each of the last 5 fiscal years in corporate income tax if this legislation had been in effect. This bill has an effective date of January 1, 2013. Oil and gas corporations would report under the new method beginning in April 2014 and tax would not be due until September 30, 2014. Therefore, we do not expect to see a change in corporate income tax as a result of this legislation until FY 2015.

Expenditures:
As stated above, this bill would require the Department of Revenue to calculate the amount of tax due by each oil and gas corporation operating in the state based on information each company provided the department. The department would have approximately 4 months to make the calculation of corporate income tax and send assessments to each taxpayer. In addition, the department would be required under this legislation to prepare a report showing aggregate information of all taxpayers and specific information of publicly traded companies. Under the current oil and gas corporate income tax, the calculation of taxable income starts with federal taxable income and then is adjusted for certain Alaska modifications. Currently, the department relies on federal corporate income tax audits as an additional audit resource. As such, the department does not audit down to the invoice level. The calculation of taxable income under separate accounting does not start with federal taxable income and, as such, the department will not be able to rely on federal audits to ensure that taxpayers are properly reporting and must conduct full scale audits including auditing down to the invoice level. There are currently 26 oil and gas corporate income tax filers. The department will have to calculate each taxpayers tax liability each year and conduct more comprehensive audits as well as provide a report each year to the legislature. The department believes it will need four additional corporate income tax auditor III's to handle the increased work as a result of this legislation. In addition, the department will need increased travel funds of approximately $25,000 each year to spend enough time at a corporation's place of business to conduct in depth audits.

REPRESENTATIVE PAUL SEATON

SESSION ADDRESS
State Capitol Building
Juneau, Alaska 99801-1182
(907) 465-2689
Fax: (907) 465-3472
1-800-665-2689

INTERIM ADDRESS
345 W. Sterling Highway
Homer, Alaska 99603
(907) 235-2921
Fax: (907) 235-4008
1-800-665-2689

ALASKA STATE LEGISLATURE
House District 35

Sponsor Statement HB 328

Separate Accounting

HB 328 requires international oil producers to pay their 9.4% Alaska Income Tax on profit made in Alaska just like companies operating only in Alaska. HB 328 replaces the current tax method under which oil companies pay a proportion of their worldwide profits calculated for their production from Alaska operations. This worldwide apportionment of corporate income tax allows oil companies to write off less profitable international or Lower 48 domestic production against their highly profitable Alaska production.

HB 328 reinstitutes Separate Accounting which simply means the companies pay on profits made in Alaska. Alaska instituted Separate Accounting from 1978 to 1982 because the state was subsidizing overseas investments by oil companies under the appointment method of calculating income taxes. During the four years that companies paid tax on their Alaska profits, about $1.8 billion dollars more was collected than would have been collected under the worldwide apportionment method. The oil companies sued on numerous grounds and lost on all points at trial. The case was appealed to the Alaska Supreme Court.

There was concern in 1981 over an increasing liability for repayment if Separate Accounting was overturned by the Supreme Court, so the state returned to worldwide apportionment awaiting case resolution. The Alaska Supreme Court upheld the states right to collect Corporate Income Tax via Separate Accounting in 1985. Oil companies then appealed to the U.S. Supreme Court which dismissed the appeal because Alaska's Separate Accounting law did not raise any federal constitutional or statutory question. Since that time, Alaska has not availed itself of its right to calculate oil company corporate income tax based on profits made in Alaska.

It was estimated that, during for the four years in which the state required Separate Accounting, the state received an additional $1.8 billion, or $450 million per year. If we multiply $450 million by the 30 years that we have not collected Corporate Income Tax through Separate Accounting, this equals approximately $13.5 billion in lost revenue to the state.

http://www.RepPaulSeaton.com
Email: Rep_Paul_Seaton@legis.state.ak.us

According to a 2000 testimony by Dan Dickenson with the Department of Revenue, Alaska lost $4.6 Billion from 1982 – 1997 by not utilizing Separate Accounting.

International energy consultant Pedro Van Meurs, who has advised Alaska and numerous jurisdictions on modifications to their petroleum tax regimes, is a strong supporter of calculating state corporate tax based on costs and revenues attributed to oil production in Alaska. Other jurisdictions such as Norway utilize separate accounting. All of the major producers operating in Alaska have been complying with the separate accounting terms in those jurisdictions.

Government Take is used for comparative attractiveness of investment in different jurisdictions. Alaska's rate of 9.4% is used for Corporate Income Tax in these comparisons. Since 9.4% is used for these comparisons we should be collecting the 9.4% tax on the profits made in Alaska.

State of Alaska
Department of Revenue

Commissioner Bryan Butcher

SEAN PARNELL, GOVERNOR
333 Willoughby Avenue, 11th Floor
P.O. Box 110400
Juneau, Alaska 99811-0400
Phone: (907) 465-2300
Fax: (907) 465-2389

The Honorable Paul Seaton
Alaska State Representative
State Capitol, Room 102
Juneau, Alaska 99801

April 3, 2012

Re: CS for House Bill 328 version I - Separate Accounting

Dear Representative Seaton:

As requested, we reviewed the CS to House Bill 328 which was drafted after taking into consideration our comments and concerns in our March 15, 2012 letter and further comments and concerns we voiced during meetings with you and your staff. The CS, as drafted, addresses some, but not all of our concerns and most of the policy issues we identified in our previous letter do not appear to be addressed at all. In addition, new language added in some areas of the bill have increased the bill's confusion and complexity. We have reiterated those items that we identified in our previous letter and discussions which we believe have not been addressed in the CS and identified other concerns we have because of new language inserted in the CS. We have also expanded on some of the issues that were discussed previously.

A. The previous version of the bill allowed the Department to require estimated tax payments, but there was no statutory penalty for failure to make those payments. We suggested adding language to impose a penalty, as under the Internal Revenue Code (IRC) Sec. 6655, using Alaska interest rates. Language has been added to require estimated tax payments per the IRC, but the estimated tax "penalty" was added by including substantially all of the language covering estimated payments and penalties from AS 43.55, the production tax. These provisions do not fit well together and cause additional confusion. Specifically, the use of a March 31 date conflicts with the IRC which specifies a tax payment due date of March 15. In addition, estimated tax payments are required to be made monthly for production tax whereas the IRC requires corporations to make quarterly estimated tax payments.

B. The language in sections 3 and 5 of the bill state that a corporation is subject to AS 43.21 (separate accounting) only if the corporation is engaged in the production or transportation of crude oil or natural gas. Our understanding of this language is that a company that is engaged in the exploration and/or development of an oil or gas lease in Alaska must calculate its taxable income based on water's edge formulary apportionment under AS 43.20.073. During discussions with you, we voiced our concerns with the fact that oil and gas

exploration companies would not be able to write off expenses incurred in Alaska for those exploration and development activities conducted prior to production as there is no provision in this bill that allows net operating losses calculated under AS 43.20 to offset income under AS 43.21. This concern has not been addressed in the CS.

C. Lease acquisition payments, petroleum property taxes, and interest incurred prior to production would not be allowed to be deducted against future production income. Although language in AS 43.21.210(c)(6) allows amortization of lease acquisition payments, petroleum property taxes, and capitalized interest before commencement of commercial production, AS 43.21.210(d) specifically disallows a deduction for items that were expensed under AS 43.20. In addition, there is no language that requires these expenses to be capitalized and there is no language dictating how amortization is to be calculated.

D. There is no language that requires certain property to be capitalized and depreciated. AS 43.21.210(c)(5) allows depreciation on property required to be capitalized under the Internal Revenue Code, but this language does not require property to be capitalized for Alaska tax purposes. In the preceding paragraph, AS 43.21.210(c)(4), corporations are allowed to deduct all direct costs. As there is no language that requires property to be capitalized, corporations could deduct the entire cost of property used on a producing lease in the year the property was acquired and also take depreciation on that same property if the property was required to be capitalized under the IRC.

E. AS 43.21.210(c)(7) allows interest expense to be deducted provided the interest was not capitalized during construction. As there is no language in AS 43.21 that requires interest expense to be capitalized during construction, this language makes no sense. If it is the intent of the bill sponsor to require interest to be capitalized during the construction phase, language is needed. Additionally, if the construction phase of a project takes place prior to production, that activity is required to be reported under AS 43.20. There is no language in this bill that addresses how capitalized interest and other items, such as depreciable property that was reported while the company was subject to AS 43.20 is suppose to be treated once a company is subject to AS 43.21.

F. AS 43.21.210(c)(8) allows expenses that were incurred on dry holes, abandoned wells, and unsuccessful exploration to be deducted from gross income. However, those expenses would have already been deducted in the calculation of taxable income under AS 43.20 if they were incurred in a year prior to when the corporation began producing. AS 43.21.210(d) specifically prohibits expenses that were deducted on a return filed under AS 43.20 to be deducted in the computation of taxable income under AS 43.21. The real problem here is that there is no provision to address net operating losses that an oil and gas exploration company incurred prior to production.

G. The education tax and film production tax credits are not allowed as credits against the tax due under AS 43.21. Was this your intent?

H. Under current law, the Internal Revenue Code is adopted, which provides rules for intercompany transactions within the federal consolidated filing corporate group. It is our understanding from conversations with you that the intent is that all expenses incurred by a corporation or any member of the corporation's consolidated business that were for oil and gas production or transportation activity in the state will be allowed as a deduction. However, the way the language is constructed, only those corporations that derive income from oil or gas production or transportation in the state are subject to AS 43.21. If expenses are incurred by a sister corporation in support of the production company, but the sister corporation is not a producer, then the sister corporation must calculate its Alaska corporate income tax liability under AS 43.20. There is no mechanism in the language to allow these deductions in the computation of tax due under AS 43.21.

I. Decoupling from the IRC causes several uncertainties and potential unintended consequences. Following are some examples of unintended consequences. Please keep in mind that these examples are not all inclusive and many other unintended consequences could surface over time.

(1) Under IRC Sec. 162(f), fines and penalties paid by a corporation to a government for the violation of any law are not deductible in the calculation of taxable income. If fines and penalties incurred by a corporate income taxpayer under AS 43.21 are a direct lease expense, they are allowed as a deduction.

(2) Subchapter S Corporations engaged in oil and gas production in Alaska are not currently subject to Alaska's corporate income tax. They will be subject to Alaska corporate income tax under AS 43.21.

(3) Intangible drilling costs are required to be capitalized and depreciated under current Alaska corporate income tax. Under AS 43.21, these expenses will be allowed to written off in the year in which they are incurred. However, if these expenses were incurred prior to production, they will not be allowed to be written off at all.

(4) Dividend income received by a parent corporation from a subsidiary producing or transporting oil or gas in Alaska may or may not be taxable. We are uncertain as to the sponsors intent regarding this type of income.

(5) The bill does not require an amended return if there is a federal audit or federal amended return.

(6) Charitable contributions made by a corporation solely engaged in oil and gas production activity do not appear to be deductible.

(7) Federal law requires that capital gains and losses be separated into specific "baskets" with specific rules for netting of those gains and losses. We are unable to determine the correct gain calculation where there are, for example, capital losses in the "Other" group and capital gains in Production or Pipeline group of activities.

(8) The taxable income from "Other" activities is equal to the Federal Taxable Income, but the statute does not "adopt" the Internal Revenue Code, Treasury Regulations, and federal Rulings. It is unclear what the sponsor's intent is, with respect to application of tax accounting rules. In addition, I would also note that this also means that we would no longer adopt federal penalties, such as the Substantial Understatement penalty or the Erroneous refund penalty.

We did our best to analyze this bill as quickly as possible and identified those issues of which we are most concerned. We will continue to analyze the bill and provide you additional feedback as our analysis continues. If you have questions about this letter or corporate income taxes in general, please contact Johanna Bales at 269-6628 or Robynn Wilson at 269-6634 of the Tax Division.

Sincerely,

Bruce Tangeman
Deputy Commissioner

State of Alaska
Department of Revenue

Commissioner Bryan Butcher

SEAN PARNELL, GOVERNOR
333 Willoughby Avenue, 11th Floor
P.O. Box 110400
Juneau, Alaska 99811-0400
Phone: (907) 465-2300
Fax: (907) 465-2389

The Honorable Paul Seaton
Alaska State Legislature
State Capitol, Room 102
Juneau, Alaska 99801

March 16, 2012

Re: House Bill 328 - Separate Accounting

Dear Representative Seaton,

We were asked to provide suggestions to make the bill workable from a Tax Administration standpoint. I have listed five suggestions below (Items A-E). Unfortunately, there are several areas where we are unable to offer suggestions because the sponsor's intent is not known. I have listed those items below as Policy Issues (Items 1-6).

A. The bill mirrors old Chapter 21, which started with the same revenue point as Production Tax. However, Production Tax in 1978 was not a tax on net profits. At the current time, Production Tax is calculated with specific deductions as allowed under AS 43.55.165. The bill, as drafted, uses the original separate accounting deductions. The deductions, although similar, are not the same as those allowed for Production Tax. This potentially produces a mismatch of allowable expenses, and greatly increases complexity in administration.

Suggestion: Consider defining "Taxable income from oil and gas production" as Production Tax Value under Chapter 55

B. Sec. 43.21.340 allows the Department to require estimated tax payments, but there is no statutory penalty for failure to make those payments

Suggestion: Add language to impose penalty, as under the Internal Revenue Code Sec. 6655, using Alaska interest rates.

C. Sec. 43.21.330 requires the Department to calculate taxable income and send the taxpayer an "assessment" by August 15. This is generally not a workable mechanism for income tax; it is more commonly used in property tax.

Suggestion: Require the taxpayer to calculate its tax and file a tax return 30 days after the taxpayer files its federal return. (See current 43.20.030)

D. Page 3, line 17 requires depreciation be calculated on a "percentage depletion basis." It is unclear how such a depreciation method would work. This is not a customary depreciation method for either book purposes or tax purposes. Further, it is my understanding that Percentage Depletion allows recovery in excess of cost. We note that the old (repealed) Chapter 21 required the use of the Unit of Production method, which is an acceptable (though not common) method of depreciation.

Suggestion: If Suggestion A above is not adopted, then change "percentage depletion basis" to "unit of production method" (as in old Chapter 21) or on the basis of IRC Sec167, as it read on 6/30/81 (as in current 43.20.072) or simply on the basis of Sec. 167.

E. Because current 43.20.072 requires that an asset be capitalized and depreciated over its useful life, taxpayers will have unamortized basis at the point that Separate Accounting would be effective.

Suggestion: Provide a transition rule to allow a taxpayer to write off its remaining Alaska basis over a period of five years.

Policy Issues: As noted above, there are several other areas which will require a policy call, and so we are unable to make a workable suggestion until we understand the sponsor's intent:

In essence, the bill divides the corporate group into three baskets: Production activities, Pipeline activities, and Other. The taxable income of the "Other" group is Federal Taxable Income (under the Internal Revenue Code) while taxable income of the Production and Pipeline activities are accounted for under state-specific rules. This division of the corporate group yields several difficulties:

1. Under current law, the Internal Revenue Code is adopted, which provides rules for intercompany transactions within the federal consolidated filing corporate group. The bill, as drafted, de-couples certain parts (not even certain corporations) from the measurement of federal taxable income. It is unclear how any intercompany transaction should be accounted for where the transaction occurs between a company engaged in Production activities and a company engaged in Other (non-production) activities. This is true for revenue/expense items such as interest, engineering fees, and other services. It also applies to recognition of certain gains/losses on intercompany sales of assets within the corporate group. We are unable to determine sponsor's intent in this area.

2. Similar to Item 1 above, the Internal Revenue Code provides direction on the deduction of intercompany dividends. We are unable to determine the correct potential treatment of dividends paid between a company engaged in Production activities and a company engaged in Other (non-production) activities, under the bill, as drafted.

3. Federal law (currently adopted) requires that capital gains and losses be separated into specific "baskets" with specific rules for netting of those gains and losses. We are unable to determine the correct gain calculation where there are, for example, capital losses in the "Other" group and capital gains in Production or Pipeline group of activities.

4. If the "Other" group of activities includes a federal deduction for charitable contributions, it is unclear how "taxable income" will be calculated for purposes of properly limiting the charitable contribution. For federal purposes, this is calculated on the consolidated Federal Taxable Income amount. For current state purposes, it is calculated based on the taxable income of the unitary combined group.

De-coupling from the Internal Revenue Code will present other uncertainties from a policy standpoint:

5. If an asset is sold in, for example, Year 2 of its useful life, the Internal Revenue Code requires the calculation of a taxable gain, commonly known as "depreciation recapture." Since this bill appears to allow immediate write-off of Production activity assets, it is unclear whether the sponsor intends that there be a gain calculated and taxed.

6. The taxable income from "Other" activities is equal to the Federal Taxable Income, but the statute does not "adopt" the Internal Revenue Code, Treasury Regulations, and federal Rulings. It is unclear what the sponsor's intent is, with respect to application of tax accounting rules. In addition, I would also note that this also means that we would no longer adopt federal penalties, such as the Substantial Understatement penalty or the Erroneous refund penalty.

This list is not all-inclusive, but is intended to reach the big-picture items.

If you need further assistance, please contact Johanna Bales at 269-6628 or Robynn Wilson at 269-6634 of the Tax Division.

Sincerely,

Bruce Tangeman
Deputy Commissioner

AOGA

OIL & GAS:
FUELING
ALASKA'S
ECONOMY

House Resources Committee

March 16, 2012

Kara Moriarty, Executive Director

AOGA Member Companies

Corporate Income Taxes

Question:
How much income of a multistate or international business is properly attributable to its in-state assets and activities so it can be taxed by that state?

Separate Accounting

Looks at what the business actually has and does in the state and then seeks to determine directly the net-income as if that in-state portion of the business stood alone – separate from the rest of the business.

Separate Accounting

Challenges:

- In-state portion of a business does not actually stand alone from the rest of the business.

- Very complicated and difficult to unravel transactions between or among parts of the same overall business.

- IRS has intense, detailed regulations governing transactions between corporate affiliates, which separate accounting requires.

Apportionment

Starts with a "pie" containing the apportionable income for the in-state and outside business together and then determines how wide a "slice" is attributable to the income-generating potential of the in-state portion of the business. It is the "slice" that is then taxes by the state.

Apportionment

- Avoids the need to unravel transactions.

- Avoids the analytical difficulties that arise when a unitary business as a whole is greater than the sum of its individual parts.

- The width of a company's "slice" of their respective business's "pie" is the average of the percentages of that business's real or tangible property (at cost), its sales, and its oil and gas production that is present within the state.

TOP FIVE OIL COMPANIES
CORPORATE INCOME TAX COMPARISON

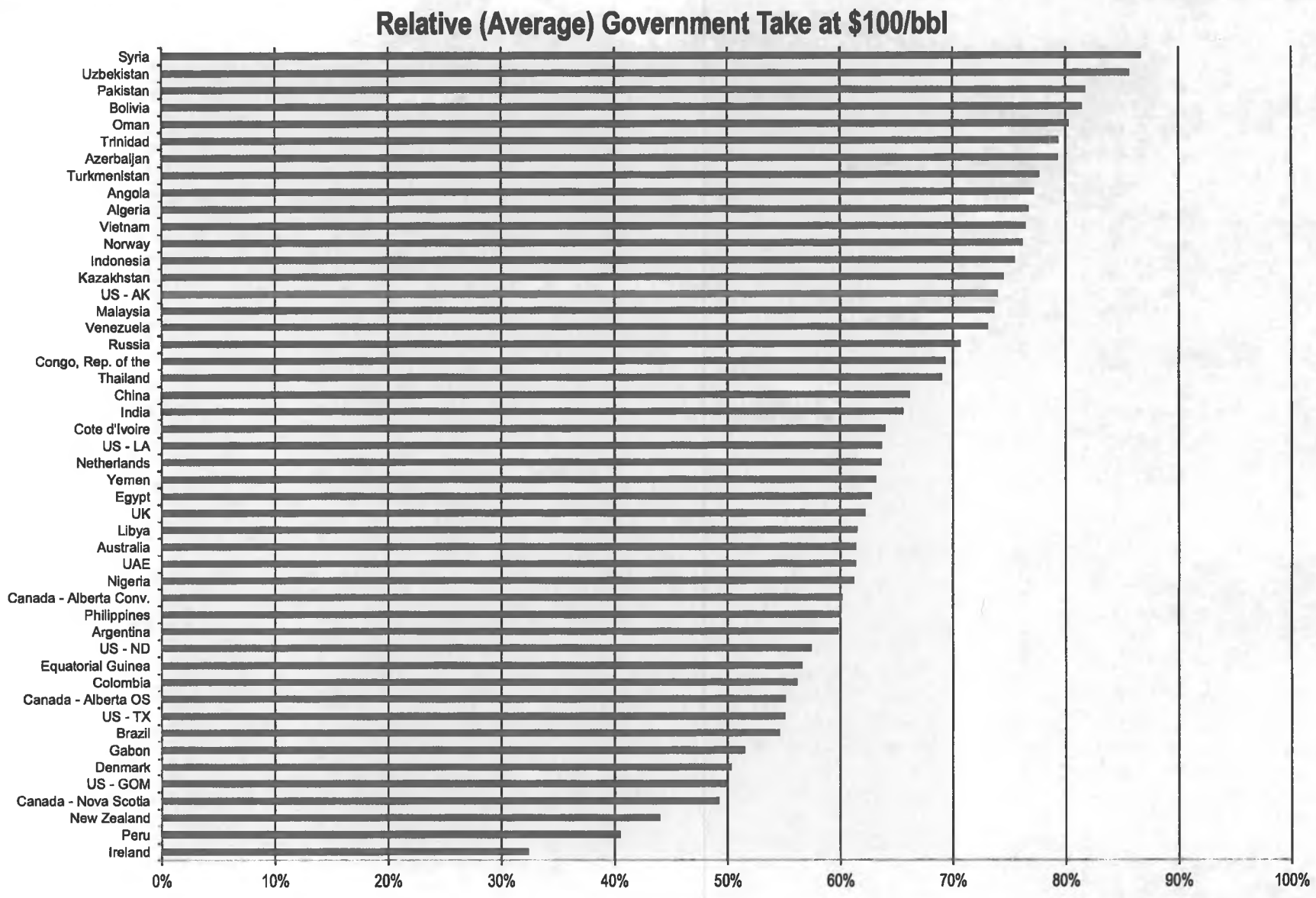
	2006	2007	2008	2009	2010	Avg.
Production Tax Value (PTV)	8,269,253,754	12,373,309,410	16,639,085,462	8,123,576,735	10,267,505,397	
Production Tax net of Credits	1,648,686,505	3,486,434,327	7,121,145,726	2,033,891,379	3,023,427,665	
PTV net of Production Tax/ Subtotal Production Income	6,620,567,249	8,886,875,083	9,517,939,736	6,089,685,356	7,244,077,732	
Transportation Income *	(24,892,884)	186,438,182	(653,974,506)	(456,078,939)	(454,804,489)	
Taxable Income **(A)**	6,595,674,365	9,073,313,265	8,863,965,230	5,633,606,417	6,789,273,243	
Tax @ 9.4% **(B)**	619,993,390	852,891,447	833,212,732	529,559,003	638,191,685	
Actual Corporate Income Tax Paid **(C)**	630,307,274	570,389,248	642,563,992	293,204,318	385,633,537	
Difference **(B - C)**	(10,313,884)	282,502,199	190,648,740	236,354,685	252,558,148	190,349,978
Effective Tax Rate Paid **(C /A)**	9.6%	6.3%	7.2%	5.2%	5.7%	

* Using FERC Form 6, Net Carrier Operating Income. Certain companies may include Transportation activities outside of Alaska.

(A) Taxable income does not include apportioned other income.

(C) Certain 2006-2008 returns are audited and/or amended.

Regime Competitiveness: Relative Government Take



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May 2011

Vol. 16, No. 19 **Week of May 08, 2011**

Eagle Ford could nudge Alaska for COP

ConocoPhillips' plans to invest $2 billion this year on liquids-rich shale plays could mean the Lower 48 edges out Alaska oil

Eric Lidji

For Petroleum News

ConocoPhillips' most recent quarterly report presented a typical view of the Houston major's exploration and production activities in the United States, but not a complete one.

Discussing the future with analysts in late March, company executives suggested that the balance between Alaska and the Lower 48 might be changing in the coming years.

For a while now, ConocoPhillips has earned more from its exploration and production activities in Alaska than it has in the Lower 48, sometimes a little and sometimes a lot.

Of the $2.7 billion the company earned from E&P worked in the United States last year, $1.7 billion came from Alaska and the rest came from the Lower 48. In the first quarter of 2011, the company earned $549 million in Alaska and $314 million in the Lower 48.

Those earnings don't reflect production levels, though.

ConocoPhillips produced 629,000 barrels of oil equivalent per day in the first

quarter, or 364,000 bpd of oil and natural gas liquids and 1.6 billion cubic feet of natural gas.

That production is lopsided by region. In the Lower 48, ConocoPhillips produced 150,000 bpd of oil and 1.5 billion cubic feet of natural gas per day, while in Alaska the company produced 214,000 bpd of oil and 67 million cubic feet of natural gas per day.

Alaska is usually more profitable for ConocoPhillips because oil trades at a premium to natural gas. And with the delivered price of Alaska North Slope crude oil at around $123 per barrel and Henry Hub at around $4.60 per mcf, that spread has rarely been wider.

So when you crunch the numbers, Alaska accounted for about 63 percent of ConocoPhillips' U.S E&P profits and 35 percent of its production in the first quarter.

COP investing in shale

That balance could flip in the next few years, though.

ConocoPhillips is investing heavily in three liquids-rich shale plays in the Lower 48 this year, the Eagle Ford of South Texas, the North Barnett of North Texas and the Bakken of North Dakota, and also plans to ramp up operations in the Permian basin of West Texas.

The company plans to spend $2 billion in those plays this year to produce some 170,000 barrels of oil per day by 2013, Greg Garland, senior vice president for exploration and production in the Americas, said at the March analysts meeting. That target, if achieved, would push the Lower 48 ahead of Alaska, both in terms of production and profits.

Like many companies, ConocoPhillips is incredibly bullish about liquids-rich Lower 48 shale right now and plans to drill 450 gross wells across the four plays this year. That's in addition to the 240 wells the company plans to drill in "other competitive areas."

13 rigs in Eagle Ford this year

In the Eagle Ford alone, ConocoPhillips budgeted $1.4 billion this year, with plans to run 13 rigs and three dedicated hydraulic fracturing crews to drill 144 wells on 220,000 acres with the goal of producing 30,000 boe per day by the end of the year, 75 percent liquids.

"The Eagle Ford is a game changer," Garland said. "It's a game changer for the industry and for our company."

In the Bakken, ConocoPhillips holds 460,000 acres with a resource potential of

400 million barrels of oil equivalent and more than 1,700 "high-value drilling opportunities."

ConocoPhillips expects to produce 20,000 boe per day from the Bakken this year.

ConocoPhillips budgeted $400 million in the Permian basin and North Barnett Shale this year. The company holds 65,000 acres with a resource potential of some 200 million barrels of oil equivalent in the North Barnett, and more than 1 million acres with a resource potential of 700 million barrels of oil equivalent in the prolific Permian basin.

ConocoPhillips expects to produce 65,000 boe per day from the two plays this year.

Alaska budget flat

By comparison, ConocoPhillips "will invest $350 million in exploitation this year, all at very good returns," Garland said. ConocoPhillips budgeted $900 million for capital expenses in Alaska this year, but expects actual spending to be somewhat lower.

"We expect ConocoPhillips Alaska's 2011 capital budget spending to be basically flat from 2010," ConocoPhillips spokeswoman Natalie Lowman told Petroleum News in February. "The 2011 capital budget includes contingency funding if we are successful in getting improvements in State fiscal terms, and resolving permitting issues with Alpine satellites." ConocoPhillips spent $730 million in 2010, its lowest level since 2007.

ConocoPhillips did not drill any traditional North Slope exploration wells this winter or last winter, but maintains ventures, such as the Alpine West satellite and Chukchi Sea prospects that it plans to pursue as soon as it overcomes permitting and legal hurdles.

Garland said ConocoPhillips still likes its "strong cash margins" in Alaska, as well as its "significant infrastructure position" and "extensive operating capability."

Shale plays remain immature

ConocoPhillips likes the Eagle Ford because of economics.

Garland said the play offered $45 per barrel margins last year, twice the average of ConocoPhillips' global portfolio. Since January 2010, well costs have fallen 40 percent.

Those plays face some obstacles, though, particularly in the short term.

Garland said that resources like rigs and hydraulic fracturing crews are "stretched

thin" in the Eagle Ford, and CFO Jeff Sheets said that some production in the Eagle Ford could remain shut-in until pipeline infrastructure catches up to drilling levels, around 2013.

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Memorandum

TO: Representative Paul Seaton

FROM: Chuck Burnham, Legislative Analyst

DATE: February 28, 2012

RE: ConocoPhillips: Net Exploration and Production Income and Income Taxes by Selected Jurisdiction
LRS Report 12.198

You asked for an account of the net exploration and production income and income taxes paid by ConocoPhillips Company for every year in which financial information for Alaska operations were delineated from that of other jurisdictions[1]. You further asked that we make certain calculations based on that information.

Prior to its August 2002 merger with Phillips Petroleum, Conoco was not an independent publicly traded company and was therefore not required to file the extensive financial disclosure documents required by the U.S. Securities and Exchange Commission (SEC).[2] Upon the completion of the merger, the combined company became ConocoPhilllips (hereafter identified by its stock symbol "COP" and began having its stock traded on the New York Stock Exchange). Among the annual SEC filings required of public companies is the form "10-K," which includes extensive financial and operations information. We gleaned all of the information in this report from the 10-K filings of COP from its first report in 2003 through the most recent report in 2011.

Table 1 (following page) shows selected net exploration and production (E&P) income and income tax information for COP for the eleven years 2000-2010.[3] In accordance with your request, the table also includes our calculation of Alaska net E&P income as a percentage of U.S. and overall net E&P income. As you can see, COP's Alaska net E&P income ranged from $829 million in 2000 to $2.55 billion in 2005.[4] Similarly wide variability in profit was seen across the jurisdictions in which COP operates, with total U.S. net E&P income ranging from $1.15 billion in 2002 to nearly $5 billion in 2008. (Please note that net E&P income figures for 2009 do not reach 100 percent in Figures 2 and 4 for 2009 because the company lost $37 million in its lower 48 operations. Therefore, in effect, Alaska represented the total of domestic net E&P income for that year.)

Alaska income taxes are not specifically delineated but rather included in the category "state and local" income taxes. Those taxes ranged from $21 million in 2002 to $621 million in 2005.[5] Federal income taxes for U.S. operations varied from $120 million in 2002 to $4.26 billion in 2007. Following Table 1 are a series of figures that graphically illustrate COP's net E&P income and income taxes by selected jurisdiction.

We hope this is helpful. If you have questions or need additional information, please let us know.

---

[1] Exploration and production are "upstream" activities and exclude "downstream" activities such as refining and marketing.

[2] Technically, Conoco was acquired by Phillips Petroleum; however, this was largely for accounting purposes. Phillips, although publicly traded prior to the merger, did not report Alaska financial information separately from that of other U.S. operations.

[3] Although the merger did not occur until 2002, the SEC requires companies new to the Commission's regulation to include data from the immediate two years prior to becoming publicly traded.

[4] All dollar figures are rounded.

[5] The unusually low domestic tax collections in 2002 are likely a product of write-offs and deferrals taken as part of the merger process.

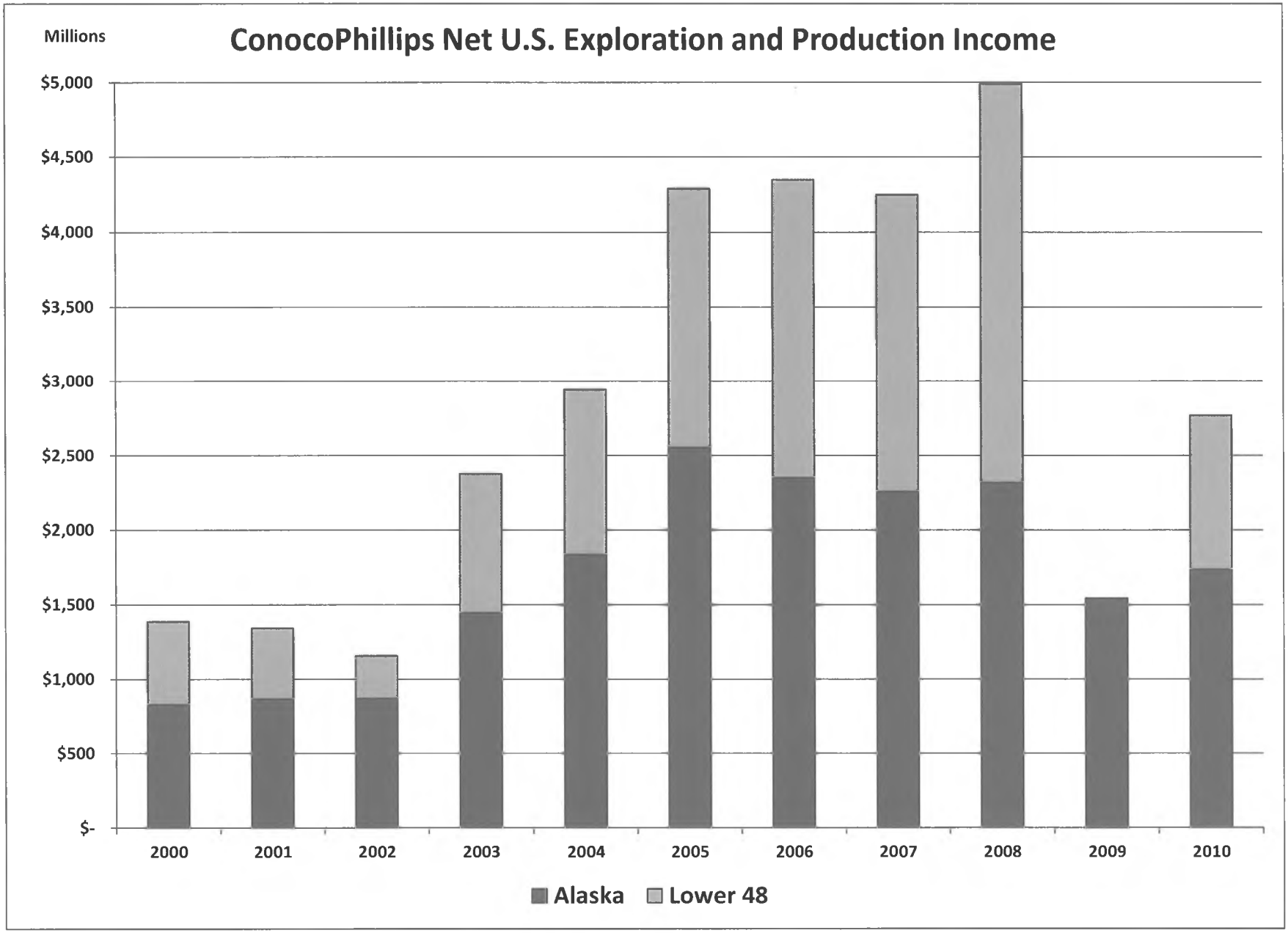
Table 1: ConocoPhillips: Net Exploration and Production Income and Income Taxes

(Millions of Dollars)

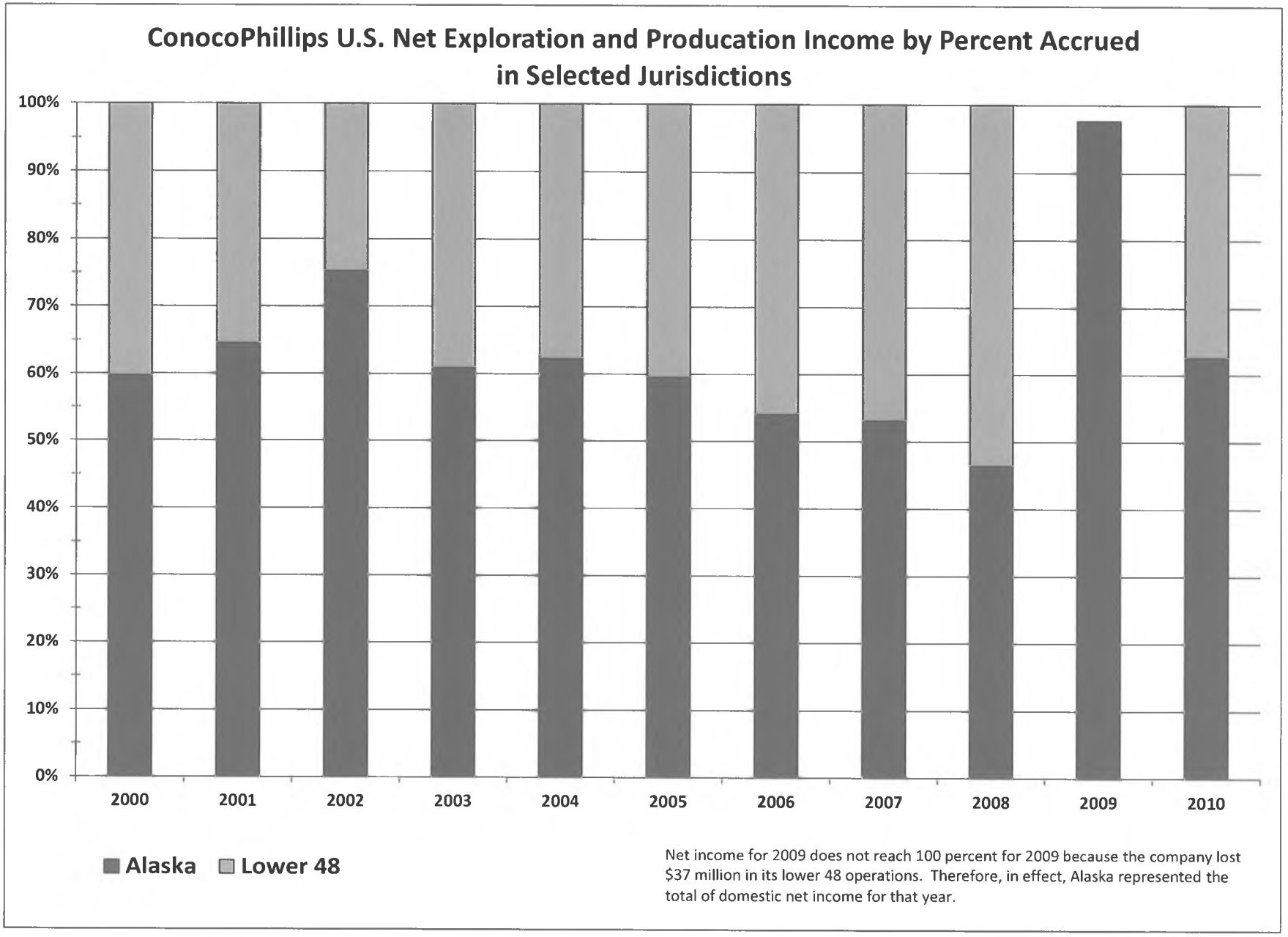
Net Income												
Jurisdiction	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**Totals**
Alaska	$ 829	$ 866	$ 870	$ 1,445	$ 1,832	$ 2,552	$ 2,347	$ 2,255	$ 2,315	$ 1,540	$ 1,735	$ 829
Lower 48	$ 559	$ 476	$ 286	$ 929	$ 1,110	$ 1,736	$ 2,001	$ 1,993	$ 2,673	$ (37)	$ 1,033	$ 559
U.S. Total	$ 1,388	$ 1,342	$ 1,156	$ 2,374	$ 2,942	$ 4,288	$ 4,348	$ 4,284	$ 4,988	$ 1,503	$ 2,768	$ 1,388
International	$ 557	$ 357	$ 593	$ 1,928	$ 2,760	$ 4,142	$ 5,500	$ 367	$ 6,976	$ 2,101	$ 6,430	$ 557
Total	$ 1,945	$ 1,699	$ 1,749	$ 4,302	$ 5,702	$ 8,430	$ 9,848	$ 4,615	$11,964	$ 3,604	$ 9,198	$ 1,945
Income Taxes												
State & Local	$ 114	$ 117	$ 21	$ 173	$ 269	$ 621	$ 574	$ 564	$ 431	$ 124	$ 317	$ 114
Federal	$ 694	$ 555	$ 120	$ 1,173	$ 2,335	$ 3,809	$ 4,236	$ 4,256	$ 3,018	$ 627	$ 2,093	$ 694
International	$ 1,092	$ 968	$ 1,302	$ 2,398	$ 3,658	$ 5,477	$ 7,973	$ 6,561	$10,316	$ 4,339	$ 5,923	$ 1,092
Total	$ 1,900	$ 1,640	$ 1,443	$ 3,744	$ 6,262	$ 9,907	$12,783	$11,381	$13,765	$ 5,090	$ 8,333	$ 1,900
Selected Calculations												
Alaska Net Income as Percent of Overall Total	42.6%	51.0%	49.7%	33.6%	32.1%	30.3%	23.8%	48.9%	19.3%	42.7%	18.9%	42.6%
Alaska NetIncome as Percent of U.S. Total	59.7%	64.5%	75.3%	60.9%	62.3%	59.5%	54.0%	52.6%	46.4%	100.0%	62.7%	59.7%

Notes: Exploration and production are "upstream" activities and exclude "downstream" activities such as refining and marketing.

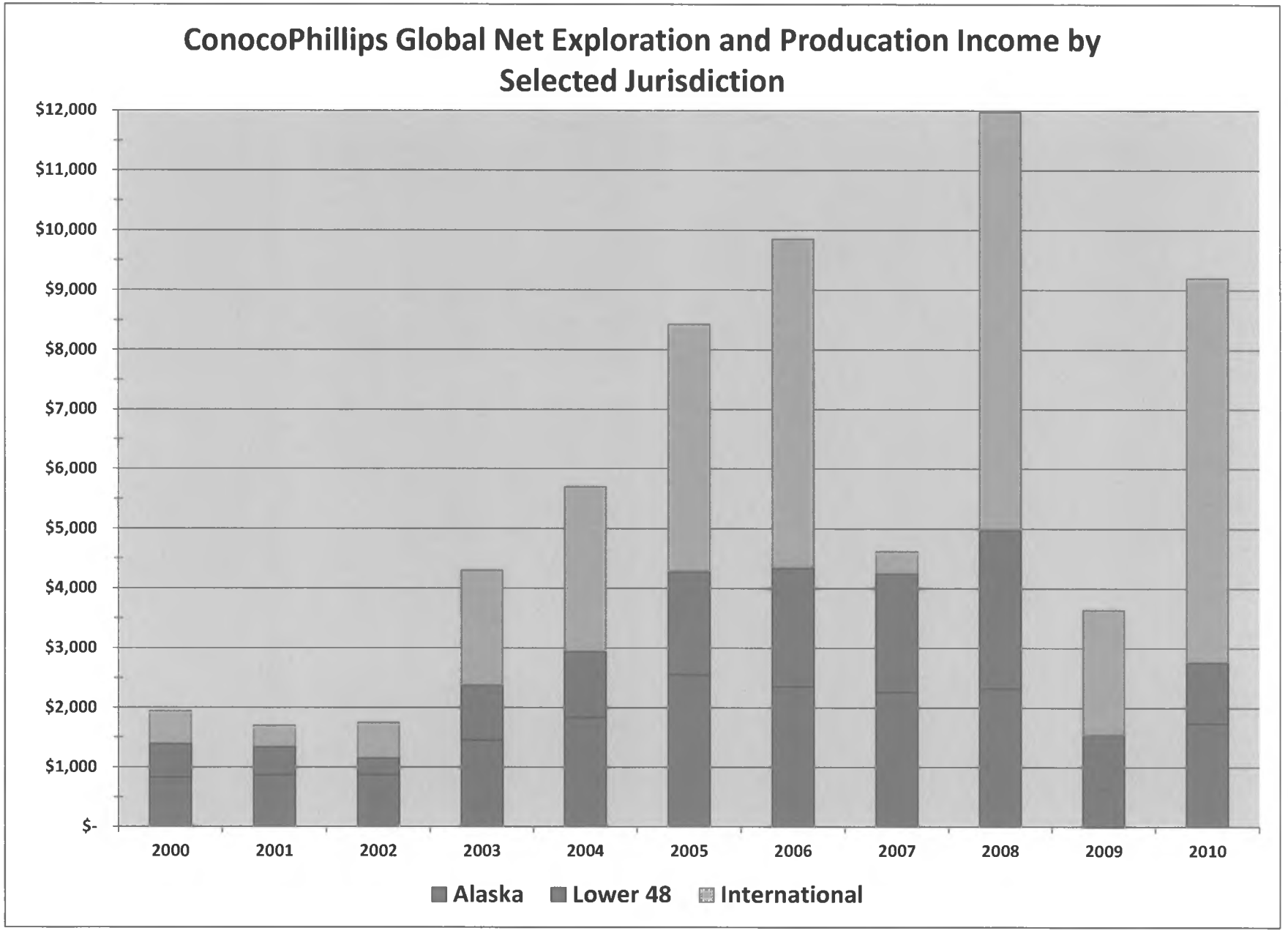
Source: Annual filings of form 10-K with the U.S. Securities and Exchange Commission posted to the EDGAR online database, *http://www.sec.gov/edgar/searchedgar/webusers.htm* .



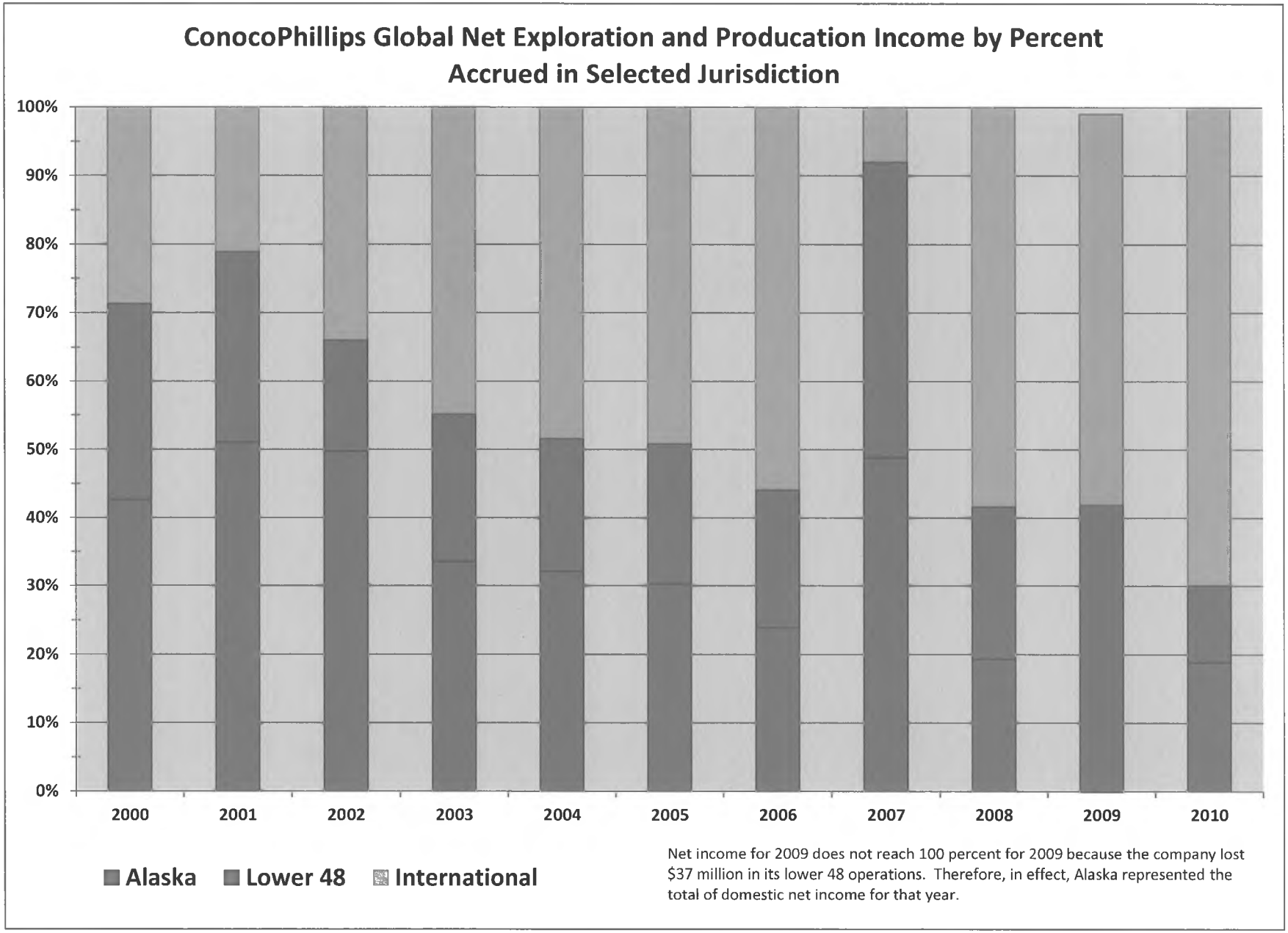
Legislative Research Services Report 12.198, Figure 1, February 2012



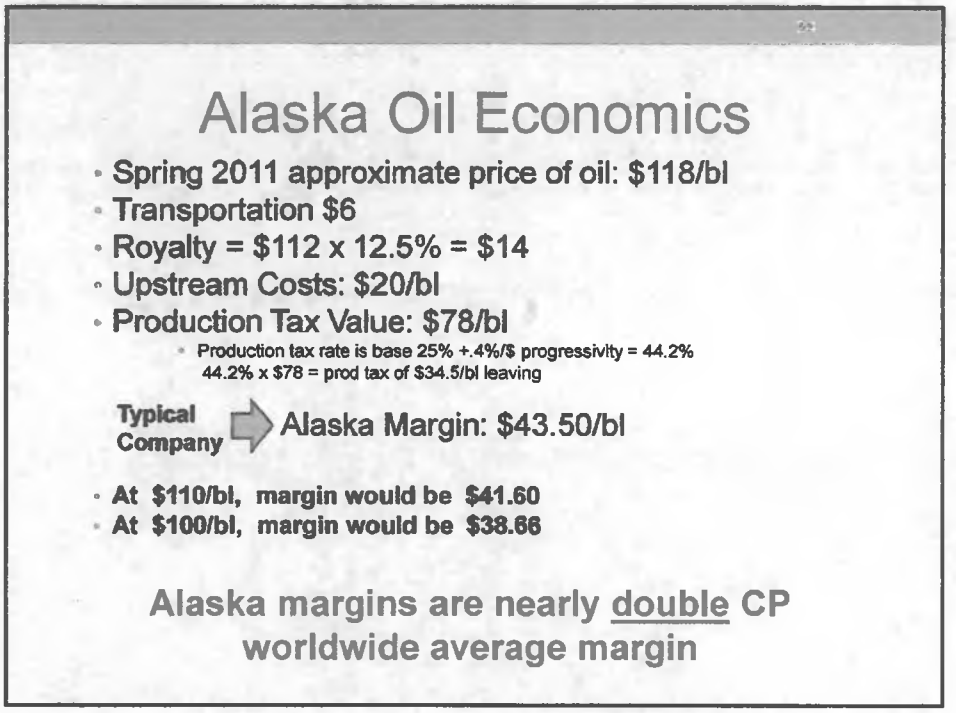
Legislative Research Services Report 12.198, Figure 2, February 2012



Legislative Research Services Report 12.198, Figure 3, February 2012



Legislative Research Services Report 12.198, Figure 4, February 2012



Alaska is close to Eagle Ford at nearly twice the global portfolio average margin. Therefore, comparative oil profits do not explain the low reinvestment rate for Alaska. The companies tell us that each has its own 'hurdle rate' for return on investment before a project can be profitable enough to be selected for investment. Obviously, nearly double the margin of funded projects pass that test.

We now know that the upstream cost for ConocoPhillips is only $15.48/bl in Alaska instead of the assumed $20/bl. This means that an additional $4.52 per barrel is added to the typical company margin, making ConocoPhillips' Alaska Margin **$48.02/bl.**

"On average, it costs ConocoPhillips $15.48 to produce a barrel of oil in Alaska" – Mary Ann Kah, ConocoPhillips' Chief Economist
January 15th, 2012 Alaska Journal of Commerce *Slope producers lay out scenario with proposed oil changes*

Slide prepared by the office of Representative Seaton. Full presentation available at http://housemajority.org/seaton/pdfs/27/HB_110_Aces_or_Not_11292011.pdf

1 of 1 DOCUMENT

Atlantic Richfield Co. v. State

File No. S-52; No. 2965

Supreme Court of Alaska

705 P.2d 418*; *1985 Alas. LEXIS 295*; *86 Oil & Gas Rep. 406

August 16, 1985

SUBSEQUENT HISTORY: [**1] As Amended.

PRIOR HISTORY: Appeal from the Superior Court of State of Alaska, Third Judicial District, Anchorage, Victor D. Carlson, Judge.

COUNSEL: J. W. Bullion, Ralph I. Miller, Thompson & Knight, Dallas, Texas; Mark L. Hazelwood, Robert E. McManus, Atlantic Richfield Co., Dallas, Texas; and William B. Rozell, John F. Clough, III, Faulkner, Banfield, Doogan & Holmes, Juneau, Alaska for Appellant Atlantic Richfield Co. and ARCO Pipe Line Co.

John F. Daum, Barton H. Thompson, Jr., M. Randall Oppenheimer, O'Melveny & Myers, Los Angeles, California; Barry L. Wertz, Archie Parnell, Exxon Co., U.S.A., Houston, Texas; and Robert J. Mahoney, Hartig, Rhodes, Norman, Mahoney & Edwards, Anchorage, Alaska, for Appellant Exxon Corp. and Exxon Pipeline Co.

David A. Nelson, Terrence G. Perris, James J. Maiwurm, Howard J. C. Nicols, Squire, Sanders & Dempsey, Cleveland, Ohio; William H. Lutz, Jr., Squire, Sanders & Dempsey, Miami, Florida; Richard H. Hahn, Standard Oil Co., Cleveland, Ohio; and Richard O. Gantz, Carl J. D. Bauman, Hughes, Thorsness, Gantz, Powell & Brundin, Anchorage, Alaska, for Appellant Sohio Alaska Petroleum Co., Sohio Pipe Line Co., and BP Alaska, Inc.

Mitchell Rogovin, George [**2] T. Frampton, Jr., Michael D. Lowe, Jeffrey Blattner, Rogovin, Huge & Lenzner, Washington, District of Columbia; Jonathan K. Tillinghast, Birch, Horton, Bittner, Monroe & Pestinger, Juneau, Alaska; John R. Messenger, Preston, Thorgrimson, Ellis & Holman, Anchorage, Alaska; Deborah Vogt, Kathyrn Kolkhorst, Assistant Attorneys General, Juneau, Alaska, and Norman C. Gorsuch, Attorney General, Juneau, Alaska, for Appellees.

J. Lawrence Blankenship and Donna E. Cox, Oklahoma City, Oklahoma, for Amicus Curiae State of Oklahoma, ex rel Oklahoma Tax Commission.

Robert H. Carpenter, Jr., Assistant Attorney General, William J. Guste, Jr., Attorney General of Louisiana, Baton Rouge, Louisiana, for Amicus Curiae State of Louisiana.

Robby R. Long, Jackson, Mississippi, for Amicus Curiae Mississippi State Tax Commission.

JUDGES: Burke, Chief Justice, Rabinowitz, Matthews, and Moore, Justices. Compton, Justice, not participating.

OPINION BY: BURKE

OPINION

[*420] This is an appeal brought by several major oil producing companies in Alaska [1] challenging the constitutionality of the Oil and Gas Corporate Income Tax, Former AS 43.21 (repealed 1982) ("the Oil Tax"). [2] The issue is whether the State of [**3] Alaska must, as a matter of constitutional law, use the formula apportionment method to determine the portion of each corporation's worldwide oil production and pipeline transportation income that can be attributed to Alaska. During the tax years 1978 to 1981 the state used separate accounting, instead of formula apportionment, to determine taxable production and pipeline transportation income.

1 Atlantic Richfield Company and ARCO Pipeline Company (collectively "ARCO"), Exxon Corporation and Exxon Pipeline Company (collectively "Exxon"), and BP Alaska, Inc. and Sohio Pipe Line Company (collectively "Sohio").

2 AS 43.21 (Ch. 110, § 3, SLA 1978; am. ch. 113, §§ 28-32, SLA 1980; am. ch. 116, §§ 6-11, § 17 SLA 1981) was repealed effective January 1, 1982. Ch. 116, § 19, SLA 1981. For convenience, we refer to the Oil Tax by the former statutory section numbers throughout this opinion. *See* Appendix 1 for the full text of AS 43.21.

Various actions challenging the constitutionality of the Oil Tax were [**4] consolidated on August 27, 1980, in the superior court. [3] Appellants ARCO, Exxon, and Sohio argued below that the Oil Tax violated the commerce, due process, contract, and *equal protection clauses of the United States Constitution*, as well as the equal protection clause of the Alaska Constitution and the state constitutional and statutory provisions against retroactivity. They sought a refund of taxes paid under the Oil Tax.

3 Other oil companies were also involved initially in the litigation, but were dismissed upon agreeing to defer their constitutional claims pending resolution of this case.

On November 12, 1981, the state moved for summary judgment seeking a declaration that the Oil and Gas Corporate Income Tax Act is constitutional. The trial court rejected the oil companies' claims of unconstitutionality and granted the state's motion for summary judgment. We affirm.

I. THE OIL TAX

In 1959, Alaska adopted the three-factor apportionment formula of the Uniform Division of Income for Tax Purposes Act [**5] (UDITPA) to determine the share of income of an integrated (unitary) interstate business subject to Alaska income taxation. AS 43.20.130 (repealed 1975). [4] The apportionment formula relies on three indicators of business activity -- payroll, property and sales -- to compute Alaska's share of taxable income. *Id.* The value of property, payroll and sales in Alaska is compared to the value of property, payroll and sales of the corporation worldwide. The resulting ratio is then multiplied by the corporation's apportionable net income worldwide to arrive at an approximation of Alaska's share of taxable income.

4 In 1970, Alaska adopted the Multistate Tax Compact, enacted as *AS 43.19.010*. It is basically a restatement of UDITPA with a few minor changes. The three-factor apportionment formula is now described at *AS 43.19.010*, art. IV, §§ 9-15.

Prior to the enactment of the Oil Tax in 1978, all of the income tax liability of oil companies was determined under the formula apportionment method. Under the Oil [**6] Tax, a different methodology, separate [*421] accounting, [5] was implemented to calculate the production and pipeline transportation income subject to Alaska taxation. The goal of the separate accounting method was to determine that portion of the value of a barrel of oil attributable to the oil being produced, i.e., taken from the ground. AS 43.21.020.

5 The oil companies dispute whether the methodology of the Oil Tax is in fact "true" separate accounting. *See infra* section II. B.

The separate accounting of oil production income began with the determination of gross production revenue or "gross income." [6] The Oil Tax defined gross income as the value of the oil at the point of production, i.e., the wellhead price. AS 43.21.020(b). Essentially, gross income equalled the price at which the oil was sold, or could be sold, to a refinery less transportation expenses. AS 43.21.020(b). The price at which oil was sold, or could be sold, to a refinery obviously did not include refining and marketing [**7] costs and profits. These costs and profits were thus excluded in determining the gross income figure for Alaskan oil. In addition, a number of other costs were deducted from gross income. "Upstream" costs, such as exploration expenses, royalties, lease acquisition and development costs, and general overhead and administrative expenses, and "downstream" costs, such as transportation and marketing costs were deducted from gross income. AS 43.21.020(c). The end result was net production income, which was [*422] taxed at the 9.4% rate applicable to all other corporate income at that time. Former *AS 43.20.011* (amended, repealed and reenacted 1981).

6 The following graph, submitted by the State of Alaska, illustrates the estimated revenues, costs and profits contained in each barrel of Alaskan oil

during the years 1978-80:

[SEE ILLUSTRATION IN ORIGINAL]

The Oil Tax used a similar methodology to tax income from the pipeline transportation of oil and gas in Alaska. The items of income and expense related [**8] to Alaska pipeline transportation were keyed to the amount reported by the oil companies to the Federal Energy Regulatory Commission as net operating income. AS 43.21.030. The validity of this portion of the Oil Tax is also at issue in this case, though the parties focus primarily on the taxation of production income.

Under AS 43.21.040, all other income of the oil companies continued to be taxed under the UDITPA formula apportionment method. Such other income was primarily from marketing and refining operations. In computing this income, worldwide oil production and pipeline transportation income was subtracted from the total amount of income subject to apportionment by Alaska. Then the three-factor formula was applied, again with the production and pipeline income in Alaska deleted. The result attributed to Alaska a portion of worldwide refining and marketing income of the oil company approximating the share of such activities occurring in Alaska. This income, like the production and pipeline income, was taxed at the rate of 9.4%. Former *AS 43.20.011* (amended, repealed and reenacted 1981).

The Oil Tax was repealed effective January 1, 1982. Ch. 116, § 19, SLA 1981. It [**9] was replaced with a modified apportionment formula for the ensuing tax years. *AS 43.20.072*. The legislature took this step primarily to avoid a further increase in the possible $1.8 billion liability caused by this litigation.

II. THE OIL TAX IS "TRUE" SEPARATE ACCOUNTING

There are three basic methods by which the income of a multistate enterprise can be divided among the states entitled to tax the enterprise's income: separate accounting, specific allocation by situs and formula apportionment. The state claims the Oil Tax is true separate accounting, while the oil companies contend it is specific allocation by situs.

A. *The Three Methods For Division Of Income*

1. *Separate Accounting*

Separate accounting attempts to carve out of the taxpayer's overall business the income derived from sources within a single state, and by accounting analysis, to determine the profits attributable to that portion of the business. [7] Income within the state is determined without reference to the success or failure of the taxpayer's activities in other states. [8] In the case of goods (such as crude oil) sent to another state for processing, separate accounting values these goods at the price [**10] which could be obtained for them in their unprocessed form when leaving their state of origin. [9] In other words, separate accounting recognizes that crude oil has a marketable value before it is refined.

7 *See generally* J. Hellerstein, State Taxation: Corporate Income and Franchise Taxes para. 8.3, at 323 - 327 (1983).

8 P. Hartman, Federal Limitations on State and Local Taxation § 9.17, at 522 (1981).

9 G. Altman & F. Keesling, Allocation of Income in State Taxation 38 (2d ed. 1950).

2. *Specific Allocation by Situs*

Specific allocation by situs refers to the method of dividing a tax measure (in whole or in part) by tracing particular property, receipts, or income to their source state, and attributing the item *in its entirety* to that state. [10] This method is troublesome because more than one state is likely to have a legitimate basis for taxing the same item, especially when the tax is one measured by income. [11] The specific allocation [*423] method has been used commonly with [**11] "non-business" income such as income from dividends, patent and copyright royalties, and gains or losses from the sale of capital assets. [12] Under UDITPA, some non-business income of this nature is allocated in its entirety to the situs state. *See AS 43.19.010*, art. IV, §§ 5-8.

10 J. Hellerstein, *supra* note 7, para. 8.4, at 328.

11 *Id.*

12 *Id.* at 329.

Confusion may arise because the separate accounting methodology is very similar to the specific allocation approach. Both methods attempt to trace income to an identifiable source. The primary difference in the two methods is that separate accounting looks to the activities in the state and seeks to determine the income related to

that activity. Specific allocation attributes income according to situs, or some other specific characteristic of the business enterprise, rather than on the basis of where the income itself was earned. Moreover, specific allocation results in *all* of a specified type of income and *all* associated [**12] profits being allocated to one state. Separate accounting, on the other hand, attempts to segregate out *only* those profits attributable to activities within the state for taxation by that state.

3. *Formula Apportionment*

Formula apportionment is the method commonly used to divide the income of a unitary business [13] among various jurisdictions in which the business operates. The formula method, "unlike separate accounting, does not purport to identify the precise geographical source of a corporation's profits; rather, it is employed as a rough approximation of a corporation's income that is reasonably related to the activities conducted within the taxing State." [14] The formula method assumes that the total income of a business enterprise results from certain income producing factors - typically property, payroll and sales. The value of the corporation's property, payroll and sales within the taxing state is compared with the value of these factors outside the taxing state. The resulting ratio is then multiplied by the total apportionable net income worldwide of the multi-state corporation. [15]

13 "[A] unitary business may be defined simply as any business which is carried on partly within and partly [outside] the taxing jurisdiction." Keesling & Warren, *The Unitary Concept In the Allocation of Income,* 12 Hastings L.J. 42, 46 (1960).

[**13]

14 *Moorman Mfg. v. Bair, 437 U.S. 267, 273, 57 L. Ed. 2d 197, 204, 98 S. Ct. 2340 (1978).*

15 P. Hartman, *supra* note 8, § 9.18, at 523-524.

B. *The Oil Tax Is Separate Accounting*

The oil companies equate the Oil Tax with the specific allocation by situs method. They contend that the Oil Tax attributes *all* of the income and profits from oil production and transportation to Alaska. Their argument ignores the difference between the Oil Tax and the specific allocation method. The Oil Tax does not attribute income from the production of oil *in its entirety* to Alaska, the source state. Instead, it attempts to tax only that portion of income from the oil which is fairly related to Alaskan production activities. While total revenue for a barrel of oil during 1978-80 was approximately $26.64, only $6.77 was deemed production income attributable to Alaskan activities and subject to the Oil Tax. [16] In segregating from total income a portion related only to activities in the state, the Oil Tax operates as a separate accounting system.

16 The wellhead price did not include refining and marketing costs and profits. The following deductions were also taken from the wellhead price: royalties, native corporation revenue sharing, production, *ad valorem* and windfall profit taxes, direct operating expenses, exploration, acquisition, and development costs, uncapitalized interest and general overhead and administrative expenses inside and outside Alaska (including a reasonable profit). AS 43.21.020(c); *15 AAC 21.200* (Eff. 2/22/79). *See* graph *supra* note 6.

[**14] The companies argue that the Oil Tax is not true separate accounting because it fails to take into account the profit-producing nature of activities occurring outside [*424] Alaska. For example, the geological and geophysical analysis of the Prudhoe Bay area was conducted primarily outside Alaska. The companies argue that only the expenses associated with these outside activities are deductible in computing income subject to the Oil Tax. Thus, in their view, the Oil Tax taxes profits earned outside Alaska.

The state contends that oil companies can deduct profits attributable to general overhead or administrative activities outside of Alaska. Under Department of Revenue regulations, profits associated with such activities could be deducted if the taxpayer in fact considered them profit generally and reported them as such to the stockholders. *15 AAC 21.290(b)* (Eff. 2/22/79, am. 3/26/82). The oil companies claim that the Security Exchange Commission prohibits the allocation of profits in this manner, citing *15 U.S.C. § 78m(b)(2)(b)(ii) (1982).* This section provides that every issuer of a security subject to the provision must have an internal accounting system that permits [**15] preparation of financial statements "in conformity with generally accepted accounting principles or any other criteria applicable to such statements." The parties' experts disagree on the acceptability, under general accounting

principles, of allocating profits to general overhead and administrative activities. Even if we assume that the allocation of profits to these activities is not generally accepted, *15 U.S.C. § 78m(b)(2)(B)(ii)* allows the use of "other criteria" in financial statements. If, as the oil companies claim, profits exist that are actually attributable to general overhead and administrative activities outside of Alaska, the Securities Exchange Act does not prevent them from reporting such profits to their shareholders, and then deducting them from their Alaska income tax.

Although amended after the repeal of the Oil Tax in 1982, *15 AAC 21.290(b)* (Eff. 2/22/79, am. 3/26/82) operates retroactively. [17] The oil companies, therefore, may amend their tax reports and returns to deduct any outside-generated profits attributable to general overhead and administrative activities associated with Alaskan oil production not previously deducted in computing Alaskan taxable income. [**16]

17 The only logical interpretation of the 1982 amendment to *15 AAC 21.290(b)* is that it operates retroactively for the tax years 1978-81. It cannot be meaningfully applied prospectively because it was adopted *after* the Oil Tax was no longer in effect. We must assume that the process of amending *15 AAC 21.290(b)* was intended to be operative. We cannot imagine that the Department of Revenue ("Department") would engage in a futile act. *See* 2A C. Sands, Sutherland Statutory Construction § 45.12, at 54 (4th ed. 1984).

The retroactivity of the Department's regulations is governed by the Alaska Administrative Procedure Act, *AS 44.62.240*. Under this statute, an "interpretative regulation," such as *15 AAC 21.290(b)*, may be retroactive only if the agency "has adopted no earlier inconsistent regulation and has followed no earlier course of conduct inconsistent with the regulation." The Department's earlier omission of a deduction for outside-generated profits attributable to general overhead and administration associated with Alaskan oil production could be construed as inconsistent conduct with the 1982 amendment to *15 AAC 21.290(b)*. *AS 44.62.240*, however, is concerned with the issues of fairness and notice. *See, e.g.,* AS 43.21.050(d) (authorizing Department to fashion an equitable tax if relief from an unfair allocation is required). In this case, a retroactive interpretation of the 1982 amendment confers a benefit on the oil companies by allowing an additional tax deduction not previously available. Unlike many retroactive enactments, *15 AAC 21.290(b)*, as amended, does not create a harsh or unfair result for the affected parties. Therefore, the 1982 amendment to *15 AAC 21.290(b)* operates retroactively for the tax years 1978-81.

[**17] The companies also assert that the Oil Tax is an inappropriate methodology because it presumes that crude oil has a value, i.e., that income has been generated when the oil is merely brought out of the ground. The oil companies argue that oil has no value whatsoever until it is sold.

The oil companies cite our decision in *Sjong v. State, Department of Revenue, 622 P.2d 967 (Alaska 1981), appeal dismissed, 454 U.S. 1131, 71 L. Ed. 2d 284, 102 S. Ct. 986 (1982)*, for the proposition that the oil has no value until it is sold. We find their reliance misplaced. In *Sjong,* we upheld an apportioned net income tax assessed [*425] against a nonresident crab fisherman, who fished exclusively in the international waters surrounding Alaska and sold his catch only to Alaska processors and canneries. Sjong claimed that no taxable income could be attributed to the state because he caught the crabs in international waters. We responded that "the process of fishing results in no profits until the catch is sold to processors in Alaska." *622 P.2d at 972* (footnote omitted). Obviously, profits do not result from crab fishing or oil production until the product is sold. This does [**18] not negate the fact that profits generated by the sale are partly attributable to the inherent value of the crab or oil at its point of production.

In the state's view, the extraction of a natural resource, in and of itself, generates income. Thus, it argues that it is reasonable to attribute the income identified with the extraction of oil, measured in terms of "wellhead value," to the state in which the oil was extracted. The state is joined in this position by Amicus Curiae, the states of Louisiana, Mississippi and Oklahoma, all which have long employed separate accounting to tax oil production income. [18]

18 *See also Texas Co. v. Cooper, 236 La. 380, 107 So. 2d 676, 687-91 (La. 1958)* (rejected

argument that production of oil, in absence of sale, does not result in taxable income); *Magnolia Petroleum v. Oklahoma Tax Comm'n, 190 Okla. 172, 121 P.2d 1008, 1013 (Okla. 1941)* ("Oil produced in the state had an easily ascertainable market price that would represent the value of the product attributable wholly to Oklahoma.").

[**19] The United States Supreme Court has likewise recognized the inherent value generated by the extraction of natural resources. In upholding the constitutionality of Montana's severance tax on coal mined in the state, the Court reasoned that "the entire value of the coal, before transportation, originates in . . . . [Montana], and mining of the coal depletes the resource base and wealth of the State, thereby diminishing a future source of taxes and economic activity." *Commonwealth Edison v. Montana, 453 U.S. 609, 624, 69 L. Ed. 2d 884, 898, 101 S. Ct. 2946 (1981)* (footnote omitted). Before it is transported for sale, oil, like coal, has inherent value, to which profits and income can properly be attributed. [19]

19 While party to a tax suit in South Carolina, Exxon recognized the existence of oil's wellhead value. In its brief, Exxon asserted that "E&P [exploration and production] income is fully earned at the wellhead, and . . . . [is] functionally independent of . . . . refining and marketing operations." Appellant's Opening Brief at 19, *Exxon v. South Carolina Tax Comm'n, 273 S.C. 594, 258 S.E.2d 93 (S.C. 1979), appeal dismissed, 447 U.S. 917, 65 L. Ed. 2d 1109, 100 S. Ct. 3005 (1980)*. Exxon went on to note that their witness

> testified that the posted field price was also accepted by the accounting profession as a reliable, independent measure of the value of crude oil at the wellhead. Using this value, ... the net income earned by exploration and production could be and is accurately measured. This is in accordance with generally accepted accounting principles, because crude oil has a known, realizable value.

Id. at 26.

[**20] We hold that the Oil Tax is fundamentally a separate accounting method for dividing income, distinct from both the specific allocation by situs and formula apportionment methods.

C. *Separate Accounting More Accurately Attributes Income Generated from Alaskan Oil Than Does Formula Apportionment*

The use of separate accounting to apportion the income of a unitary business, such as each of the companies in this litigation, has been roundly criticized. [20] The United States Supreme Court has noted:

> The problem with this method is that formal accounting is subject to manipulation and imprecision, and often ignores or captures inadequately the many subtle and largely unquantifiable transfers of [*426] value that take place among the components of a single enterprise.

Container Corp. of America v. Franchise Tax Board, 463 U.S. 159, 164-65, 77 L. Ed. 2d 545, 553, 103 S. Ct. 2933 (1983) (citation omitted). For instance,

> while it [separate accounting] purports to isolate portions of income received in various States, [it] may fail to account for contributions to income resulting from functional integration, centralization of management, and economies [**21] of scale. Because these factors of profitability arise from the operation of the business as a whole, it becomes misleading to characterize the income of the business as having a single identifiable "source." Although separate geographical accounting may be useful for internal auditing, *for purposes of state taxation it is not constitutionally required.*

Mobil Oil v. Commissioner of Taxes, 445 U.S. 425, 438, 63 L. Ed. 2d 510, 521, 100 S. Ct. 1223 (1980) (emphasis added; citations omitted).

20 *See, e.g.,* G. Altman & F. Keesling, *supra* note 9, at 38 ("It is obvious, however, that a separate accounting, no matter how detailed, is basically false if the business done in more than one state is of a unitary character, ..."); Dexter,

The Unitary Concept in State Income Taxation of Multistate - Multinational Businesses, 10 Urb. Lawyer 181, 207 (1978) ("The use of separate accounting to attribute unitary income to a taxing jurisdiction is conceptually inconsistent.").

These criticisms, however, [**22] are inapplicable to the oil and gas industry. The standard three-factor formula apportionment method was "developed and designed to meet the needs of manufacturing and mercantile industries, and [is] poorly adapted to a good many other businesses." [21] The United States Supreme Court has noted that the three-factor formula is "necessarily imperfect":

> First, the one-third-each weight given to the three factors is essentially arbitrary. Second, *payroll, property, and sales still do not exhaust the entire set of factors arguably relevant to the production of income.*

Container Corp. of America v. Franchise Tax Board, 463 U.S. at 183 n.20, 77 L. Ed. 2d at 565 n.20 (emphasis added). An assumption made in the use of formula apportionment is that *"major* income-producing elements can be identified and that these major elements contribute the largest portion of the unitary income of the taxpayer." [22]

21 J. Hellerstein, *supra* note 7, para. 10.9, at 689.

22 A. Cohen, Apportionment and Allocation Formulae and Factors Used by States in Levying Taxes Based on or Measured by Net income of Manufacturing, Distributive and Extractive Corporations 14 (1954). [Record 1561]

[**23] A unique characteristic of unitary oil and gas businesses is that the major income-producing element is the value of the oil and gas reserves in the ground. While this element can be readily identified, it is not recognized under traditional formula apportionment methods. [23] Instead, the typical factors used are property, payroll and sales, none of which accurately reflects the oil and gas corporations' activities in Alaska. The property factor includes only the original cost of the wells and the lease, which do not necessarily represent the value of the oil reserves themselves. *See AS 43.19.010,* art. IV, § 11. As a result, the Prudhoe Bay field is valued at about one percent of its actual worth. [24] Under UDITPA, the payroll factor includes only wages paid to employees based in the state. *AS 43.19.010,* art. IV, §§ 13-14. Oil production, however, is not a labor-intensive industry. Moreover, much of the production work is done by employees based in other states, or by independent contractors, whose earnings do not appear in the payroll factor. Finally, and most importantly, the sales receipts under UDITPA are credited solely to the destination state. *AS 43.19.010,* art. [**24] IV, § 16. The oil companies and the state agree that only a "tiny fraction" of the oil produced in Alaska is actually sold within the state.

23 *Id.*

24 *See* B. Sorensen, Memorandum to the Honorable Nels A. Anderson, Jr. (May 27, 1976) (discussing state corporate income tax).

For all of the above reasons, separate accounting, not formula apportionment, is the prevailing method throughout the United States for reporting income from oil production. [25] The Comptroller General's [*427] report explains that states use separate accounting to determine the income division for unitary oil and gas businesses "because it conforms more to [the businesses'] financial accounting procedures and . . . . more accurately reflects income than formula apportionment." [26]

25 Rudolph, *State Taxation of Interstate Business: The Unitary Business Concept and Affiliated Groups,* 25 Tax L. Rev. 171, 191 (1970). Of the top five producing states, three - Alaska, Louisiana and Oklahoma - require the use of separate accounting to determine income attributable to oil production. Texas imposes no corporate income tax, and California requires formula apportionment. Statistical Abstract of the United States at 730 (1983). *But see Cal. Rev. & Tax Code Ann. § 25137* (West 1979) (allowing separate accounting, or other alternative methods of apportionment, when total formula apportionment does "not fairly represent the extent of the taxpayer's business activity in this state.").

[**25]

26 GAO Report to the Chairman, House Committee on Ways and Means: Key Issues Affecting State Taxation of Multijurisdictional Corporate Income Need Resolving 3 (1982).

[Record 17,023].

Alaska has not employed separate accounting to divide the income of all unitary businesses. According to the state, the Alaska legislature turned to separate accounting for oil producing businesses only after it determined that the use of formula apportionment to compute Alaska's share of oil production income would seriously underestimate the production income that was rightly subject to taxation by this state. [27]

> 27 The Oil Tax was enacted only after it was considered by two legislatures over a four year period. Sixty-three hearings were held and dozens of studies and reports were made.

The oil companies cite portions of legislative history to show that the Oil Tax was imposed in an effort to unilaterally effect a renegotiation [**26] of oil leases so as to shift the cost of Alaska's government to the oil industry. The legislature, however, formally declared that the income tax of corporations engaged in oil production or pipeline transportation would be computed under the Oil Tax because the formula apportionment method did not fairly represent the extent of those corporations' oil production and transportation activities in Alaska. Ch. 110, § 1, SLA 1978. To look beyond this articulated basis would lead to a "parade of legislators' affidavits containing their perceptions" of the Oil Tax's purpose. *Alaska Public Employees Association v. State, 525 P.2d 12, 16 (Alaska 1984)*. We have recently disapproved of such inquiries. *Id.* The United States Supreme Court has also declined to search for the "real" motive beyond the legislature's expressed purposes when adjudicating equal protection and commerce clause challenges. In *Minnesota v. Clover Leaf Creamery, 449 U.S. 456, 66 L. Ed. 2d 659, 101 S. Ct. 715 (1981)* the Court stated that it would

> assume that the objectives articulated by the legislature are actual purposes of the statute, unless an examination of the circumstances forces us to conclude [**27] that they "could not have been a goal of the legislation."

449 U.S. at 463 n.7, 66 L. Ed. 2d at 668 n.7 (quoting *Weinberger v. Wiesenfeld, 420 U.S. 636, 648 n.16, 43 L. Ed. 2d 514, 525 n.16, 95 S. Ct. 1225 (1975)*). Nothing in the record leads us to conclude that accurate and fair allocation could not have been the legislature's goal in enacting the Oil Tax. [28]

> 28 *See, e.g.,* Minutes of Senate Finance Committee (May 21, 1977): "The income tax is not designed to pick up additional money but to try to establish equal treatment between companies operating within the state." (Statement of Senator Chancy Croft) [Record 4759]; Minutes of Senate Resource Committee (February 22, 1978): "If we're seeking to raise money -- I think the most effective way is through a severance tax." (Statement of Commissioner Sterling Gallagher [Record 1704]); Office Memo to Senator Rader from Kay Brown (December 22, 1977): "Separate accounting [is the] most equitable method because under it every corp[oration] pays [the] same effective tax rate." (Statement of Senator Chancy Croft) [Record 1661]; Testimony Before House/Senate Resources Committees (January 25, 1978): "The purpose [of separate accounting] is not to get higher taxation, but it gives you a direct fix on what the profitability of the industry's operations are." (Statement of consultant Milton Lipton) [Record 1941]

[**28] The fact that the traditional formula apportionment method inaccurately reflects the oil companies' income and profits derived from Alaskan production activities is [*428] illustrated in the case of Sohio. The oil companies maintain that during 1978-80, when the Oil Tax was in effect, an average of only 10% of Sohio's payroll, 12% of its sales and 50% of its property were in Alaska. At the same time, Sohio indicated in its 1980 annual report that over 90% of its total oil production derived from the reserves in Alaska. [Record 1559] A media report offered by the state, with which the oil companies did not take issue, indicated that Alaskan oil had elevated Sohio from seventeenth to seventh in earnings in the oil industry:

> Once severely short of crude, Sohio's bonanza from its huge reserves of Alaskan oil skyrocketed 1979 profits to $1.2 billion, a phenomenal 2,200% blast in just one decade. [29]

Clearly the traditional formula apportionment method would inadequately reflect the phenomenal value of the

companies' oil reserves in Alaska.

29 *Investing a Mountain of Cash Before the Oil Runs Out: An Oil Giant's Dilemma,* Bus. Wk. 60 (August 25, 1980). [Record 684]

[**29] III. SUMMARY JUDGMENT WAS PROPER

The oil companies argue that there are numerous disputed issues of fact which preclude summary judgment for the state. Several of the alleged disputed issues of fact are irrelevant to the constitutional challenge and do not preclude summary judgment. [30] Other claims by the oil companies reduce to the assertion that the characterization of the Oil Tax as a separate accounting methodology is a disputed issue of fact. The state argues that the question as to whether the Oil Tax is a form of separate accounting is a question of law. We agree with the state that a trial is not required in this case. The characterization of the Oil Tax is at most a "legislative fact" which is not the type of factual issue for which trial is necessary. *See State v. Erickson, 574 P.2d 1, 4-6 (Alaska 1978).* As the trial court held, "the asserted issues of material fact do not preclude summary judgment in any event because they are facts only in the sense that they provide premises in the process of legal reasoning. They are not that type of fact for which a trial is mandated."

30 For example, whether the oil companies had, themselves, measured their income by methods similar to those used by the Oil Tax is irrelevant.

[**30] Finally, the oil companies claim that it is a disputed issue of fact whether the Oil Tax results in double taxation because it reaches income earned outside Alaska. An income attribution method, be it single-factor or three-factor formula apportionment or separate accounting, is not constitutionally invalid merely because it may result in taxation of some income that did not have its source in the state. *See Moorman Manufacturing v. Bair, 437 U.S. 267, 272, 57 L. Ed. 2d 197, 204, 98 S. Ct. 2340 (1978).* Even if facts demonstrate that the Oil Tax reaches income earned outside Alaska, as alleged by the oil companies, the statute will be stricken only upon "clear and cogent evidence" that the income Alaska attributes to itself is "out of all appropriate proportions to the business transacted in [the] State," or has "led to a grossly distorted result." *Container Corp. of America v. Franchise Tax Board, 463 U.S. at 170, 77 L. Ed. 2d at 556* (citations omitted). Nothing in the record demonstrates that the Oil Tax led to a "grossly distorted result" or that it is "out of all appropriate proportions" to the business of extracting billions of barrels of oil from reserves located [**31] within Alaska.

Disposition by summary judgment was appropriate in this case because no issue of material fact remained. The record provided the trial judge with a sufficient background to reach a decision. [31] *See Kelly v.* [*429] *Zamarello, 486 P.2d 906, 914 (Alaska 1971); cf. Ault v. Alaska State Mortgage Association, 387 P.2d 698, 701-02 (Alaska 1963).*

31 An extensive record was developed, which is divisible into three categories. First, the bulk of the record consists of the legislative history of the Oil Tax. Second, competing affidavits from various economists and accountants present divergent economic theories on how oil production income is generated, and how, as a matter of policy, it should be divided among the states for taxation purposes. Finally, a large number of affidavits submitted by the companies describe the various activities associated with oil production which occur outside Alaska.

IV. CONSTITUTIONAL CHALLENGES TO THE OIL TAX

A. *Background*

When state corporate income [**32] taxes were first adopted, [32] separate accounting was regarded as the most precise method for dividing the income of a multistate corporation for taxation purposes. [33] Although apportionment formulas were employed by states and their use approved by the United States Supreme Court, [34] separate accounting was initially viewed as a benchmark by which to judge the reasonableness of state apportionment formulas. Thus, in *Hans Rees' Sons, Inc. v. North Carolina, 283 U.S. 123, 128, 75 L. Ed. 879, 905, 51 S. Ct. 385 (1931),* the Supreme Court invalidated a state's apportionment formula under federal due process because the taxpayer showed that under separate accounting only 17% of the income was attributable to the state, whereas under the apportionment formula used, the state taxed from 66% to 85% of the corporation's income.

32 Wisconsin adopted the first corporate income tax in 1911. J. Hellerstein, *supra* note 7, para.

1.2, at 5.

33 *Id.* para. 8.3, at 324.

34 *Underwood Typewriter v. Chamberlain, 254 U.S. 113, 65 L. Ed. 165, 41 S. Ct. 45 (1920).*

[**33] The use of separate accounting as a basis for challenging state formula apportionment methods was eventually rejected in *Butler Brothers v. McColgan, 315 U.S. 501, 86 L. Ed. 991, 62 S. Ct. 701 (1942).* There, the Court acknowledged that an apportionment formula could be invalidated only if the taxpayer established by clear and cogent evidence that the formula taxed extraterritorial values. The Court held that the fact that no net income would be attributable to the state under separate accounting was insufficient to invalidate an apportionment formula.

> It is true that appellant's separate accounting system for its San Francisco branch attributed no net income to California. But . . . . [that] does not prove appellant's assertion that extraterritorial values are being taxed.

315 U.S. at 507, 86 L. Ed. at 996.

The Court developed the doctrine that if a multistate business is unitary, then the use of a formula apportionment method by the state is presumptively valid. [35] In the instant litigation, all of the companies involved are unitary businesses. Thus, it is undisputed that the use of an apportionment formula would have been a permissible means of attributing [**34] a portion of the companies' income to Alaska.

35 *See* J. Hellerstein, *supra* note 7, para. 8.7, at 338-343.

This case presents an interesting twist on previous constitutional challenges to state taxation methods by corporate taxpayers.

> In the past, apportionability often has been challenged by the contention that income earned in one State may not be taxed in another if the source of the income may be ascertained by separate geographical accounting.

Mobil Oil v. Commissioner of Taxes, 445 U.S. at 438, 63 L. Ed. 2d at 521. Conversely, in this litigation, the oil companies seek to defeat Alaska's separate accounting method by arguing that formula apportionment is *required* for unitary businesses. In recent years, the Court's endorsement of formula apportionment as the preferred method to divide income of a unitary business has become increasingly apparent. [36] However, we do not interpret [*430] this preference as being a constitutional ruling that formula apportionment *must* [**35] be employed in lieu of separate accounting.

36 *See, e.g., Exxon v. Wisconsin Dep't of Revenue, 447 U.S. 207, 229-30, 65 L. Ed. 2d 66, 85, 100 S. Ct. 2109 (1980); Mobil Oil v. Commissioner of Taxes, 445 U.S. 425, 446, 63 L. Ed. 2d 510, 526, 100 S. Ct. 1223 (1980).*

While separate accounting is not constitutionally required, [37] and while it may have some weaknesses when applied to some unitary businesses, [38] this methodology has not been rejected as unconstitutional. The United States Supreme Court in *Container Corp.* concluded that:

> Both geographical accounting and formula apportionment are imperfect proxies for an ideal which is not only difficult to achieve in practice, but difficult to describe in theory . . . .
>
> But we see no evidence demonstrating that the margin of error (systematic or not) inherent in the three-factor formula is greater than the margin of error (systematic or not) inherent in . . . . separate accounting . . . .

463 U.S. at 182, 183-84, 77 L. Ed. 2d at [**36] *564, 565.*

37 *See Mobil, 445 U.S. at 438, 63 L. Ed. 2d at 521; Exxon v. Wisconsin Dep't of Revenue, 447 U.S. at 223, 65 L. Ed. 2d at 81.*

38 *See Mobil, 445 U.S. at 438, 63 L. Ed. 2d at 521; Earth Resources v. State, Dep't of Revenue, 665 P.2d 960, 966 (Alaska 1983).*

B. *Due Process*

The oil companies claim that the Oil Tax is unconstitutional because it taxes extraterritorial values. They claim that the state impermissibly taxes all of their

production income from Alaska oil, despite the contributions that other states have made to those earnings in terms of research, management and sales.

"As a general principle, a state may not tax value earned outside its borders." *Earth Resources v. State, Department of Revenue, 665 P.2d 960, 966 (Alaska 1983)* (quoting *ASARCO v. Idaho State Tax Commission, 458 U.S. 307, 315, 73 L. Ed. 2d 787, 794, 102 S. Ct. 3103 (1982)*); *Container Corp. of America v. Franchise Tax Board, 463 U.S. at 164, 77 L. Ed. 2d at 552*. Any attempt to tax extraterritorial [**37] values would be an unconstitutional taking of property under the due process clause. [39]

39 The due process clause of the fourteenth amendment provides in part:

> Nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

U.S. Const. amend. XIV, § 1.

Due process imposes two requirements before a state may tax income generated in interstate commerce. First, a "minimal connection" must exist between the interstate activities and the taxing state. Second, the income attributed to the taxing state must bear a rational relationship to intrastate values of the enterprise. *Exxon v. Wisconsin Department of Revenue, 447 U.S. 207, 219-220, 65 L. Ed. 2d 66, 79, 100 S. Ct. 2109 (1980)*; *Mobil Oil v. Commissioner of Taxes, 445 U.S. at 436-37, 63 L. Ed. 2d at 520*; *Moorman Manufacturing v. Bair, 437 U.S. at 272-73, 57 L. Ed. 2d at 204*.

The first requirement - a minimal connection [**38] - is established if the corporation "avails itself of the 'substantial privilege of carrying on business' within the State." *Exxon v. Wisconsin Department of Revenue,* 447 U.S. at 220, 65 L. Ed. 2d 79 (quoting *Mobil, 445 U.S. at 437, 63 L. Ed. 2d at 520*, quoting *Wisconsin v. J.C. Penney Co., 311 U.S. 435, 444-45, 85 L. Ed. 267, 271, 61 S. Ct. 246 (1940)*). Clearly, a nexus exists between the oil production and transportation activities of ARCO, Exxon, and Sohio, and the State of Alaska.

As to the second requirement, the United States Supreme Court has not required absolute precision in determining a state's share of interstate income. In *Moorman Manufacturing v. Bair, 437 U.S. 267, 57 L. Ed. 2d 197, 98 S. Ct. 2340*, an animal feed company which manufactured its product in Illinois and sold it in Iowa challenged the constitutionality of Iowa's statutory [*431] apportionment formula. Instead of the typical three-factor (payroll, property and sales) formula, Iowa used a single-factor formula based exclusively on sales. The corporation argued that this formula resulted in extraterritorial taxation and violated the due process and *commerce clauses of the federal Constitution*. [**39] In addressing the rational relationship requirement, the Supreme Court stated:

> States have wide latitude in the selection of apportionment formulas and . . . . a formula-produced assessment will only be disturbed when the taxpayer has proved by "clear and cogent evidence" that the income attributed to the State is in fact "out of all appropriate proportion to the business transacted . . . . in that State," or has "led to a grossly distorted result."

437 U.S. at 274, 57 L. Ed. 2d at 205 (citations omitted). The Court found the taxpayer had failed to demonstrate any arbitrary result in its case, and thus the tax survived the due process challenge.

More recently the United States Supreme Court has expressly refused to constitutionally require a particular income attribution method to the exclusion of all others. In *Container Corp. of America v. Franchise Tax Board, 463 U.S. 159, 77 L. Ed. 2d 545, 103 S. Ct. 2933*, the Supreme Court upheld California's inclusion of the income of Container Corporation's foreign subsidiaries in the state's apportionment formula. The corporation argued that inclusion of this income violated both the due process and commerce clauses, [**40] because the same income California was subjecting to apportionment was taxed by foreign jurisdictions under a separate accounting methodology. In rejecting this argument, the Court noted:

> In the case of a more-or-less integrated business enterprise operating in more than one State, ... arriving at precise territorial allocations of "value" is often an

> elusive goal, both in theory and in practice. For this reason and others, *we have long held that the Constitution imposes no single formula on the States,* and that the taxpayer has the "distinct burden of showing by 'clear and cogent evidence' that [the state tax] results in extraterritorial values being taxed . . . ."
>
> *One way of deriving locally taxable income is on the basis of formal geographical or transactional accounting* [separate accounting].

463 U.S. at 164, 77 L. Ed. 2d at 552-53 (citations omitted, emphasis added).

We hold that the Oil Tax satisfies the second requirement of the due process clause. It makes a reasonable attempt to attribute only that income to Alaska that was generated in Alaska, while excluding expenses and profits generated beyond Alaska's borders. Under a separate accounting [**41] approach, income is viewed as earned when and where the principal operating activity occurs. Support activities are universally accounted for only as expenses, whether they occur in or outside the income-producing state. As with other states' separate accounting methods, the Oil Tax allows for the deduction of costs and profits from marketing, refining and transportation, and expenses related to other support activities. [40] Moreover, Alaska's tax is unique in allowing a deduction for out-of-state profits as well as costs of general overhead and administrative activities incident to Alaskan oil production and transportation, if the companies report them as such. *See 15 AAC 21.290(b)* (Eff. 2/22/79, am. 3/26/82). By allowing all of these deductions, the Oil Tax is intended to tax only those profits associated with the companies' activities within the state. Thus, the Oil Tax taxes only a portion of the companies' income, although by a technique quite different from formula apportionment. [41] Because the Oil Tax operates [*432] to tax only a portion of the companies' income, we hold that it satisfies the dual requirements of due process.

> 40 *See* La. Income Tax Reg. art. 47:244.A (1985); *Miss. Code Ann. § 27-7-23(b)(3)* (1983); *Okla. Stat. Ann. tit. 68, § 2358*, A.4.a, b, c (1985); *see also Webb Resources v. McCoy, 194 Kan. 758, 401 P.2d 879, 890 (Kan. 1965).*

[**42]

> 41 *See Container Corp., 463 U.S. at 188, 77 L. Ed. 2d at 568* (Formula apportionment and separate accounting are "two distinct methods of allocating the income of a multinational enterprise.").

C. *Commerce Clause*

We have previously recognized that the commerce clause [42] "places restraints upon the taxing power of states similar to those of the due process clause. In fact, these two constitutional limits overlap to a great extent." *Sjong v. State, Department of Revenue, 622 P.2d at 973.* Generally, if a state tax "is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce and is fairly related to the services provided by the State," there is no impermissible burden on interstate commerce. *Complete Auto Transit v. Brady, 430 U.S. 274, 279, 51 L. Ed. 2d 326, 331, 97 S. Ct. 1076 (1977).* The nexus and fair apportionment factors have been discussed in the previous due process section. We now turn to a consideration of the other two factors of the *Complete Auto Transit* test.

> 42 The commerce clause is set forth in article I, § 8 of the United States Constitution:
>
> > The Congress shall have Power To . . . . regulate Commerce with foreign Nations, and among the several States, and with the Indian tribes; . . . .

[**43] The oil companies contend that the Oil Tax violates the commerce clause because it inevitably results in overlapping or duplicative taxation, thus discriminating against businesses engaged in interstate commerce. They claim that recent United States Supreme Court decisions on the subject of multiple taxation render the Oil Tax unconstitutional, citing *Japan Line v. County of Los Angeles, 441 U.S. 434, 60 L. Ed. 2d 336, 99 S. Ct. 1813 (1979)*, *Mobil Oil v. Commissioner of Taxes, 445 U.S. 425, 63 L. Ed. 2d 510, 100 S. Ct. 1223*, and *Exxon v. Wisconsin Department of Revenue, 447 U.S. 207, 65 L. Ed. 2d 66, 100 S. Ct. 2109.* We disagree.

In *Japan Line,* six Japanese companies challenged a California property tax on shipping containers. The

Japanese-owned containers were subject to a property tax on 100% of their value in their home port of Japan. Under California's tax, all containers in the state on a specified tax day were subject to an apportioned *ad valorem* property tax. The companies contended that California's tax, as applied to their containers, created multiple taxation and violated the commerce clause.

The Court in *Japan Line* assumed that the *Complete* [**44] *Auto Transit* test was met. However, because taxation of instrumentalities of foreign commerce was at issue, the Court found it necessary to inquire whether California's tax, notwithstanding its fair apportionment, created a substantial risk of international multiple taxation. *441 U.S. at 451, 60 L. Ed. 2d at 349.* In this regard, the Court contrasted taxation of interstate instrumentalities with that of international instrumentalities:

> In order to prevent multiple taxation of interstate commerce, this Court has required that taxes be apportioned among taxing jurisdictions, so that no instrumentality of commerce is subjected to more than one tax on its full value. The corollary of the apportionment principle, of course, is that no jurisdiction may tax the instrumentality in full. "The rule which permits taxation by two or more states on an apportionment basis precludes taxation of all of the property by the state of the domicile . . . . Otherwise there would be multiple taxation of interstate operations." The basis for this Court's approval of apportioned property taxation, in other words, has been its ability to enforce full apportionment by all potential taxing bodies.

[**45] *441 U.S. at 446-47, 60 L. Ed. 2d at 347* (citations omitted). While the Court could require apportionment among the states for property taxation purposes, it obviously could not prevent Japan from taxing 100% of the value [*433] of the containers. The Court held California's nondiscriminatory tax unconstitutional because it resulted in actual multiple taxation of instrumentalities of international commerce. [43]

> 43 The Court indicated that it need not decide "under what circumstances the mere *risk* of multiple taxation would invalidate a state tax, or whether this risk would be evaluated differently in foreign, as opposed to interstate, commerce." *441 U.S. at 452 n.17, 60 L. Ed. 2d at 350 n.17* (emphasis in original).

The oil companies in the present litigation argue that if Alaska had been the home port instead of Japan in *Japan Line,* the Supreme Court would have invalidated Alaska's 100% *ad valorem* tax. We agree that Alaska would not be entitled to apply a property tax to the full value [**46] of instrumentalities of foreign commerce. But the oil companies' attempt to equate a property tax on the full value of goods used in foreign commerce with the Oil Tax is inappropriate. While the single situs property tax may be analogous to the specific allocation by situs method of income taxation, it is a totally different species from separate accounting. [44] The Oil Tax, as a separate accounting division-of-income method, does not automatically conflict with an apportionment method and result in double taxation. [45] Because separate accounting and formula apportionment can coexist without overlapping tax bases, *Japan Line* does not require invalidation of the Oil Tax. [46]

> 44 *See* discussion *supra* section II. A. 2.
>
> 45 *Container Corp., 463 U.S. at 194-95, 77 L. Ed. 2d at 572.*
>
> 46 There is language in *Japan Line* to the effect that an "unapportioned" tax will not be sustained. *441 U.S. at 447, 60 L. Ed. 2d at 347.* However, this statement must be read in context. In the property tax area, separate accounting is not even a viable theory for dividing income. Allocation of the full property to one state or apportionment among several states are the only two options. Since allocation of the full property value to one of several proper taxing jurisdictions is unconstitutional, apportionment is the only permissible means of dividing the value of property used in interstate commerce for property taxation purposes.

[**47] In *Mobil Oil v. Commissioner of Taxes, 445 U.S. 425, 63 L. Ed. 2d 510, 100 S. Ct. 1223*, the Court upheld the constitutionality of the inclusion of foreign

source dividend income in the total income subject to taxation by Vermont. Mobil argued that Vermont could not tax its dividend income because New York, the state of commercial domicile, had the power under the commerce clause to allocate all of the dividend income to itself. Allowing Vermont to tax a share of the income by apportionment would, therefore, result in double taxation if New York implemented such a tax. In this situation, the Court considered the risk of multiple taxation to be sufficient since the specific allocation by situs method was "theoretically incommensurate" with apportionment. 47 The Court found that if one method were constitutionally preferable, a tax based on the other method could not be sustained. *445 U.S. at 444-45, 63 L. Ed. 2d at 525.*

> 47 *Cf. Moorman, 437 U.S. at 277, 57 L. Ed. 2d at 207.*

Instead of accepting Mobil's [**48] argument that specific allocation by situs was preferable, the Court found apportionment to be the better approach. While the Court chose not to rule on the constitutionality of a hypothetical New York tax, the Court stated that in theory New York could not exclusively tax Mobil's dividend income since

> the dividends reflect income from a unitary business, part of which is conducted in other states. In that situation, the income bears relation to benefits and privileges conferred by several states. These are the circumstances in which apportionment is *ordinarily* the accepted method.

Id. at 446, 63 L. Ed. 2d at 526 (emphasis added).

Several months after the *Mobil* case, the Court decided *Exxon v. Wisconsin Department of Revenue, 447 U.S. 207, 65 L. Ed. 2d 66, 100 S. Ct. 2109. Exxon,* like this litigation, involved state taxation of oil production [*434] income. Exxon's activities in Wisconsin were limited to the marketing of petroleum products. Exxon challenged Wisconsin's inclusion of oil production income in the income subject to apportionment by Wisconsin. Exxon argued that production of oil and marketing of oil were two distinct operations. [**49] In Exxon's view, since it could illustrate by separate accounting that these two activities were distinct, Wisconsin could not constitutionally include production income in the tax base for apportionment.

Exxon contended that the commerce clause required the allocation of all income derived from exploration and production functions to the situs state, rather than inclusion in the apportionment formula. Exxon asserted that since the producing state was constitutionally entitled to allocate all production income to itself, non-producing states could not tax an apportioned share of this same income.

To this, the Supreme Court replied:

> We do not agree. As was the case with income from intangibles, there is nothing "talismanic" about the concept of situs for income from exploration and production of crude oil and gas. Presumably, the States in which appellant's crude oil and gas production is located are permitted to tax in some manner the income derived from that production, there being an obvious nexus between the taxpayer and those States. However, "there is no reason in theory why that power should be exclusive when the [exploration and production income as distinguished [**50] through separate functional accounting] reflect[s] income from a unitary business, part of which is conducted in other States. In that situation, the income bears relation to benefits and privileges conferred by several States. These are the circumstances in which apportionment is ordinarily the accepted method."
>
> In short, the Commerce Clausedoes not require that any income which a taxpayer is able to separate through accounting methods and attribute to exploration and production of crude oil and gas be allocated to the States in which those production centers are located. *The geographic location of such raw materials does not alter the fact that such income is part of the unitary business of the interstate enterprise and is subject to fair apportionment among all States to which there is a sufficient nexus with the*

interstate activities of the business.

447 U.S. at 229-30, 65 L. Ed. 2d at 85 (emphasis added; citations omitted).

Basically, both the oil companies and the state view *Japan Line, Mobil* and *Exxon* as prohibiting allocation of oil production income entirely to the situs state. The debate focuses on whether the Oil Tax allocates all oil production [**51] income to Alaska, as the oil companies contend, or is instead a distinct method of dividing the production income, as the state contends. Because we hold that the Oil Tax is a distinct method of dividing oil production income by use of separate accounting, its constitutional validity is not directly determined by these three cases. [48]

48 *See* W. Hellerstein, Memorandum to Mr. Milton Barker (April 20, 1981) (discussing proposed Oil Tax). [Record 17,091]

While *Mobil* and *Exxon* indicate the Court's strong endorsement of the use of apportionment formulas, the Court clearly implied that the use of separate accounting is constitutionally permissible under the commerce clause. [49] The constitutional preference for apportionment of "unitary" dividend income in *Mobil* stemmed from the fact that the two competing methods at issue -- specific allocation and formula apportionment -- were "theoretically incommensurate." [*435] *Mobil, 445 U.S. at 444, 63 L. Ed. 2d at 525.* [50]

49 In both *Exxon* and *Mobil,* the Court stated that separate accounting "is not constitutionally required." *Exxon, 447 U.S. at 223, 65 L. Ed. 2d at 81*; *Mobil, 445 U.S. at 438, 63 L. Ed. 2d at 521.*
[**52]

50 *See* W. Hellerstein, *supra* note 48, at 2. [Record 17,093]

The type of duplicative taxation found unacceptable in *Japan Line, Exxon* and *Mobil* all involved one taxing jurisdiction using the specific allocation by situs method, while another used apportionment. In other words, one taxing jurisdiction taxed the whole pie, while another taxed a slice. In such a situation, double taxation is inevitable, and one method has to be chosen over another. By contrast, in *Moorman Manufacturing v. Bair, 437 U.S. 267, 57 L. Ed. 2d 197, 98 S. Ct. 2340*, two jurisdictions used different apportionment formulas. Each took only a slice of the pie, but since they used different formulas to divide the pie, the Court recognized that there was high probability of some overlap. While the potential for overlap existed, it certainly was not inevitable, and the Court upheld Iowa's apportionment method. The Court held that prevention of duplicative taxation should be effected by a national uniform rule for the division of income, but that the "Constitution . . . . is neutral with respect to [**53] the content of any uniform rule." *Id. at 279, 57 L. Ed. 2d at 208.* Given the absence of federal legislation, the Court was unwilling to specify that a particular methodology was constitutionally preferable. While acknowledging a clear risk of multiple taxation in a variety of situations due to the divergence in division-of-income techniques employed by the various states, the Court found such risk preferable to choosing one technique as constitutionally superior to another. *Id. at 278-80, 57 L. Ed. 2d at 207-09.*

The oil companies in the present litigation acknowledge that *Moorman* evidenced the Supreme Court's high degree of tolerance for apportionment formulas. But in their view, this tolerance does not extend beyond the apportionment method. They claim that *Moorman* does not sanction the use of Alaska's Oil Tax because the tax is not apportioned. We disagree. First, as we have previously explained, the Oil Tax utilizes a division-of-income method. Second, while *Moorman* pertained to the conflict presented when two jurisdictions employ different types of formula apportionment, the principle of the opinion was that non-uniform state taxes are inevitable and [**54] constitutionally permissible. Since *Moorman,* the Court has continued to maintain that states enjoy broad leeway in their choice of division-of-income methods. *See Container Corp. of America v. Franchise Tax Board, 463 U.S. at 164, 77 L. Ed. 2d at 552.*

Container Corp. closely resembles the situation in this case. In *Container Corp.,* California sought to determine its share of total income by use of formulary apportionment, while foreign jurisdictions employed separate accounting. [51] Discussing discrimination against interstate commerce, the Court reiterated its view that the Constitution does not require the elimination of all overlapping taxation on the interstate level. *463 U.S. at 171, 77 L. Ed. 2d at 557.* Thus, if the problem were limited to the interstate level, "the fact that different jurisdictions applied different methods of taxation . . . . would probably make little constitutional difference." *463 U.S. at 185, 77 L. Ed. 2d at 566.*

51 *See* discussion *supra* section IV. B.

[**55] In *Container Corp.,* the Court faced the additional complication of international commerce. Even so, the Court upheld the tax, distinguishing *Japan Line* on the ground that Japan's specific allocation by situs method necessarily resulted in double taxation.

> Here, by contrast, we are faced with two distinct methods of allocating the income of a multi-national enterprise. The "arm's-length" approach [i.e., separate accounting] divides the pie on the basis of formal accounting principles. The formula apportionment method divides the same pie on the basis of a mathematical generalization. Whether the combination of the two methods results in the [*436] same income being taxed twice or in some portion of income not being taxed at all is dependent solely on the facts of the individual case.

463 U.S. at 188, 77 L. Ed. 2d at 568 (footnote omitted). The Court held that the two taxing methods do "not create an *automatic* 'asymmetry'." *Id. at 194-95, 77 L. Ed. 2d at 572.* "It would be perverse, [therefore,] simply for the sake of avoiding double taxation, to require California to give up one allocation method that sometimes results in double taxation [**56] in favor of another allocation method that also sometimes results in double taxation." *Id. at 193, 77 L. Ed. 2d at 571.* The fact that the Court found the two methods could coexist on the international level, where duplicative taxation is viewed more strictly, makes separate accounting a quite permissible alternative when only interstate commerce is involved, as is the case in the present litigation.

The Supreme Court has repeatedly recognized that neither separate accounting nor formula apportionment will result in the attribution of the exact amount of income earned in the state to that particular state. Some multiple taxation may result when one jurisdiction employs one method and another uses a different approach. This threat is inherent in any system where state attribution methods are nonuniform. But a state does not offend the commerce clause merely because its method of dividing income is different from that of its neighbors. *Moorman Manufacturing v. Bair, 437 U.S. at 278-80, 57 L. Ed. 2d at 208-09.*

We have already explained that the separate accounting method employed by the State of Alaska does not tax all profits generated from Alaskan oil production and does [**57] not impermissibly attribute extraterritorial values to Alaska. Using the leeway it retains absent a federal uniform approach, the Alaska legislature chose a constitutionally permissible method of income division, albeit not the one "ordinarily" employed for most other types of unitary businesses.

We hold that the Oil Tax comports with the requirements of the *Complete Auto Transit* test and creates no impermissible burden on interstate commerce. The location of the oil fields in Prudhoe Bay creates a substantial "nexus" between the oil companies' activities and the State of Alaska. [52] As discussed above, the Oil Tax is fairly apportioned to represent only that part of the companies' income generated from its Alaskan activities -- oil and gas production and transportation. As in *Container Corp.,* the Oil Tax does not inevitably result in multiple taxation. Moreover, any possible overlap created by Alaska's use of separate accounting and other jurisdictions' use of different income division methods is not the fault, in the constitutional sense, of Alaska. Thus, the Oil Tax does not discriminate against interstate commerce. Finally, because the oil companies all benefit from [**58] the "substantial privilege" [53] of extracting oil in Alaska, the Oil Tax is fairly related to services provided in the state.

52 *See Exxon v. Wisconsin Dep't of Revenue, 447 U.S. at 229, 65 L. Ed. 2d at 85.*

53 *See Commonwealth Edison v. Montana, 453 U.S. at 628-29, 69 L. Ed. 2d at 901.*

D. *Federal and State Equal Protection*

The oil companies assert that the Oil Tax violates both state and federal equal protection since it "arbitrarily [and] irrationally subject[s] a special group of taxpayers to treatment not accorded taxpayers at large." They argue, in effect, that using a distinct method of taxation for multistate oil companies, but not for any other unitary businesses, violates equal protection. We reject the oil companies' equal protection challenge.

The analysis under Alaska's equal protection clause involves a three-step process. *Alaska Pacific Assurance v. Brown, 687 P.2d 264, 269-70 (Alaska 1984)* [hereinafter [*437] cited as ALPAC]; *State v. Ostrosky, 667 P.2d* [**59] *1184, 1192-94 (Alaska 1983), appeal*

dismissed, 467 U.S. 1201, 81 L. Ed. 2d 339, 104 S. Ct. 2379 (1984); *State v. Erickson, 574 P.2d 1, 11-12 (Alaska 1978)*. [54] First, in order to ascertain the appropriate level of review, the nature of the constitutional interest affected must be identified. *ALPAC,* 687 P.2d at 269. Next, the validity of the statutes' purpose must be analyzed in light of the interest impinged. *Id.* Lastly, the means chosen must be examined, also in light of the interest, to insure that they are sufficiently related to the goals of the statute. *Id. at 269-70.*

> 54 In determining questions of equal protection under the Alaska Constitution, we employ a single test. As we stated in *State v. Erickson, 574 P.2d 1, 12 (Alaska 1978)*:
>
> > Such a test will be flexible and dependent upon the importance of the rights involved. Based on the nature of the right, a greater or lesser burden will be placed on the state to show that the classification has a fair and substantial relation to a legitimate governmental objective.

[**60] The interest involved here, freedom from disparate taxation, lies at the low end of the continuum of interests protected by the equal protection clause. [55] Regarding the statute's purpose, the oil companies claim that greed and other improper motives led the Alaska legislature to enact the Oil Tax. The state, however, has adequately established that a primary purpose of the Oil Tax was to rectify a perceived underestimation of oil production and pipeline transportation income that occurred with the application of an apportionment formula. The goal was to insure that the tax rate assessed to the oil companies on this income was commensurate with the rate applicable to the income of other corporations in the state. Ch. 110, § 1, SLA 1978. Taxing the oil companies differently to rectify a perceived inequity was the legislature's attempt to prevent disparate treatment; thus, the validity of this purpose in light of the companies' interest is established. Finally, the means chosen were sufficiently related to the goals of the legislation. The use of separate accounting, rather than formula apportionment, increased the amount of production and transportation income subject to Alaska [**61] taxation and more fairly represented the extent of the business activities of the oil companies in Alaska.

> 55 *See Regan v. Taxation with Representation of Washington, 461 U.S. 540, 547, 76 L. Ed. 2d 129, 138, 103 S. Ct. 1997 (1983). See generally* P. Hartman, *supra* note 8, § 3.1, at 131-38.

The Oil Tax did not adversely affect any fundamental interest, nor did it contain a suspect classification. Thus, to be upheld under the federal analysis, it need only to have been rationally related to a legitimate state interest. *Exxon v. Eagerton, 462 U.S. 176, 195-96, 76 L. Ed. 2d 497, 513, 103 S. Ct. 2296 (1983)*. The rational basis standard is particularly easy to meet in the area of taxation. The United States Supreme Court has stated that "legislatures have especially broad latitude in creating classifications and distinctions in tax statutes." *Regan v. Taxation with Representation of Washington, 461 U.S. 540, 547, 76 L. Ed. 2d 129, 138, 103 S. Ct. 1997 (1983)*. The Oil Tax clearly bore a rational [**62] relationship to the state's goal of correcting a perceived inequity in the tax structure.

While the oil companies dispute the underlying premise that the Oil Tax rectifies inequities, the legislature could have reasonably concluded that the Oil Tax would more accurately compute the companies' income generated in Alaska. Thus, the Oil Tax survives the equal protection challenge, under both the United States and the Alaska Constitutions.

E. *Contract Clause*

The oil companies argue that the Oil Tax is invalid because it impairs the obligation of the state's lease contracts with them. [56] They contend that the tax increases the state's share under the lease [*438] contracts, and that such modification of the terms of the leases violates the contract clause of the United States Constitution. [57]

> 56 The State of Alaska began issuing oil and gas leases a few months after passage of the Alaska Land Act, 38.05, in 1959. The first oil and gas leases at Prudhod Bay were issued in 1964 the state entered into lease contracts with the oil companies, whereby the state sold the companies whatever gas and oil might be found on the leaseholds in exchange for "bonus" payments and royalties of 12 1/2%.

[**63]

57 "No State shall . . . . pass any . . . . Law impairing the Obligation of Contracts . . . ." *U.S. Const., art. I, § 10, cl. 1.*

This argument is without merit. No lease provision has been impaired. In entering into the leases the state could not, [58] and did not, contract away its power as a sovereign to tax income earned in the state. *Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 71 L. Ed. 2d 21, 102 S. Ct. 894 (1982)* disposes of this issue:

> Contractual arrangements remain subject to subsequent legislation by the presiding sovereign. Even where the contract at issue requires payment of a royalty for a license or franchise issued by the governmental entity, the government's power to tax remains unless it "has been specifically surrendered in terms which admit of no other reasonable interpretation." *St. Louis v. United R. Co., 210 U.S. 266, 280, 52 L. Ed. 1054, 28 S. Ct. 630 (1908).*

455 U.S. at 148, 71 L. Ed. 2d at 36 (citations omitted); *see also Exxon v. Eagerton, 462 U.S. at 187-94, 76 L. Ed. 2d at 508-12.*

58 The Alaska Constitution provides: "The power of taxation . . . . shall not be . . . . contracted away, except as provided in this article." *Alaska Const. art. IX, § 1.*

[**64] VIII. RETROACTIVITY OF THE OIL TAX

The Oil Tax Act was signed into law on July 8, 1978. [59] Section 4 of the Act provided that it would apply retroactively to January 1, 1978. Section 5 provided the Act would be "effective" immediately. While the Senate voted 16 to 4 to approve section 5, the entire Oil Tax Act only passed by a vote of 11 to 9. Thus, at no time did more than 11 senators vote to approve section 4.

59 Ch. 110, SLA 1978.

The companies argue that the Act may not constitutionally be made applicable to income earned prior to July 8, 1978. They interpret *article II, § 18 of the Alaska Constitution* [60] and *AS 01.10.070(a)* [61] as requiring the approval of two-thirds majority of each house of the legislature to give retroactive effect to a new law. The companies argue that even though a two-thirds vote was attained for an immediate effective date, a two-thirds vote was also required to enact section 4, applying the Act retroactively to January 1, 1978. We disagree.

60 *Alaska Const. art. II, § 18* provides:

> Laws passed by the legislature become effective ninety days after enactment. The legislature may, by concurrence of two-thirds of the membership of each house, provide for another effective date.

[**65]

61 *AS 01.10.070(a)* contains language paralleling *Alaska Const. art. II, § 18.*

AS 01.10.090 states that "no statute is retrospective unless expressly declared therein." A two-thirds vote requirement does not appear in that section, nor elsewhere in Alaska law. The legislature, however, has recognized that where retroactive application of a portion or all of a bill is desired, an immediate effective date, which does require a two-thirds vote under article II, § 18 and *AS 01.10.070(a)*, should be used in conjunction with the retroactivity section. Legislative Affairs Agency, *Manual of Legislative Drafting* 11 (1977); Uniform Rules of the Alaska State Legislature, Rule 10 (May 3, 1977). Accordingly, because two-thirds of the legislature voted to make the Oil Tax Act immediately effective, a separate two-thirds vote for the Act to be retroactive was not constitutionally required. The Oil Tax was properly retroactive to January 1, 1978.

The superior court's action in granting the state's motion for summary judgment is AFFIRMED.

APPENDIX 1

AS 43.21, Oil and Gas Corporate Income Tax provided:

[**66] Sec. 43.21.010. Application [Repealed effective January 1, 1982]. AS 43.21.010 - [*439] 43.21.120 applies to every corporation doing business in the state which derives income from the production of oil or gas from a lease or property in the state or from the

pipeline transportation of oil or gas in the state. The tax calculated under AS 43.21.010 - 43.21.120 is measured by the total taxable income of the corporation during the tax period as determined under AS 43.21.020 -- 43.21.040 and is calculated at the rates established under *AS 43.20.011(e)*.

Sec. 43.21.020. Determination of taxable income from oil and gas production [Repealed effective January 1, 1982]. (a) The taxable income of a corporation from the production of oil and gas from a lease or property in the state shall be the corporation's net income as calculated by the department in accordance with this section.

(b) Gross income of a corporation from oil and gas production shall be the gross value at the point of production of oil or gas produced from a lease or property in the state. The department shall by regulation determine a uniform method of establishing the gross value at the point of production. [**67] In making its determination the department may use the actual prices or values received for the oil or gas, the posted prices for the oil or gas in the same field, or the prevailing prices or values of oil or gas in the same field. In addition, in its determination of gross value at the point of production of oil or gas produced from a lease or property, the department shall determine the reasonable costs of transportation from the point of sale to the point of production of the oil or gas. Transportation costs set by a tariff properly on file with the Alaska Pipeline Commission or other regulatory agency shall be considered prima facie reasonable, but if a tariff properly on file with a regulatory agency is subsequently amended, changed, or overturned retroactively, the reasonable costs of transportation shall be recomputed for that period using the newly determined tariff.

(c) Net income from oil and gas production shall be determined by the department by deducting from gross income the following:

(1) royalties paid in kind or in value;

(2) taxes imposed under *AS 43.55.011 - 43.55.150* and AS 43.57.010 which are actually paid or incurred by the corporation on the production [**68] from a lease or property in the state;

(3) taxes imposed under *AS 43.56.010 - 43.56.210* and AS 29.53.010 - 29.53.460 which are actually paid or incurred by the corporation on property used directly in the production of oil or gas from a lease or property in the state, including property used in production, gathering, treatment, or preparation of the oil or gas for pipeline transportation, but only if those property tax payments were due and payable only after the date of commercial production from the lease or property with which the property was associated;

(4) the direct costs incurred by or for the corporation in operating the lease or property, including the direct costs of producing, gathering, treating, or preparing the oil or gas for pipeline transportation, but not of any payments received for those activities and not including any indirect cost or overhead expense;

(5) depreciation (using the unit of production method or such other reasonable methods as the department may by regulation establish) on property used directly in the production, gathering, treatment, or preparation of the oil or gas for pipeline transportation including amortization of capitalized interest for [**69] investments in this property at a rate not to exceed the average cost of borrowed capital to the taxpayer during the year in which it is capitalized;

(6) the amortization of lease acquisition payments and taxes paid or incurred under *AS 43.56.010 - 43.56.210* and AS 29.53.010 - 29.53.460 (including capitalized interest on both) for or on producing properties before the commencement of commercial production from the lease or property for which the property is being used;

[*440] (7) interest expense of the corporation not capitalized during construction, that was paid or incurred in connection with property in Alaska; however, unless (f) of this section applies,

the interest expense may not exceed that portion of the total interest paid by the consolidated business of which the corporation is a part, determined by multiplying the total interest by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business; in this subsection, "total interest [**70] paid by the consolidated business" does not include interest expense arising from intercompany obligations within the consolidated business except to the extent that the interest expense reflects a pass-through of interest on a third-party borrowing by the parent or other member of the consolidated business with the purpose, expressed at the time of the third-party borrowing, of financing Alaska business activity of the taxpayer corporation;

(8) expenses incurred by the corporation after December 31, 1977, of unsuccessful exploration of oil or gas in the state including the acquisition costs of abandoned properties, dry hole costs, and the costs of geologic and geophysical exploration related to those abandoned properties;

(9) general overhead or administrative expense incurred by the corporation attributable to deriving income from the production of oil or gas from a lease or property in the state to the extent, except as provided in (f) of this section, that it does not exceed that portion of the total general overhead or administrative expense incurred by the consolidated business of which the corporation is a part, determined by multiplying the total general overhead or administrative [**71] expense by a fraction, the numerator of which is the value of the corporation's real and tangible personal property used directly in the production of oil or gas from a lease or property in the state and the denominator of which is the value of all real and tangible personal property of the consolidated business;

(10) the amount of income from the production of oil and gas from a lease or property that is divided among the regional Native corporations under sec. 7(i) of the Alaska Native Claims Settlement Act. (P.L. 92-203);

(11) the tax imposed by *sec. 4986 of the Internal Revenue Code* that is paid or incurred by the taxpayer for oil production from leases or properties in the state.

(d) Deductions from gross income under this section shall not include expenses previously deducted on a return filed under *AS 43.20.011 - 43.20.350.*

(e) Where a corporation subject to AS 43.21.010 - 43.21.120 shares the production or proceeds of the production from a lease or property through a working interest, royalty interest, overriding royalty interest, production payment, net profit interest, joint venture or other agreement, the department shall allocate the deductions from gross income [**72] between the corporation and the persons with whom it has such an agreement in accordance with the terms of the agreement.

(f) If a corporation demonstrates to the satisfaction of the department that it paid or incurred actual expenses for interest or for general overhead or administration attributable to deriving income from the production of oil or gas from a lease or property in the state in an amount greater than the amount determined under (c)(7) or (c)(9) of this section, the department may allow the corporation to deduct the greater amount.

Sec. 43.21.030. Determination of income from oil and gas pipeline transportation [Repealed effective January 1, 1982]. (a) Except as provided in (c) of this section, taxable income attributable to the transportation of oil in a pipeline engaged in interstate commerce in Alaska shall be determined [*441] by the department and shall be the amount reported or that would be required to be reported to the Federal Energy Regulatory Commission or its successors as net operating income,

less those portions of interest and general administrative expense attributable to the pipeline transportation of oil in the state, except that taxable [**73] income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general administrative expense attributable to pipeline transportation of oil in the state.

(b) Except as provided in (c) of this section, taxable income attributable to the transportation of natural gas in a pipeline engaged in interstate commerce in Alaska shall be determined by the department and shall be the amount reported or that would be required to be reported to the Federal Energy Regulatory Commission as net operating income less that portion of interest and general administrative expense attributable to pipeline transportation in the state, except that the taxable income shall also include taxes on or measured by income. The department shall establish regulations governing the determination of interest and general administrative expense attributable to pipeline transportation of natural gas in the state.

(c) Taxable income attributable to the transportation of oil or natural gas in Alaska of any corporation not under the Federal Energy Regulatory Commission jurisdiction, or of a corporation under the jurisdiction of the Federal [**74] Energy Regulatory Commission but not reporting the operation of pipelines in Alaska separately from the operation of pipelines elsewhere, shall be determined by the department and shall be based upon an amount equal to that which would have been reported to the Federal Energy Regulatory Commission under (a) of this section in the case of oil pipelines, or (b) of this section in the case of natural gas pipelines, had the corporation been, in fact, under Federal Energy Regulatory Commission jurisdiction for the taxable year and required to report on the operation of Alaska pipelines separately from the operation of pipelines elsewhere.

Sec. 43.21.040. Determination of income from activities other than oil and gas production or pipeline transportation [Repealed effective January 1, 1982]. (a) Taxable income of a corporation subject to AS 43.21.010 - 43.21.120 from activities in this state other than the production of oil or gas from a lease or property in the state or the pipeline transportation of oil or gas in the state shall be determined in accordance with the method established in art. IV of *AS 43.19.010* and in *AS 43.20.071*, as modified by (b) - (f) of this section.

(b) The [**75] total taxable income of the consolidated business is its entire income less the portion of that entire income attributable to worldwide production and pipeline transportation of oil and gas. In this section,

> (1) for a member of a consolidated business who is required to file under the Internal Revenue Code, "entire income" means taxable income under Subtitle F and chapter 1 of Subtitle A of the Internal Revenue Code of 1954, as amended, except that those provisions adopted after December 31, 1975, which change or modify exemptions from tax are not adopted by reference as a part of this section until the second January 1 following the effective date of the federal law;
>
> (2) for a member of a consolidated business who is not required to file under the Internal Revenue Code, "entire income" means book income, except that a taxpayer may elect to report his income as the income would be determined under (1) of this subsection.

(c) The numerator and denominator of the property factor, of the payroll factor and of the sales factor shall be calculated without reference to that portion of property, payroll or sales directly related to the production of oil or gas from a lease of property [**76] in the state or the pipeline transportation of oil or gas in the state.

(d) Repealed by § 17 ch. 116, SLA 1981.

(e) Repealed by § 17 ch. 116, SLA 1981.

[*442] (f) The value attributed to vessels transporting Alaskan oil or gas of the consolidated business which are not owned or effectively owned by the consolidated business shall be excluded from the property factor.

Sec. 43.21.050. Assessment of income and tax [Repealed effective January 1, 1982]. (a) The department shall assess taxable income and the amount of tax

payable on that taxable income.

(b) On or before August 15 of each year the department shall send to every corporation taxable under AS 43.21.010 - 43.21.120 a notice of assessment showing the amount of income taxable under AS 43.21.010 - 43.21.120 for the previous year and the amount of tax payable on that taxable income.

(c) For purposes of AS 43.21.010 - 43.21.120 the department may combine taxable incomes of corporations subject to tax under AS 43.21.010 - 43.21.120 who are part of the same consolidated business.

(d) If the methods of allocation and apportionment provided in AS 43.21.010 - 43.21.120 do not fairly represent the extent of a corporation's [**77] business activity in the state, the corporation may petition for or the department may require, in respect to all or any part of the corporation's business activity, if reasonable, the employment of any method authorized under art. IV, sec. 18, of the Multistate Tax Compact (*AS 43.19.010*) to effectuate an equitable allocation and apportionment of the corporation's income. The commissioner shall include in his annual report required in AS 43.21.110 a report on all relief granted under this subsection, including for each case a statement of the changes in tax liability resulting from the granting of relief, the tax years involved, and a description of the method of determining taxable income that was substituted for those provided in AS 43.21.010 - 43.21.120.

Sec. 43.21.060. Returns [Repealed effective January 1, 1982]. On or before April 15 of each year, a corporation subject to tax under AS 43.21.010 - 43.21.120 shall submit a return in a form prescribed by the department setting out information required by the department to determine taxable income. For purposes of AS 43.21.010 - 43.21.120, the department may require corporations subject to tax under AS 43.21.010 - 43.21.120 [**78] who are part of the same consolidated business to file a single return.

Sec. 43.21.070. Payment of tax [Repealed effective January 1, 1982]. The tax levied under AS 43.21.010 - 43.21.120 is payable to the department on or before September 30 of each year or in installments, including prepayments of estimated tax, at the times and under the conditions the department may by regulation require. This tax is payable on the due date set out in this section even though the assessment is under appeal or the validity, enforceability or application of AS 43.21.010 - 43.21.120 or any provision of AS 43.21.010 - 43.21.120 is challenged before the department or in the courts.

Sec. 43.21.080. Transitional rules [Repealed effective January 1, 1982]. The department shall provide by regulation transition rules for corporations subject to tax under *AS 43.20.011 - 43.20.350* before July 9, 1978 to avoid double taxation of the same income or double deduction of the same expense of those corporations as a result of becoming subject to tax under AS 43.21.010 - 43.21.120.

Sec. 43.21.090. Regulations [Repealed effective January 1, 1982]. The department may adopt regulations in accordance with [**79] the Administrative Procedure Act (*AS 44.62.010 - 44.62.650*) as appropriate to administer and enforce AS 43.21.010 - 43.21.120.

Sec. 43.21.100. Penalties [Repealed effective January 1, 1982]. The penalties established in *AS 43.20.011 - 43.20.350* apply to AS 43.21.010 - 43.21.120.

Sec. 43.21.110. Public reporting [Repealed effective January 1, 1982]. (a) The commissioner of revenue shall compile and transmit to the legislature an annual consolidated report of state revenues and taxation policies under AS 43.21.010 - 43.21.120. [*443] This report shall include total aggregate income tax paid by corporations covered under AS 43.21.010 - 43.21.120 and aggregate income and deductions by category, so classified as to prevent the identification of particular returns or reports.

(b) The legislative auditor shall transmit to the legislature an annual report reviewing the actions of the department in administering AS 43.21.010 - 43.21.120.

Sec. 43.21.120. Definitions [Repealed effective January 1, 1982]. Unless the context requires otherwise the definitions contained in *AS 43.55.140* are applicable to AS 43.21.010 - 43.21.120. In addition, in AS 43.21.010 - 43.21.120

(1) [**80] "base of operations" means the closest point on land to the offshore oil or gas production operations from which goods, services and supplies flow to those offshore oil or gas production operations;

(2) "consolidated business" means a corporation or group of corporations having more than 50 per cent

common ownership direct or indirect, or a group of corporations in which there is common control either direct or indirect as evidenced by any arrangement, contract or agreement.

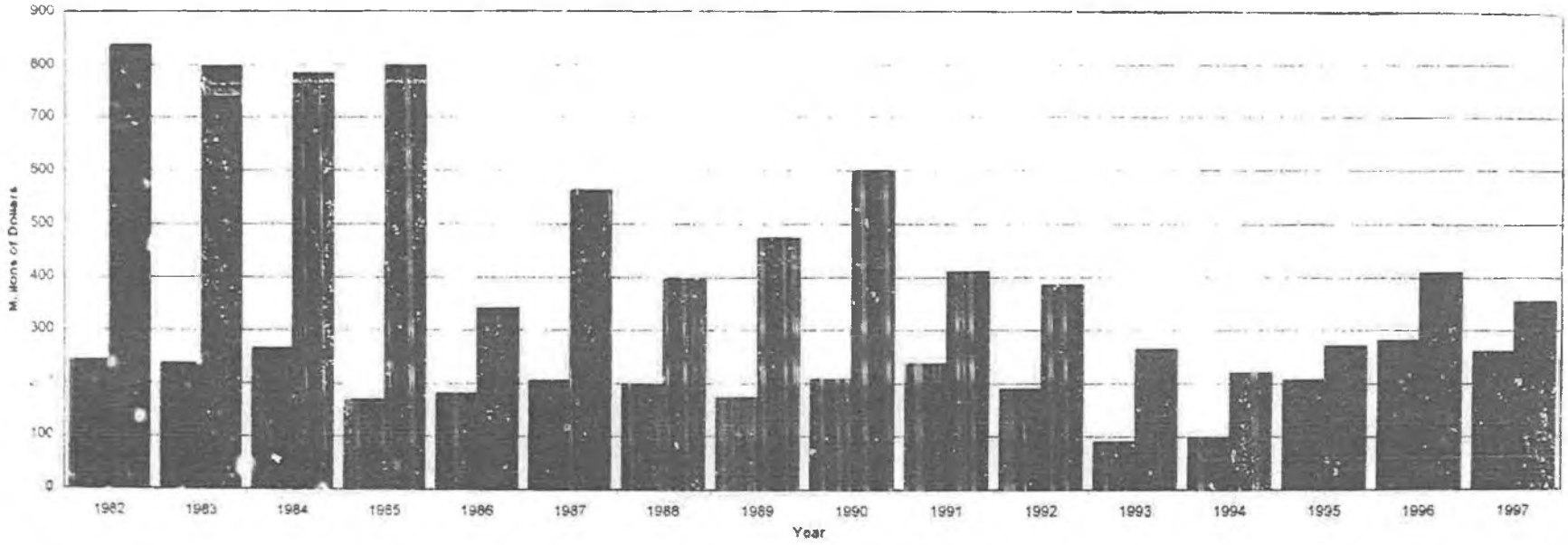
Burke, Chief Justice, Rabinowitz, Matthews, and Moore, Justices. Compton, Justice, not participating.

Comparison of Actual Oil and Gas Corporate Income Tax Collected with Estimated Revenues using a Separate Accounting Income Tax Approach (In Millions)

	Actual O&G Income Tax Collected	Estimated Separate Accounting Revenues	Difference
1982	242.50	837.62	595.12
1983	236.00	796.15	560.15
1984	265.10	782.86	517.76
1985	163.60	797.00	628.40
1986	181.00	341.00	160.00
1987	205.00	562.00	357.00
1988	198.00	396.00	198.00
1989	174.00	473.00	299.00
1990	208.00	598.00	390.00
1991	237.00	410.00	173.00
1992	189.00	385.00	196.00
1993	90.00	264.00	174.00
1994	98.00	219.00	121.00
1995	206.00	270.00	64.00
1996	281.00	408.00	127.00
1997	259.00	355.00	96.00
TOTALS	**$3,238.20**	**$7,894.63**	**$4,656.43**

Source: 1986-97 calendar year data from DOR letter D. Dickinson to J. Donohue Sept. 23, 1999; 1982-85 fiscal data is from DOR report dated Oct. 31, 1985, Wright to Nordale, In re HB353; data for second half of 1985 not available at this time.

Comparison of Actual Oil and Gas Corporate Income Tax Collected with Estimated Revenues using a Separate Accounting Income Tax Approach Assuming Existing AS 43.20 Rate



Source: 1986-97 calendar year data from DOR letter, D. Dickinson to J. Donohue, 9/23/99; 1982-85 fiscal data is from DOR report dated 10/31/85, Wright to Nordale, in re HB353. Data for second half of 1985 not available at this time. Since the actual income tax collections for FY82 (the phase out year) included revenue from both separate accounting and modified apportionment, the actual income tax collections for FY82 depicted on the chart includes an estimate of revenue from modified apportionment as if it had been in effect for the entire fiscal year.

To: Rep. Paul Seaton

From: Roger Marks

Date: March 9, 2012

Re: Jurisdictions that Require Separate Accounting - Revised

Per your March 1 request to Rep. Hawker, the following discusses the jurisdictions both international and domestic that require separate accounting for deriving taxable income for oil and gas corporate income taxes. This memo supersedes my March 7 note.

At the national level, of the 57 countries in BP's 2011 "Statistical Review of World Energy"[1] that produce either a minimum of 80,000 barrels per day of oil, or 0.1 billion cubic feet per day of gas (see attached), nearly all of them impose a corporate income tax.[2] (Iran, Libya, Mexico, and Trinidad and Tobago do not.)

At the national level, in all cases the tax is calculated on a separate accounting basis. This takes one of three different forms. In some cases the taxable income is ring fenced on a project basis or an area basis. In some cases taxable income is based on the worldwide income of the domestic producers (recognizing foreign taxes paid). And in some cases the taxable income is based on domestic sourced income. But again, in all cases, a separate accounting approach is used to derive taxable income for corporate income taxes at the national level.

At the sub-national level, there are only two instances where political subdivisions are empowered to levy corporate income taxes: the United States (state level) and Canada (provincial level). In most other nations local income is usually raised through either gross proceeds taxes, or indirect taxes such as sales or property taxes.

In the U.S. there are 24 oil producing states that have a corporate income tax. Twenty-two of them use apportionment. In general they use payroll, sales, and property factors. Some states use equal weight for all three factors. Some give greater weights to some factors over others. Some do not use all the factors. Only Alaska uses an extraction (production) factor to derive oil and gas income (in lieu of payroll). (This is tied up in the history of the relationship between the state corporate income tax and the production tax in Alaska.)

Some of these states use worldwide income to apportion. Some use water's edge.

In one of these states, Louisiana, the taxpayer can solicit the state to use separate accounting if a) it can demonstrate apportionment yields an unfair result, b) the unit of the taxpayer's business operating in the state could be successfully operated independently of the units in other states, c) the unit makes all of its sales in the state or derives all of its gross revenues from sources in the state, *and* d) any merchandise or products sold by the unit in the state are either i) produced by

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[1] BP Statistical Review of World Energy, June 2011

[2] Sources: Ernst & Young, KPMG. Van Meurs, Wood Mackenzie

the taxpayer in Louisiana, ii) purchased by the taxpayer from nonaffiliated sources, iii) purchased from an affiliated source at not more than the price at which similar merchandise or products in similar quantities could be purchased from nonaffiliated sources, *or* iv) transferred from another department of the taxpayer's business at not more than the actual cost to the taxpayer. It is unclear how many taxpayers, if any, are doing this, but I would opine that given the criteria, most major integrated producers would not qualify for separate accounting.

Two states use separate accounting for oil and gas: Mississippi and Oklahoma.

In Canada the provinces apportion worldwide income using a 50/50 sales/payroll factor formula.

Production*

Thousand barrels daily	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Change 2010 over 2009	2010 share of total
US	7733	7669	7626	7400	7228	6895	6841	6847	6734	7271	7513	3.2%	8.7%
Canada	2721	2677	2858	3004	3085	3041	3208	3297	3251	3224	3336	4.3%	4.2%
Mexico	3450	3560	3585	3789	3824	3760	3683	3471	3167	2979	295a	-0.8%	3.7%
Total North America	13904	13906	14069	14193	14137	13696	13732	13616	13152	13474	13a0a	2.5%	16.6%
Argentina	819	830	818	806	754	725	716	698	682	676	651	-1.8%	0.8%
Brazil	1268	1337	1499	1555	1542	1716	1809	1833	1899	2029	2137	5.3%	2.7%
Colombia	711	627	601	564	551	554	559	561	616	685	e01	16.9%	1.0%
Ecuador	409	416	401	427	535	541	545	520	514	495	495	*	0.6%
Peru	100	98	98	92	94	111	116	114	120	145	157	8.2%	0.2%
Trinidad & Tobago	138	135	155	164	152	171	174	154	149	151	146	-4.3%	0.2%
Venezuela	3239	3142	2895	2554	2907	2937	2808	2613	2558	2438	2471	1.4%	3.2%
Other S. & Cent. America	130	137	152	153	144	142	139	141	139	133	131	-1.6%	0.2%
Total S. & Cent. America	6813	6722	6619	6314	6680	6898	6865	6835	6676	6753	69e9	3.5%	9.0%
Azerbaijan	282	301	311	313	315	452	654	869	915	1033	1037	0.5%	1.3%
Denmark	363	348	371	368	390	377	342	311	287	265	249	-5.8%	0.3%
Italy	95	86	115	116	113	127	120	122	108	95	106	11.7%	0.1%
Kazakhstan	744	836	1018	1111	1297	1356	1426	1484	1554	1688	1757	4.4%	2.1%
Norway	3346	3418	3333	3264	3189	2969	2779	2551	2459	2358	2137	-9.4%	2.5%
Romania	131	130	127	123	119	114	105	99	98	93	e9	-4.7%	0.1%
Russian Federation	6536	7056	7698	8544	9287	9552	9769	9978	9888	10035	10270	2.2%	12.9%
Turkmenistan	144	162	182	202	193	192	186	198	207	210	216	2.8%	0.3%
United Kingdom	2667	2476	2463	2257	2028	1809	1636	1638	1526	1452	1339	-7.7%	1.6%
Uzbekistan	177	171	171	166	152	126	125	114	114	107	a7	-17.8%	0.1%
Other Europe & Eurasia	465	486	501	509	497	489	458	453	432	411	374	-7.0%	0.5%
Total Europe & Eurasia	14950	15450	16395	16873	17580	17542	17586	17815	17590	17746	17661	-0.4%	21.8%
Iran	3855	3892	3709	4183	4248	4234	4286	4322	4327	4199	4245	0.9%	5.2%
Iraq	2614	2523	2116	1344	2030	1833	1999	2143	2428	2442	2460	0.6%	3.1%
Kuwait	2206	2148	1995	2329	2475	2618	2690	2636	2782	2480	250e	0.6%	3.1%
Oman	959	960	904	824	786	778	742	715	754	813	e65	5.0%	1.0%
Qatar	757	754	764	879	992	1028	1110	1197	1378	1345	1569	13.5%	1.7%
Saudi Arabia	9491	9209	8928	10164	10638	11114	10853	10449	10846	9893	10007	0.7%	12.0%
Syria	548	581	548	527	495	450	435	415	398	375	3e5	2.7%	0.5%
United Arab Emirates	2620	2551	2390	2695	2847	2983	3149	3053	3088	2750	2e49	3.5%	3.3%
Yemen	450	455	457	449	420	416	380	345	304	287	264	-7.9%	0.3%
Other Middle East	48	47	48	48	48	34	32	35	33	37	3a	0.6%	*
Total Middle East	23547	23120	21858	23442	24881	25488	25675	25309	26038	24625	251ea	1.7%	30.3%
Algeria	1578	1562	1680	1852	1946	2015	2003	2016	1993	1818	1809	-0.3%	2.0%
Angola	746	742	905	870	1103	1405	1421	1684	1875	1784	1e51	3.8%	2.3%
Chad	–	–	–	24	168	173	153	144	127	118	122	3.5%	0.2%
Republic of Congo (Brazzaville)	254	234	238	217	223	245	278	229	241	270	292	8.1%	0.4%
Egypt	781	758	751	749	721	696	697	710	722	742	736	-0.6%	0.9%
Equatorial Guinea	91	177	230	266	351	358	342	350	347	307	274	-10.8%	0.3%
Gabon	327	301	295	240	235	234	235	230	235	230	245	6.5%	0.3%
Libya	1475	1427	1375	1485	1623	1745	1815	1820	1820	1652	1659	0.5%	2.0%
Nigeria	2155	2274	2103	2238	2431	2499	2420	2305	2113	2061	2402	16.2%	2.9%
Sudan	174	217	241	265	301	305	331	468	480	479	4a6	1.5%	0.6%
Tunisia	78	71	74	68	71	73	70	97	89	83	a0	-4.7%	0.1%
Other Africa	144	134	135	138	164	154	153	166	162	156	143	-8.0%	0.2%
Total Africa	7804	7897	8029	8411	9334	9902	9918	10218	10204	9699	1009e	4.2%	12.2%
Australia	809	733	730	624	582	580	551	555	555	520	562	8.9%	0.6%
Brunei	193	203	210	214	210	206	221	194	175	168	172	2.5%	0.2%
China	3252	3306	3346	3401	3481	3637	3705	3737	3809	3800	4071	7.1%	5.2%
India	726	727	753	756	773	738	762	769	768	754	a26	9.8%	1.0%
Indonesia	1456	1387	1289	1176	1130	1090	996	972	1003	990	9a6	-0.3%	1.2%
Malaysia	735	719	757	776	793	759	747	763	768	739	716	-3.1%	0.8%
Thailand	176	191	204	236	223	265	296	305	321	331	334	0.9%	0.4%
Vietnam	328	350	354	364	427	398	367	337	317	345	370	6.9%	0.5%
Other Asia Pacific	200	195	193	195	235	298	306	320	340	329	312	-4.7%	0.3%
Total Asia Pacific	7874	7811	7837	7742	7854	7959	7941	7951	8054	7978	e350	4.9%	10.2%
Total World	74e98	74888	74788	77075	a0540a	a14e5	a1729	a1544	a2015	a077a	a2095	2.2%	100.0%
of which: OECD	21591	21314	21440	21174	20775	19870	19463	19114	18414	18471	1a490	0.2%	22.1%
Non-OECD	53361	53550	53260	55900	50730	61616	62266	62430	63600	61807	63605	2.7%	77.9%
OPEC	31145	30640	29061	31020	33775	34051	35098	34757	35722	33365	34324	2.5%	41.5%
Non-OPEC‡	35734	35606	35907	35556	35385	34685	34315	33981	33466	33639	342a7	1.9%	41.7%
European Union	3493	3285	3339	3128	2902	2659	2422	2398	2222	2098	1951	-6.5%	2.4%
Former Soviet Union	8014	8660	9533	10409	11407	11839	12316	12795	12827	13214	134e4	2.0%	16.8%

*Includes crude oil, shale oil, oil sands and NGLs (the liquid content of natural gas where this is recovered separately). Excludes liquid fuels from other sources such as biomass and coal derivatives.
*Less than 0.05%.
‡Excludes Former Soviet Union.
Note: Annual changes and shares of total are calculated using million tonnes per annum figures.

Production*

Billion cubic metres	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Change 2010 over 2009	2010 share of total
US	543.2	555.5	536.0	540.6	526.4	511.1	524.0	545.8	570.8	582.8	**611.0**	4.7%	19.3%
Canada	182.2	186.5	187.9	184.7	183.7	187.1	188.4	182.5	176.4	163.9	**159.6**	-2.5%	5.0%
Mexico	38.9	38.2	39.4	41.1	43.6	45.0	51.6	53.6	54.2	54.9	**55.3**	0.7%	1.7%
Total North America	764.7	780.1	763.5	766.8	753.8	743.3	763.9	781.8	801.5	801.8	**825.1**	2.9%	26.0%
Argentina	37.4	37.1	36.1	41.0	44.9	45.6	46.1	44.5	44.1	41.4	**40.1**	-3.0%	1.3%
Bolivia	3.2	4.7	4.9	6.4	9.8	11.9	12.8	13.8	14.3	12.3	**14.4**	16.8%	0.4%
Brazil	7.5	7.7	9.2	10.0	11.0	11.0	11.3	11.2	12.7	11.7	**14.4**	23.5%	0.5%
Colombia	5.9	6.1	6.2	6.1	6.4	6.7	7.0	7.5	9.1	10.5	**11.3**	7.2%	0.4%
Peru	0.3	0.4	0.4	0.5	0.9	1.5	1.8	2.7	3.4	3.5	**7.2**	108.4%	0.2%
Trinidad & Tobago	14.5	15.5	18.0	26.3	27.3	31.0	36.4	38.0	39.3	40.6	**42.4**	4.4%	1.3%
Venezuela	27.9	29.6	28.4	25.2	26.4	27.4	31.5	29.5	30.0	28.7	**28.5**	-0.7%	0.9%
Other S. & Cent. America	3.4	3.5	3.4	3.1	3.1	3.4	4.1	3.9	3.7	3.7	**3.6**	-0.9%	0.1%
Total S. & Cent. America	100.3	104.5	106.7	118.7	131.7	138.6	151.1	152.5	157.6	151.9	**161.2**	6.2%	5.0%
Azerbaijan	5.1	5.0	4.7	4.6	4.5	5.2	6.1	9.8	14.8	14.8	**15.1**	2.2%	0.5%
Denmark	8.2	8.4	8.4	8.0	9.4	10.4	10.4	9.2	10.1	8.4	**8.2**	-3.0%	0.3%
Germany	16.9	17.0	17.0	17.7	16.4	15.9	16.6	14.3	13.0	12.2	**10.6**	-12.7%	0.3%
Italy	15.2	14.0	13.4	12.7	11.9	11.1	10.1	8.9	8.5	7.3	**7.6**	3.6%	0.2%
Kazakhstan	10.4	10.5	10.2	12.6	20.0	22.6	23.9	26.8	29.8	32.5	**33.6**	3.3%	1.1%
Netherlands	58.1	62.4	60.3	58.1	68.5	62.5	61.6	60.5	66.6	62.7	**70.5**	12.4%	2.2%
Norway	49.1	53.0	66.5	73.1	78.5	86.0	87.6	89.7	90.3	103.7	**106.4**	2.5%	3.3%
Poland	3.7	3.9	4.0	4.0	4.4	4.3	4.3	4.3	4.1	4.1	**4.1**	0.5%	0.1%
Romania	13.8	13.6	13.2	13.0	12.8	12.4	11.9	11.5	11.4	11.3	**10.9**	-2.9%	0.3%
Russian Federation	528.5	526.2	538.8	581.5	573.3	580.1	595.2	592.0	601.7	527.7	**588.9**	11.6%	18.4%
Turkmenistan	42.5	46.4	48.4	53.5	52.8	57.0	60.4	65.4	66.1	36.4	**42.4**	16.4%	1.3%
Ukraine	16.2	16.6	17.0	17.6	18.4	18.6	18.7	18.7	19.0	19.3	**18.6**	-3.8%	0.6%
United Kingdom	108.4	105.8	103.6	102.9	96.4	88.2	80.0	72.1	69.6	59.7	**57.1**	-4.3%	1.8%
Uzbekistan	51.1	52.0	51.9	52.0	54.2	54.0	54.5	59.1	62.2	60.9	**59.1**	-1.5%	1.8%
Other Europe & Eurasia	11.1	10.9	11.2	10.6	11.0	10.9	11.5	10.6	10.3	9.7	**10.0**	3.0%	0.3%
Total Europe & Eurasia	938.9	948.0	967.4	1001.9	1032.3	1038.0	1051.7	1053.2	1080.5	960.8	**1048.1**	7.8%	32.6%
Bahrain	9.8	9.1	9.5	9.6	9.8	10.7	11.3	11.8	12.7	12.8	**13.1**	2.4%	0.4%
Iran	60.2	66.0	75.0	81.5	84.9	103.5	108.6	111.9	116.3	131.2	**138.5**	5.6%	4.3%
Iraq	3.2	2.8	2.4	1.6	1.0	1.5	1.5	1.5	1.9	1.2	**1.3**	8.7%	*
Kuwait	9.8	10.5	9.5	11.0	11.9	12.2	12.5	12.1	12.8	11.2	**11.6**	3.5%	0.4%
Oman	9.7	14.0	16.0	16.5	18.5	19.8	23.7	24.0	24.1	24.8	**27.1**	9.4%	0.8%
Qatar	23.7	27.0	29.5	31.4	33.2	45.8	50.7	63.2	77.0	89.3	**116.7**	30.7%	3.6%
Saudi Arabia	49.8	53.7	56.7	60.1	65.7	71.2	73.5	74.4	80.4	78.5	**83.9**	7.0%	2.6%
Syria	5.5	5.0	6.1	6.2	6.4	5.5	5.7	5.6	5.3	5.7	**7.8**	37.3%	0.2%
United Arab Emirates	38.4	44.9	43.4	44.8	46.3	47.8	48.0	50.3	50.2	48.8	**51.0**	4.5%	1.6%
Yemen	–	–	–	–	–	–	–	–	–	0.8	**6.2**	704.6%	0.2%
Other Middle East	0.3	0.3	0.9	0.8	1.5	1.9	2.8	3.0	3.7	3.1	**3.5**	15.0%	0.1%
Total Middle East	206.1	233.3	241.2	262.9	285.1	319.9	338.1	357.8	384.3	407.1	**469.7**	15.2%	14.4%
Algeria	84.4	78.2	80.4	82.8	80.0	88.2	84.5	84.6	85.8	79.6	**80.4**	1.1%	2.5%
Egypt	21.0	25.2	27.3	30.1	33.0	42.5	54.2	56.7	59.0	62.7	**61.3**	-2.2%	1.9%
Libya	5.9	6.2	5.9	5.5	8.1	11.3	13.2	15.3	15.9	15.9	**15.8**	-0.6%	0.5%
Nigeria	12.5	14.9	14.2	19.2	22.8	22.4	28.4	35.0	35.0	24.8	**33.6**	35.7%	1.1%
Other Africa	6.5	6.9	6.6	7.2	8.9	9.9	10.4	12.3	15.8	16.3	**17.6**	8.4%	0.6%
Total Africa	130.3	131.5	134.4	144.9	154.7	174.3	191.2	203.1	211.5	199.2	**209.8**	4.9%	6.5%
Australia	31.2	32.1	32.2	32.7	35.8	37.2	40.2	41.9	41.6	47.9	**50.4**	5.1%	1.6%
Bangladesh	10.0	10.7	11.4	12.3	13.2	14.5	15.3	16.3	17.9	19.7	**20.8**	5.3%	0.6%
Brunei	11.3	11.4	11.5	12.4	12.2	12.0	12.6	12.3	12.2	11.4	**12.2**	6.7%	0.4%
China	27.2	30.3	32.7	35.0	41.5	49.3	58.6	69.2	80.3	85.3	**96.8**	13.5%	3.0%
India	26.4	26.4	27.6	29.5	29.2	29.6	29.3	30.1	30.5	30.2	**50.9**	29.7%	1.6%
Indonesia	65.2	63.3	69.7	73.2	70.3	71.2	70.3	67.6	69.7	71.9	**82.0**	14.0%	2.6%
Malaysia	45.3	46.9	48.3	51.8	53.9	61.1	63.3	64.6	64.7	64.1	**66.5**	3.7%	2.1%
Myanmar	3.4	7.0	8.4	9.6	10.2	12.2	12.6	13.5	12.4	11.5	**12.1**	4.8%	0.4%
Pakistan	21.5	22.7	24.6	30.4	34.5	35.5	36.1	36.8	37.5	38.4	**39.5**	2.7%	1.2%
Thailand	20.2	19.6	20.5	21.5	22.4	23.7	24.3	26.0	28.8	30.9	**36.3**	17.4%	1.1%
Vietnam	1.6	2.0	2.4	2.4	4.2	6.4	7.0	7.1	7.5	8.0	**9.4**	16.7%	0.3%
Other Asia Pacific	9.0	9.5	10.9	10.7	10.1	11.1	14.2	16.9	17.7	17.9	**17.3**	-3.4%	0.5%
Total Asia Pacific	272.1	282.0	300.2	321.6	337.4	363.0	383.7	402.2	420.7	440.4	**493.2**	10.3%	15.4%
Total World	**2413.4**	**2476.0**	**2513.4**	**2616.5**	**2694.0**	**2776.9**	**2880.7**	**2950.5**	**3062.1**	**2975.9**	**3193.3**	**7.3%**	**100.0%**
of which: OECD	1073.9	1096.6	1096.4	1092.8	1091.9	1076.4	1092.9	1102.2	1134.3	1126.3	**1159.6**	2.9%	36.5%
Non-OECD	1339.5	1381.4	1433.0	1519.7	1602.1	1701.6	1787.9	1848.3	1927.8	1849.5	**2033.5**	9.9%	63.5%
European Union	231.9	230.8	227.6	223.6	227.3	213.0	201.3	187.5	180.4	171.5	**174.9**	2.0%	5.5%
Former Soviet Union	654.2	657.1	671.4	702.1	723.4	737.7	752.0	772.1	783.8	690.9	**757.9**	9.7%	23.7%

*Excluding gas flared or recycled.

Source: Includes data from Cedigaz.

*Less than 0.05%.

Notes: As far as possible, the data above represent standard cubic metres (measured at 15°C and 1013 mbar), because it is derived directly from tonnes of oil equivalent using an average conversion factor, it does not necessarily equate with gas volumes expressed in specific national terms.

Annual changes and shares of total are calculated using million tonnes of oil equivalent figures.

Natural gas production data expressed in billion cubic feet per day is available at www.bp.com/statisticalreview

MISSISSIPPI
STATE TAX COMMISSION
OFFICE OF REVENUE
FORM 83-100

1999

PLEASE USE THIS LABEL
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1999 Corporation Income and Franchise Tax Forms

If someone else prepares your income tax return, please take this forms packet to that person so the peel-off label above and the enclosed envelope may be used for your return. There are some important things you can do to help speed processing and reduce the cost of your government:

- **Use the peel-off label**. Remove the label and place it in the name and address area of your return. If the label is NOT correct, neatly mark through incorrect information and plainly print or type correct information on the label. DO NOT USE THIS LABEL ON COMPUTER GENERATED FORMS.
- **Use the envelope enclosed inside this booklet.**
- Additional schedules and attachments may be stapled to your return.
- C-Corporations and S-Corporations have separate forms booklets. If you received the wrong booklet, please call (601) 923-7000 for the correct set of forms and instructions.
- **Web site** - Please visit our web site located at **http://mstc.state.ms.us** to find any updates to the instructions and/or worksheets that are contained in this booklet. Click on **Tax Area** in the index and then on **Corporate Income and Franchise Tax, Partnerships, LLP, LLC**.

CHANGES FOR 1999:

Attention: Multistate Taxpayers. The 1997 Regular Session of the Mississippi Legislature changed the way that the Mississippi receipts for the franchise tax apportionment ratio is calculated. Starting for years ending on or after January 1, 1999, taxpayers that apportion their income to Mississippi using an apportionment method that includes a sales or receipts ratio will no longer use the income tax ratio to calculate the Mississippi receipts for the franchise tax apportionment ratio. See instructions in this booklet for details. (1997 House Bill 1816)

NEW 1999 LEGISLATION

The 1999 Regular Session of the Mississippi Legislature deleted the requirement to use the cost method of accounting in determining the ratio to be used by holding corporations to make the holding company exclusion of capital from its capital base for tax years ending after 3/16/99. (Senate Bill 2740) Amended Section 27-13-9(2)

A new tax credit was added that provides an income tax credit to certain taxpayers who incur cost for approved reforestation practices. Corporations and Partnerships must use Form 83-315 and Individuals are to use Form 80-315. (House Bill 832) See instructions inside. Created Section (cite unknown at time of printing)

For years beginning on or after 1/1/99 dividends received by a holding corporation, as defined in Section 27-13-1, from a subsidiary corporation, as defined in Section 27-13-1 are excluded from income tax. (Senate Bill 2919).

GENERAL INSTRUCTIONS

HOW TO FILL OUT FORMS

Use Black Ink when preparing these returns.

Indicating a Loss - To indicate a loss (negative income), shade the minus (-) box next to the dollar amount. See the example on page 7 of these instructions.

WHO MUST FILE

Every corporation, domesticated or qualified to do business in Mississippi, and every corporation engaged in business in Mississippi or having sources of income from Mississippi, must file a Mississippi combination return of corporate income and franchise tax, Form 83-105.

Every corporation domesticated or qualified to do business in Mississippi must file a return even though the corporation is inactive or not otherwise engaged in business. **SUCH A CORPORATION REMAINS SUBJECT TO THE FILING REQUIREMENTS UNTIL SUCH TIME AS THE CORPORATION IS OFFICIALLY DISSOLVED OR WITHDRAWN THROUGH THE OFFICE OF THE MISSISSIPPI SECRETARY OF STATE.**

Foreign corporations engaged in business in Mississippi or having sources of income in this state who have not qualified to transact business in this state through the offices of the Secretary of State are subject to the measure of the income and franchise tax levy. Corporations exempt from one or more of the levies covered by the combination report must indicate their authority for the exemption.

Under Section 27-7-23(c)(1) and Section 27-13-7 of the Mississippi Code of 1972, as amended, every foreign corporation (those chartered outside Mississippi) which has obtained a certificate of authority from the Secretary of State to do business in Mississippi, or which is in fact doing business, as defined in the Mississippi Code Sections above, regardless of qualifications, is subject to the income/franchise tax levy and is required to file annual income/franchise tax returns unless the corporation is specifically exempt from tax within the purview of Code Section 27-7-29 and Section 27-13-63.

Any corporation subject to the filing requirements noted in the paragraph above MUST FILE AN INCOME/FRANCHISE TAX RETURN BASED ON THE INCOME FROM ITS ACTIVITY, AND ON THE CAPITAL EMPLOYED IN THE STATE. When a corporation obtains a certificate of authority from the Secretary of State to do business in

shall in no case be less than the assessed value of the Mississippi property of the organization for the year preceding the year in which the return is due.

(2) (a) For the purpose of this section, for tax returns for tax years ending before January 1, 1999, an organization which uses a formula method of apportionment in making income tax returns to this state shall determine its gross receipts from business carried on in Mississippi by applying to total unitary receipts the ratio achieved, or which would be achieved, by such formula and adding to the result of such application any nonunitary Mississippi receipts.

(b) For the purpose of this section, for tax returns for tax years ending on or after January 1, 1999, the gross receipts of an organization that is required to use a formula method of apportionment in making income tax returns to this state shall be the same (both as to gross receipts from business carried on in Mississippi and gross receipts wherever located) as the gross receipts (or sales) used for the receipts or sales factor in the applicable income tax formula. However, gross receipts from business carried on in Mississippi, for the purposes of this section, shall also include any receipts from the taxpayer's business operations which are not apportioned but rather are directly allocated or assigned to this state. If the taxpayer is required to use a formula method of apportionment in making income tax returns which does not have a receipts or sales factor, then the receipts factor for the franchise tax formula shall be determined by regulation of the commission.

The amount of capital apportioned to Mississippi is computed on line 14, Form 83-110.

The section of Form 83-110 concerning the assessed values of all real and personal property in Mississippi must be completed by all corporations. Sections 27-13-9 and 27-13-13, Mississippi Code of 1972, provide that the amount of the determined capital in Mississippi shall in no case be less than the assessed value of the Mississippi property of the corporation for the year preceding the year in which the return is due.

Taxable capital and the net franchise tax due are calculated on lines 16 through 20 of Form 83-110. The amount of taxable capital shown on line 17 should be entered on line 1, Form 83-105. The net franchise tax due as shown on line 20 should be entered on line 2, Form 83-105.

INSTRUCTIONS FOR COMPUTING TAXABLE INCOME

Generally, all domestic and foreign corporations having income from sources within Mississippi must complete Form 83-122, Computation of Net Taxable Income Schedule, which makes adjustments for additions to and deductions from Federal ordinary income due to differences in Federal and Mississippi laws, in arriving at the net income (loss) for State purposes.

Total Assignment of Income. If the business activity in respect to any trade or business of the corporation occurs within this state, and if by reason of such business activity the corporation is not taxable in another state, the total net income (loss) of the corporation is assigned to Mississippi.

Direct or Separate Accounting. Any taxpayer, taxable both within and without this State, which maintains or could maintain books of account detailing allocation of receipts and expenditures reflecting clearly the business income attributable to property owned or business done in this State, shall determine Mississippi net business income (loss) from such business activity on the basis of direct or separate accounting. See Regulation 806 for guidelines and details. Multistate entities filing direct accounting must complete Form 83-124, Direct Accounting Income Statement. Multistate construction contractors must complete page 2 of Form 83-124.

Apportionment of Business Income. If the business activity in respect to any trade or business of a taxpayer occurs both within and without this state, and if by reason of such business activity the taxpayer is taxable in another state, the portion of the net income (loss) arising from such trade or business which is derived from sources within this state, shall, where direct or separate accounting of net income (loss) is not feasible, be determined by apportionment in accordance with the formulas prescribed by Regulation 806. In such case, the taxpayer must complete Form 83-125, Mississippi Business Income Apportionment Schedule.

Allocation of Nonbusiness Income. Nonbusiness income (loss) shall be allocated by multistate corporations within and without this state in accordance with the provisions of Regulation 806.

Divisional Accounting. If the business activity in respect to any trade or business of a taxpayer is conducted on a division basis and division or divisions of the taxpayer are "doing business" within this state, the Mississippi taxable income of the taxpayer, where separate accounting is or can be maintained on each division, shall, at the election of the Commissioner, be determined on a divisional basis in lieu of a company-wide accounting basis. See Regulation 806.

CONSOLIDATED OR COMBINED INCOME TAX RETURNS FOR AFFILIATED GROUP OF CORPORATIONS

Under certain conditions and limitations, an affiliated group of corporations shall have the privilege of making, or the Commissioner may require, a consolidated or combined return for the tax year in lieu of separate returns. Mississippi Regulation 807 shall govern with respect to the manner and basis for filing consolidated or combined returns of an affiliated group of corporations.

EACH corporation of an affiliated group of corporations eligible for and electing to file in a combined income tax return must file its own Mississippi corporate income tax return (Form 83-105) and each corporation must complete and attach to their respective return all applicable schedules including the schedule for computation of net income (loss), Form 83-122.

One corporation of the group of corporations must be designated as the Reporting Corporation for purposes of reporting income(loss) for the group. This is indicated on page 1, line 3, of Form 83-105. In addition to the regular income tax return, the designated Reporting Corporation must complete and attach to its return Form 83-310, Summary of Net Income of Corporations. (Please refer to instructions on Form 83-310). The combined net income (loss) (Form 83-310, column C) of the affiliated group must be reported by the Reporting Corporation on its return by entering such amount on page 1, line 4, Form 83-105. Other included members of the group should enter "zero" on page 1, line 4, Form 83-105 and must indicate the name and I.D. number of the Reporting Corporation in the space provided.

A Mississippi consolidated tax return is where two or more 100% Mississippi corporations file as one corporation for income tax purposes. Form 83-310 is not filed in this case, as only one income tax return is being filed by the reporting corporation for the group.

Consolidated or combined reporting is authorized only with respect to the income tax levy. Mississippi law does **NOT** authorize consolidated or combined reporting for franchise tax; therefore, separate returns are required of all corporations chartered to do business in Mississippi or which are in fact doing business in Mississippi.

Mississippi income tax due on the combined net income of the affiliated group must be determined and reported by the Reporting Corporation. In case of delinquency or failure on the part of the Reporting Corporation to report and pay the income tax due, each included member of the affiliated group is severally liable for the tax on a consolidated or combined return and for any determined deficiency thereon.

An affiliated group of corporations required by the Commissioner to file a consolidated or combined income tax return must do so in accordance with the provisions of Mississippi Regulation 807, or from specific instructions from the Commissioner.

NET OPERATING LOSSES

For any taxable year ending after December 31, 1997, the period for net operating loss carrybacks and net operating loss carryovers shall be the same as those established by the Internal Revenue Code and the rules, regulations, rulings and determinations promulgated thereunder. §27-7-17(1)(l) of the Mississippi Code of 1972, as amended, was amended so that when the Internal Revenue Code loss carryback and carryforward periods change, the Mississippi carryback and carryforward will change as well.

For years ended on or before December 31, 1997 the following applies: A net operating loss for any tax year ending after December 31, 1991, could be carried back to the taxable year preceding the year of the loss. A net operating loss for any tax year ending after December 31, 1992, can be carried back to the 2 taxable years preceding the year of the loss. A net operating loss for any tax year ending after December 31, 1993, can be carried back to the 3 taxable years preceding the year of the loss. Carry the net operating loss to the earliest year first. A short taxable year counts as a taxable year. A taxpayer can elect to relinquish the entire carryback period with regard to a net operating loss from an eligible year, but once this election is made, it cannot be changed.

Prior to January 1, 1992, Mississippi allowed a 5 year NOL carryforward but no carryback.

Form 83-155 or other comparable schedule must be attached, or the NOL will not be allowed.

CAPITAL GAINS AND LOSSES

The Federal Schedule D and Federal Form 4797 cannot be used for the Mississippi return, but the federal forms have been replaced with similar state forms. Federal Schedule D has been replaced by state Form 83-135. Federal Form 4797 has been replaced by state Forms 83-140 and 83-145. The reason for this is that for state purposes some types of gains and

losses must be allocated and some must be apportioned. A taxpayer should only use the forms that apply to it.

Mississippi Form 83-135 should be substituted for Federal Schedule D. It provides for both apportioning capital gains and losses and allocating capital gains and losses to Mississippi on one page. All corporations that are not multistate (100% of their income is reported to Mississippi) should use Form 83-135, Column f. Multistate corporations may need to use both Columns f and g. A multistate corporation must segregate gains and/or losses into business (see Regulation 806 for state definition of business income) and nonbusiness. If the corporation apportions income, then business gains or losses would be apportioned and nonbusiness gains or losses would be allocated. Business gains or losses subject to apportionment would be computed on Form 83-135, Column g. Nonbusiness gains or losses allocated to Mississippi would be computed on Form 83-135, Column f, and would include only the allocated Mississippi property and amounts.

Mississippi Form 83-140 should be substituted for Federal 4797 and should be used for gains or losses that are allocated directly to Mississippi. Form 83-145 should also be substituted for Federal Form 4797, but it should be used for gains or losses that are apportioned to Mississippi.

If a corporation files showing all of its income in Mississippi, the state form should still be used. The correct form(s) to use are Forms 83-135 and 83-140. The state form should still be used because the state capital loss carryforward may be different and some of the items that flow into the federal forms (casualty and theft losses, etc.) may be different for state purposes.

For Mississippi income tax purposes, a multistate corporation either allocates (directly assigns) or apportions income.

If a taxpayer files using separate accounting (allocates), then income is directly assigned to the different states in which the taxpayer is doing business. Even if separate accounting is used, any general or administrative income, such as business dividends should be apportioned between the states in which the corporation is doing business. If a corporation files using separate accounting, then any gains or losses other than G&A gains or losses should be computed on the correct state form (Form 83-135 or Form 83-140) for allocation. The G&A gains or losses should computed on the correct state form (Form 83-135 or Form 83-145) for apportionment. Both forms (if used) would then be attached to the return and the Mississippi amounts computed on the form(s) entered into the appropriate income schedule.

If a taxpayers files using an apportionment formula, then income is apportioned (on a percentage basis) among the states in which the taxpayer is doing business. Gains or losses from the sale of business assets (Mississippi's definition of business assets, not the federal definition; see Regulation 806 for more detail) is apportioned. Gains or losses from the sale of nonbusiness assets are allocated. For gains or losses that are apportioned use Form 83-135 or Form 83-145. For gains or losses that are allocated use Form 83-135 or Form 83-140.

Forms 83-140 and 83-145 have not been included in this booklet. They may be obtained by calling 601-923-7800 or requested on our web site located at http://mstc.state.ms.us.

Long Term Capital Gains from Sales of Stock/Interest in Domestic (Mississippi) Corporations, Limited Partnerships or Limited Liability Companies

The 1997 Regular Session of the Mississippi Legislature amended Section 27-7-9 of the Mississippi Code of 1972 to clarify how gains that are not recognized from the sale of interests in certain Mississippi businesses are treated for income tax purposes and for related purposes. The amendment was effective March 18, 1997 and codified in Section 27-7-9(f)(10) and is generally effective for taxpayers whose tax year begins from and after that date. A copy of the amendment is reproduced on page 2 of Form 83-135, 1999 Allocable and Apportionable Capital Gains and Losses Schedule included in this booklet.

"Domestic" means the corporation, limited partnership, or limited liability company must have been incorporated or formed in the State of Mississippi.

Capital Loss Carrybacks/Carryforwards. Effective for tax years beginning on or after January 1, 1992, the capital loss provisions were changed for Mississippi income tax purposes. Prior to the change, capital losses could be deducted against other income, but they were not allowed to be carried forward. After the law change, capital losses can only offset capital gains, but a capital loss can be carried back to the 3 taxable years preceding the loss year and be carried over to the 5 years succeeding the loss year. All provisions of the Internal Revenue Code in regard to limitations on capital losses, capital loss carrybacks and carryovers and holding periods shall be applicable.

BUSINESS INCOME OF PRODUCERS OF MINERAL OR NATURAL RESOURCE PRODUCTS

Taxpayers engaged in the trade or business of producing oil, gas, other liquid hydrocarbons, sulphur, coal, sand, gravel and other mineral or natural resource products, except timber, shall determine Mississippi net business income from such activity on a direct or separate accounting basis. The Mississippi gross business income from the production of mineral or natural resources shall include: (a) Sales of natural or mineral resources produced in Mississippi and sold in this state; (b) the market value, at the time of transfer, of all natural or mineral resources produced in this state and transferred by the taxpayer to another state for sale, refining, processing or manufacturing, provided that if the natural or mineral resources are sold by means of an "arms-length" transaction prior to refining, processing or manufacturing, the market value prescribed herein shall not exceed the selling price; and (c) the market value at the time of transfer, of all natural or mineral resources produced by the taxpayer in Mississippi and transferred to a refinery, processing plant, or manufacturing facility of the taxpayer in Mississippi.

A natural resource product shall be deemed to be sold in Mississippi if it is located in this state at the time title thereto passes to the purchaser. In the absence of specific proof of value of natural resources at the time of transfer from the state, the value of natural resources at the time of production shall be determined in accordance with the methods prescribed for the determination of "gross income from the property" for purposes of percentage depletion for federal income tax purposes.

INCENTIVE CREDITS

Incentive credits may be used to offset all or part of the corporate income tax liability. For any of these credits to be allowed, schedules must be attached showing the computations.

Form 83-401, Income Tax Credit Summary, should be completed and attached as a part of the return.

The following is a brief description of the major credits allowed under State statutes:

Jobs Tax Credit. A credit is allowed for increasing employment levels in certain types of business. For a credit to be allowed, the business must be primarily engaged in manufacturing, processing, warehousing, distribution, wholesaling, or research and development; or designated by rule and regulation by the Department of Economic and Community Development as air transportation and maintenance facilities, final destination or resort hotels having a minimum of 150 guest rooms, or movie industry studios, or telecommunications enterprises.

The amount of the credit is determined by the classification of the county in which the qualified job is located. The 82 counties are divided into 3 groups. These groups are less developed, moderately developed and developed.

Credit is allowed annually for each net new full time job created for 5 years beginning with years 2 through 6 after the creation of the job. Credit is not allowed for a year if the net employment increase falls below the minimum level. The dollar credit per employee and the minimum number of new jobs needed to be created, in a given year, to qualify for this credit is listed below.

County Classification	Minimum No. of Jobs in a Given Year	Dollar Credit Per Job
Less Developed	10 or More	$2,000 Annually
Moderately Developed	15 or More	$1,000 Annually
Developed	20 or More	$ 500 Annually

The number of jobs created is calculated by taking the average level of employment for the given year (taxpayers reporting period for income tax) less the average level of employment of the prior reporting prior (12 months). The Corporate Tax Section should be consulted if short periods are involved. This is the only credit that involves the use of an average increase over the prior year in its calculation.

Form 83-450, New Jobs Credit Schedule, must be completed and attached to the return.

National and Regional Headquarters Credit. A credit of $500 for each net new full-time employee is allowed for any company establishing or transferring its national or regional headquarters from within or outside the State of Mississippi. The headquarters credit is available to any company regardless of the business in which it engages except for businesses engaged in the transportation, handling, storage, processing or disposal of hazardous waste.

Research and Development Jobs Skills Credit. A $500 credit is authorized for each full-time employee in any new job requiring research and development skills. Specific examples of jobs requiring research and development skills are chemists and engineers. Qualification of other jobs for this credit would require as a minimum a bachelors degree in a scientific or technical field of study from an accredited four (4) year college or university, employment in the area of expertise and compensation at a professional level. The research and development job credit is available to any company regardless of the business in which it engages.

A business interested in qualifying for the research and development jobs tax credit should request approval in writing and provide the following information for each individual research and development position: (1) Title, (2) Purpose, (3) Education requirements, (4) Experience requirements, (5) Hours worked per week, (6) Salary or compensation and (7) Expected hire date. The applicant will be notified on approval of the application for credit.

2000 OKLAHOMA INCOME TAX FORMS AND INSTRUCTIONS FOR PARTNERSHIPS

Packet contains:

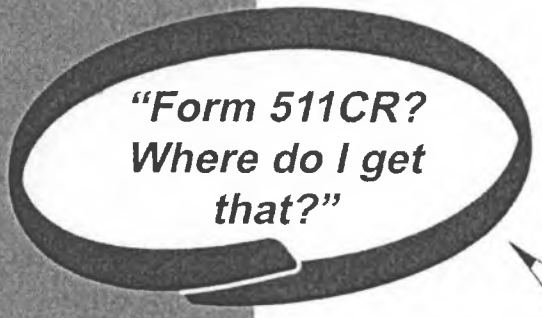
- Instructions for completing the Form 514
- Two 514 partnership income tax forms
- One return envelope

Filing date:

- Your Oklahoma return is due the same date as your Federal return.

Need assistance or have a tax question?

- Phone, fax, e-mail, web or in-person, there are many ways to reach us! Check out page 7 for all the options!



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Adjustments by the IRS...

Taxpayers who file "consents" extending the time for making of Federal adjustments, automatically extend the time for making State adjustments. Also, the taxpayer is required to furnish copies of all Revenue Agents' reports.

Amended Returns...

Use Form 514 for all amended returns. Place an "X" in the space provided, in the upper right hand corner of the form, next to the form number (514X). Enclose the Federal amended Form 1065 when applicable.

Allocable Income or Loss...

Part One, Column A and Part Four, Column A is to be completed by all partnerships.

Part One, Column B is to be completed by partnerships deriving all of their income from within Oklahoma and by partnerships whose business is oil and gas production, mining, farming, or rental within and without Oklahoma, on a direct accounting basis.

Apportionment Income or Loss...

Part Two is to be completed by partnerships conducting a business of a unitary nature. A unitary business is one whose income is derived from the conduct, in more than one state, of a single business enterprise (commonly called unitary business) all the factors of which are essential to the realization of an ultimate gain derived from the enterprise as a whole, and not from its component parts which are too closely connected and necessary to each other to justify division or separate allocation. Partnerships consisting of business other than oil and gas production, mining, farming or rentals operating in more than one state should compute their Oklahoma income by using the three factor formula consisting of Sales, Payroll and Property. (Section 2358 (A) (4) and Section 2358 (A) (5) of the Oklahoma Statutes Title 68). When a partnership has capital gains (or other allocable items such as depletion) a separate schedule must be furnished showing the Oklahoma portion and the total amount claimed on the Federal Return.

Oklahoma Depletion in Lieu of Federal Depletion...

Oklahoma depletion on oil and gas well production, at the option of the taxpayer, may be computed at 22% of gross income derived from each Oklahoma property during the taxable year, but limited to 50% of the net income (computed without the allowance for depletion) from each property. Any depletion deduction allowable is the amount so computed minus Federal depletion claimed. If Oklahoma options are exercised, the Federal depletion not used due to 65% limit may not be carried over. Lease bonus received is considered income subject to depletion. If depletion is claimed on a lease bonus and no income is received as a result of non-producing properties, upon expiration of the lease, such depletion must be restored. A complete schedule by property must be furnished.

Agricultural Commodity Processing Facility Exclusion...

Owners of agricultural commodity processing facilities may exclude 15% of their investment in a new or expanded agricultural commodity processing facility located within Oklahoma. Agricultural commodity processing facility means building, structures, fixtures and improvements used or operated primarily for the processing or production of agricultural commodities to marketable products. The investment is deemed made when the property is placed in service.

Attach a separate schedule showing the type of investment(s), the date placed in service, the cost, the total exclusion and the exclusion available for each partner. Do not include this exclusion in the Oklahoma distributive income, each partner shall report their allowable share of the exclusion on the designated line of their individual return.

(continued on page 4)

Don't Forget to Sign the Return!

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» Coal
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» Fuels
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» Tax Professionals

- Career Opportunities
- Frequently Asked Questions
- Miscellaneous Tax Forms and Publications

600 E. Boulevard Ave.
Bismarck, ND 58505-0599

701.328.7088 phone

Corporation Income

Every corporation engaged in business in North Dakota or having sources of income in North Dakota must file a North Dakota corporation income tax return. The return is due on the 15th day of the fourth month following the close of the tax year. Returns of tax-exempt organizations reporting unrelated business taxable income are due on the 15th day of the fifth month after the close of the tax year. Returns filed by cooperatives are due on the 15th day of the ninth month following the close of the tax year.

Tax rates: The current tax rates for corporations, which apply to tax years beginning on or after January 1, 2011, are shown below:

If taxable income is:			
Over	But not over	**The tax is:**	
$ 0	$ 25,000	1.68%	of North Dakota Taxable Income
25,000	50,000	$ 420.00	+ 4.23% of amount over $25,000
50,000		1,477.50	+ 5.15% of amount over $50,000

If a corporation elects to use the water's edge method to apportion its income, the corporation will be subject to an additional 3.5% surtax on its North Dakota taxable income.

Prior years' tax rates: For the tax rates that apply to corporations for tax years prior to 2011, see **Corporation Income Tax Rates** - (33kb pdf)

IN THE SUPREME COURT FOR THE STATE OF ALASKA

ATLANTIC RICHFIELD COMPANY; ARCO PIPE LINE COMPANY; BP ALASKA, INC.; EXXON CORPORATION; EXXON PIPELINE COMPANY; SOHIO ALASKA PETROLEUM COMPANY; and SOHIO PIPE LINE COMPANY,	)	
Appellants,	)	
vs.	)	
STATE OF ALASKA; ALASKA DEPARTMENT OF REVENUE; ALASKA DEPARTMENT OF ADMINISTRATION; COMMISSIONER OF REVENUE ROBERT D. HEATH, and COMMISSIONER OF ADMINISTRATION LISA RUDD,	)	Supreme Court No. S-52
Appellees.	)	Superior Court Nos. 3AN-79-1903 Civil 3AN-80-1542 Civil

APPENDIX A OF BRIEF OF APPELLEES

11. The estimated interest that would be payable on a refund of the difference between AS 43.21 and AS 43.20 tax liabilities:

YEAR	INTEREST ON ESTIMATED REFUND*
1978	$ 40,000,000
1979	89,000,000
1980	138,000,000
1981	159,000,000
TOTAL	$426,000,000

*Interest through 4/27/84

12. The estimated total refund liability of the State is:

YEAR	ESTIMATED TOTAL REFUND LIABILITY
1978	$ 122,000,000
1979	311,000,000
1980	570,000,000
1981	821,000,000
TOTAL	$1,824,000,000

Further your affiant saith naught.

Robert D. Heath, Commissioner
Department of Revenue

SUBSCRIBED AND SWORN TO before me this 27th day of April, 1984.

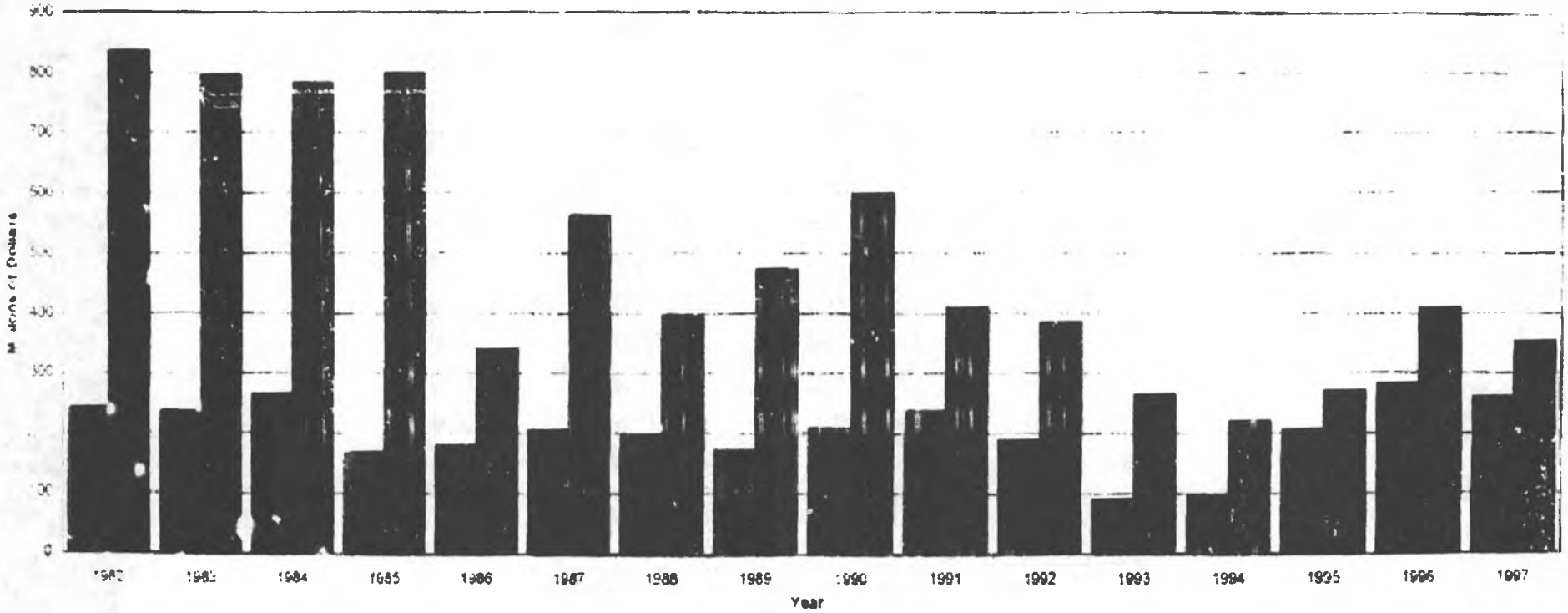
Notary Public, State of Alaska
My commission expires: 12/19/84

Comparison of Actual Oil and Gas Corporate Income Tax Collected with Estimated Revenues using a Separate Accounting Income Tax Approach (In Millions)

	Actual O&G Income Tax Collected	Estimated Separate Accounting Revenues	Difference
1982	242.50	837.62	595.12
1983	236.00	796.15	560.15
1984	265.10	782.86	517.76
1985	163.60	797.00	628.40
1986	181.00	341.00	160.00
1987	205.00	562.00	357.00
1988	198.00	396.00	198.00
1989	174.00	473.00	299.00
1990	208.00	598.00	390.00
1991	237.00	410.00	173.00
1992	189.00	385.00	196.00
1993	90.00	264.00	174 00
1994	98.00	219.00	121.00
1995	206.00	270.00	64.00
1996	281.00	408.00	127.00
1997	259.00	355.00	96.00
TOTALS	**$3,238.20**	**$7,894.63**	**$4,656.43**

Source: 1986-97 calender year data from DOR letter D. Dickinson to J. Donohue Sept. 23, 1999; 1982-85 fiscal data is from DOR report dated Oct. 31, 1985, Wright to Nordale, In re HB363; data for second half of 1985 not available at this time.

Comparison of Actual Oil and Gas Corporate Income Tax Collected with Estimated Revenues using a Separate Accounting Income Tax Approach Assuming Existing AS 43.20 Rate



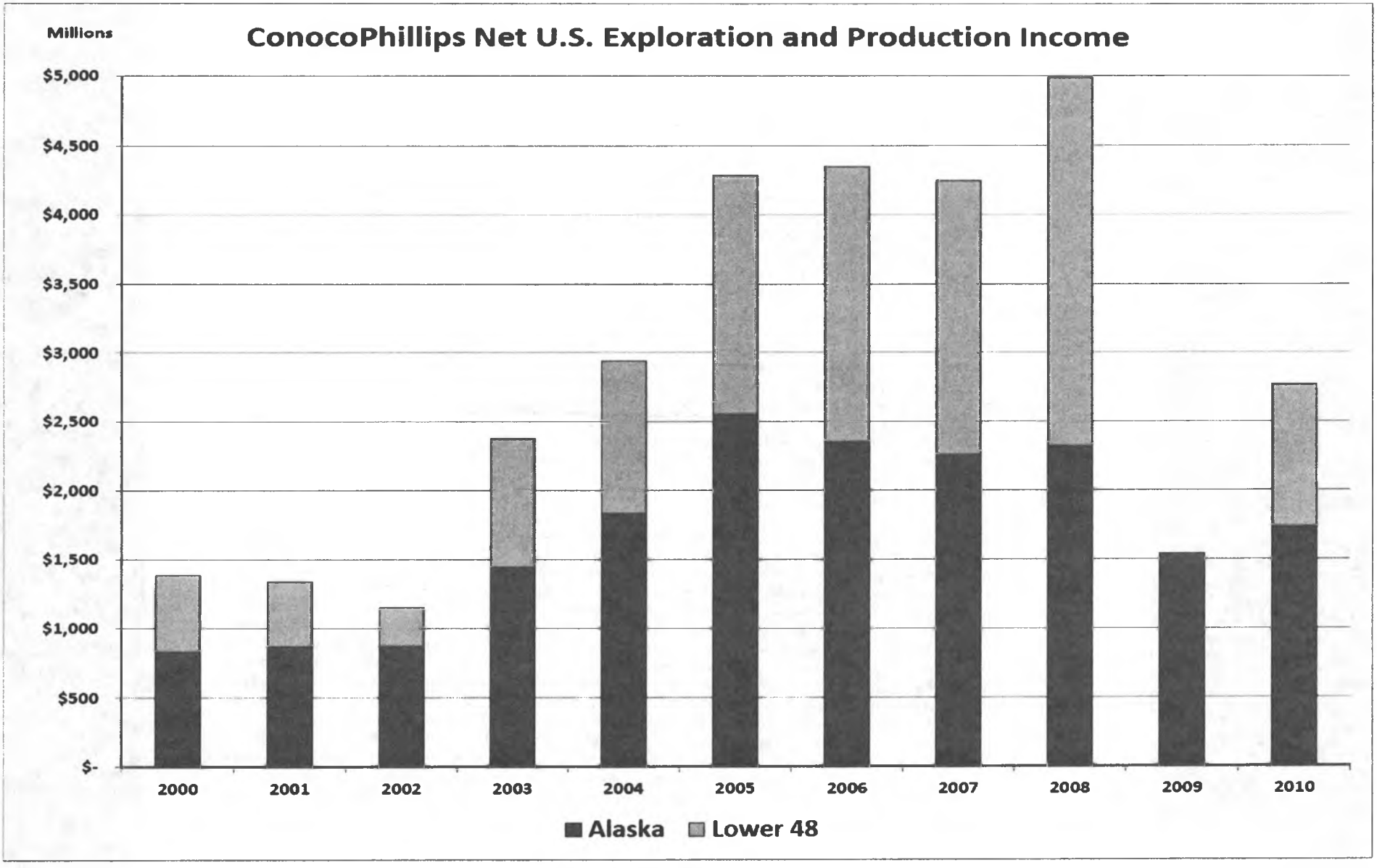
Source: 1986-97 calendar year data from DOR letter, D. Dickinson to J. Donohue, 9/23/99, 1982-85 fiscal data is from DOR report dated 10/31/85, Wright to Nordale, in re HB353. Data for second half of 1985 not available at this time. Since the actual income tax collections for FY82 (the phase out year) included revenue from both separate accounting and modified apportionment, the actual income tax collections for FY82 depicted on the chart includes an estimate of revenue from modified apportionment as if it had been in effect for the entire fiscal year.

Analysis

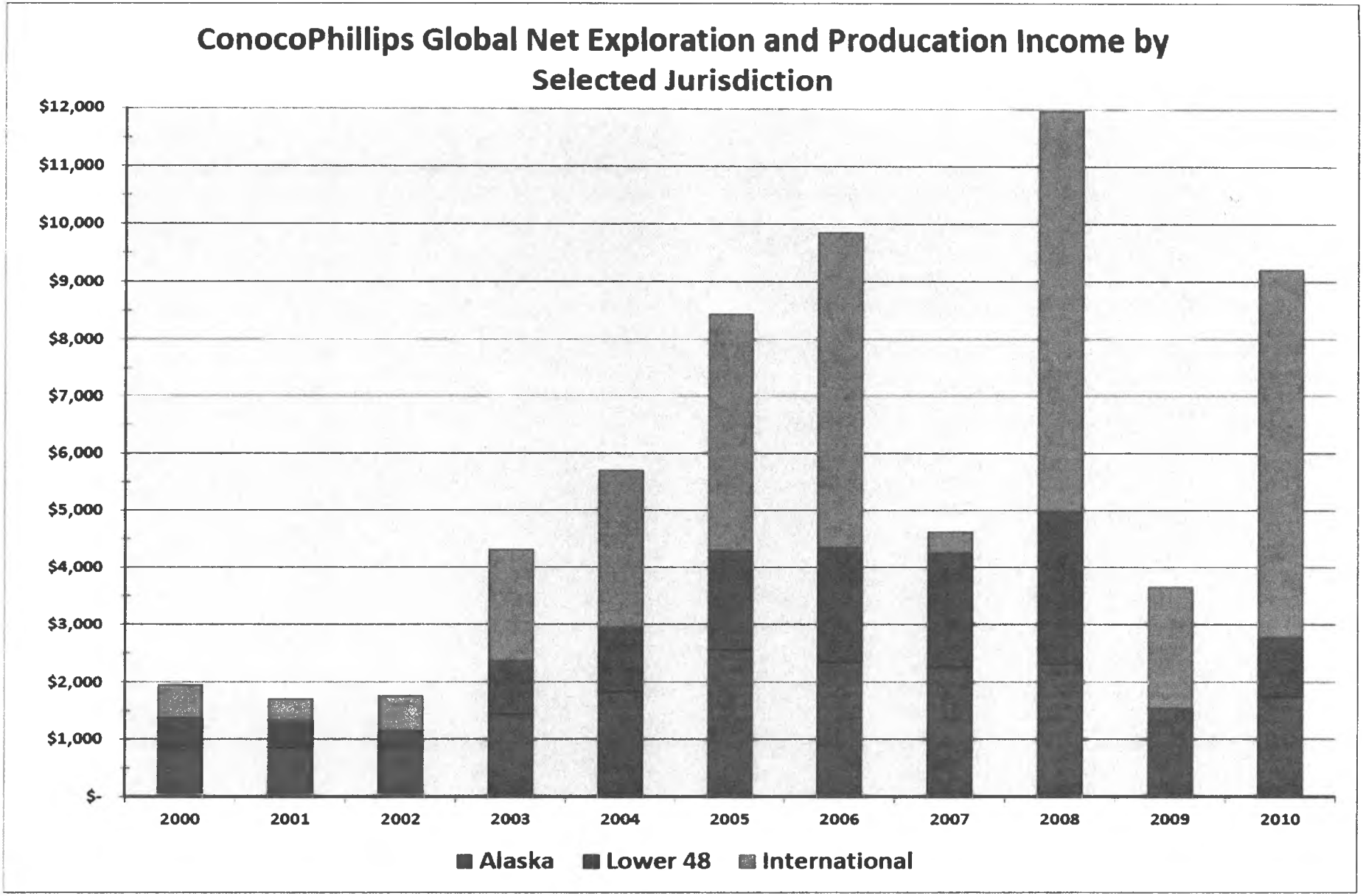
Bill Language:
This bill would repeal the current corporate income tax on oil and gas corporations under AS 43.20.072 (worldwide combination and apportionment) and replace it with a corporate income tax based on separate accounting. Current oil and gas corporate income tax is based on a formula where total worldwide income of a corporation's unitary group is apportioned to Alaska based on the amount of property, extraction and sales attributable to Alaska. This bill would require Alaska oil and gas corporations to calculate income tax for their oil and gas producing and transportation companies based on income earned solely in Alaska. If oil and gas companies are also engaged in activities other than oil and gas production and transportation, this bill would require those companies to calculate and pay tax on those other activities based on worldwide combination and apportionment. This bill would require oil and gas corporations to file a return by April 15 each year providing information the department needs to calculate each corporation's taxable income and income tax. This bill requires the department to calculate each corporation's income tax and send an assessment by August 15 each year to each company subject to the tax. Corporations must then pay the amount of tax as calculated by the department by September 30 of each year. This bill also requires the department to prepare a report each year showing the aggregate amount of income and deductions by category reported by all oil and gas corporate income tax taxpayers. The department would also be required to disclose specific information about a taxpayer if the taxpayer is a publicly traded company and if the information was included in a report filed with the US Securities Exchange Commission (SEC) and the SEC publicly disclosed the information.

Revenues:
The department does not have enough information to accurately and fully estimate the change in oil and gas corporate income tax as a result of this legislation. Preliminary estimates show that under separate accounting, oil and gas corporations would have paid approximately $250 million more during each of the last 5 fiscal years in corporate income tax if this legislation had been in effect. This bill has an effective date of January 1, 2013. Oil and gas corporations would report under the new method beginning in April 2014 and tax would not be due until September 30, 2014. Therefore, we do not expect to see a change in corporate income tax as a result of this legislation until FY 2015.

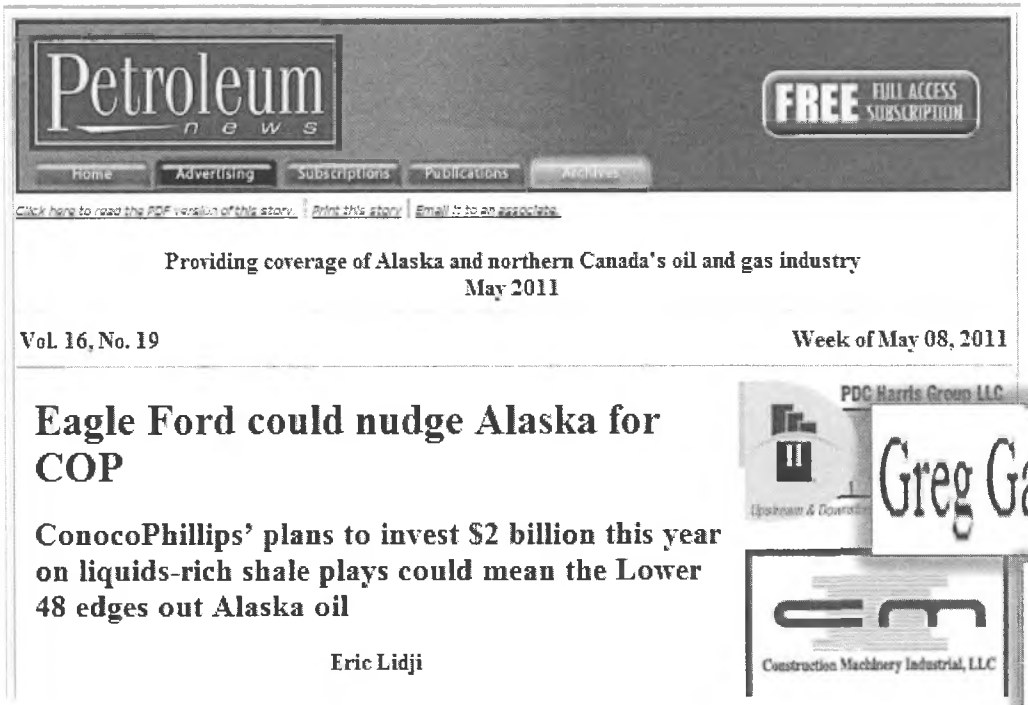
Expenditures:
As stated above, this bill would require the Department of Revenue to calculate the amount of tax due by each oil and gas corporation operating in the state based on information each company provided the department. The department would have approximately 4 months to make the calculation of corporate income tax and send assessments to each taxpayer. In addition, the department would be required under this legislation to prepare a report showing aggregate information of all taxpayers and specific information of publicly traded companies. Under the current oil and gas corporate income tax, the calculation of taxable income starts with federal taxable income and then is adjusted for certain Alaska modifications. Currently, the department relies on federal corporate income tax audits as an additional audit resource. As such, the department does not audit down to the invoice level. The calculation of taxable income under separate accounting does not start with federal taxable income and, as such, the department will not be able to rely on federal audits to ensure that taxpayers are properly reporting and must conduct full scale audits including auditing down to the invoice level. There are currently 26 oil and gas corporate income tax filers. The department will have to calculate each taxpayers tax liability each year and conduct more comprehensive audits as well as provide a report each year to the legislature. The department believes it will need four additional corporate income tax auditor III's to handle the increased work as a result of this legislation. In addition, the department will need increased travel funds of approximately $25,000 each year to spend enough time at a corporation's place of business to conduct in depth audits.



Legislative Research Services Report 12.198, Figure 1, February 2012



Legislative Research Services Report 12.198, Figure 3, February 2012



Petroleum news

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Providing coverage of Alaska and northern Canada's oil and gas industry
May 2011

Vol. 16, No. 19 Week of May 08, 2011

Eagle Ford could nudge Alaska for COP

ConocoPhillips' plans to invest $2 billion this year on liquids-rich shale plays could mean the Lower 48 edges out Alaska oil

Eric Lidji

PDC Harris Group LLC

Upstream & Downstream

Construction Machinery Industrial, LLC

Greg Garland, senior vice president for exploration and production in the Americas

ConocoPhillips likes the Eagle Ford because of economics.

Garland said the play offered $45 per barrel margins last year, twice the average of ConocoPhillips' global portfolio. Since January 2010, well costs have fallen 40 percent.

Alaska Oil Economics

- Spring 2011 approximate price of oil: $118/bl
- Transportation $6
- Royalty = $112 x 12.5% = $14
- Upstream Costs: $20/bl
- Production Tax Value: $78/bl
  - Production tax rate is base 25% +.4%/$ progressivity = 44.2%

44.2% x $78 = prod tax of $34.5/bl leaving

Typical Company → Alaska Margin: $43.50/bl

- **At $110/bl, margin would be $41.60**
- **At $100/bl, margin would be $38.66**

Alaska margins are nearly <u>double</u> CP worldwide average margin