Leg. Finance

1483

NOTES TO TABLE 9

We estimated the Alaska state income tax liability for Sadlerochit oil production by forecasting each category of deductions and subtracting their total from gross returns. All oil price and production assumptions remain unchanged.

(1) State royalty share equals 12.5% of gross returns less cleaning charges. (Col. 1) = (Col. 4, Table 5).

(2) Production and conservation taxes were calculated separately. Production taxes equal Col. 7, Table 5. Conservation taxes equal one-eighth cent per barrel for each non-royalty barrel produced.

(3) Ad valorum property taxes from Col. 4, Table 6.

(4) Total operating costs from Col. 8, Table 3.

(5) Depreciation of development costs on a unit of production basis includes amortization of capitalized interest. We first calculated unit of production factors which measure the annual volume of oil produced as a percent of remaining recoverable oil. Assumptions regarding production and initial total volumes are from Col. 1, Table 1. The factors, which range from .062 in FY 80 to .092 in FY 85 depreciate the unamortized base. We began with a Department of Revenue estimate of the unamortized base as of January 1, 1980, of $3121. million. From this we calculated the beginning of FY 1981 base by depreciating the 1980 base one half year and adding one half the estimated 1980 investment of $586. million. The resulting beginning fiscal year 1981 unamortized base was $3317.25 million. Thereafter, for each succeeding fiscal year we depreciated the prior years base and added to the base that year's projected capital outlay, Col. 5, Table 4.

(6) Acquisition costs include estimates of amortization of lease acquisition payments and property taxes paid prior to production. The fiscal year 1981 estimates were provided by the Department of Revenue. This amount was assumed to increase at an annual rate of 15% per year throughout the period.

(7) This column contains estimates of interest expense not capitalized. The fiscal year 1981 estimate was calculated by the Department of Revenue. Following years were assumed to increase at the rate of 10.5% per year.

(8) Exploration costs include the costs of unsuccessful exploration for oil and gas, abandonment, and dry hole costs. The fiscal year 1981 estimate was from Department of Revenue data. Following years were assumed to increase at the rate of 15% per year.

(9) Administrative costs were calculated in FY 1981 at 12¢ per barrel, the ceiling price provided in AS 43.21.020(9)(B). This amount was assumed to increase at 9% per year.

NOTES TO TABLE 9 CONT'D.

(10) Total Deductions, (Col. 10) = sum of (Col. 1). . . to (Col. 9).

(11) (Col. 11) = (Col. 2, Table 5).

(12) Total taxable = (Col. 12) = (Col. 11) - (Col. 10).

(13) Total tax liability equals 9.4 percent of Col. 12. These estimated tax liabilities have not been adjusted for reporting and payment lags. To compare these estimates to actual state receipts or other state revenue forecasts, see our adjusted data in Table 16.

TABLE 10

KUPARUK RESERVOIR

PRODUCTION, ROYALTY, AND TAX ESTIMATES
(IN MILLIONS OF DOLLARS EXCEPT AS NOTED)

Fiscal Year	(1) AVERAGE WELLHEAD PRICE ($/B)	(2) OIL PRODUCTION (MMB/Day)	(3) GROSS REVENUE	(4) STATE ROYALTY	(5) PRODUCTION TAX
1981	19.76	-	-	-	-
82	26.31	.020	192.06	24.01	18.55
83	30.58	.100	1116.17	139.52	104.30
84	33.79	.125	1541.67	192.71	139.27
85	37.33	.125	1703.18	212.90	153.00

Fiscal Year	(6) AD VALORUM PROPERTY TAX	(7) DEPRECIATION COSTS	(8) OPERATING & MISC. EXP.	(9) TOTAL TAXABLE INCOME	(10) INCOME TAX LIABILITY
1981	17.15	-	-	-	-
82	21.47	16.11	7.2	104.62	9.83
83	24.87	84.06	30.50	726.92	68.33
84	29.05	105.08	45.63	1029.93	96.81
85	30.16	105.08	45.63	1156.41	108.70

NOTES TO TABLE 10

To estimate impact of Kuparuk oil development on state revenues, a preliminary projection was made of Kuparuk production volumes, royalty, and tax revenues.

(1) Wellhead prices assumed the same as for Sadlerochit oil. This treats the pipeline to TAPs as a large gathering line. It also assumes no significant market price difference between Kuparuk and Sadlerochit oil.

(2) Oil production is assumed to commence April, 1982, at an average daily rate of 80,000 bbls. and increase to 125,000 B/day by FY 1984. This is still significantly less than the planned 195,000 B/day capacity of the pipeline to TAPs Pump Station One.

(3) (Col. 3) = (Col. 1) * (Col. 2).

(4) State royalty oil was calculated as 12.5% of Gross Revenue, disregarding cleaning charges. (Col. 4) = (Col. 3) * .125%.

(5) Production tax estimates assume the same per well production rates, hence economic limit factors, as Sadlerochit oil. (Col. 5) = [(Col. 3) - (Col. 4)] * .1225 * (Col. 6, Table 5).

(6) Property tax valuations are based on estimates provided by the Department of Revenue of Phase 1 annual capital investment, including $60 million for the pipeline. Added are estimates of $100 million in FY 82 and FY 83 for the initiation of Phase 2 development.

(7) Depreciation costs assume unit of production depreciation of total development costs. Depreciation factors are calculated on the basis of 600 million barrels oil recovery. Total capital costs are assumed to be 10% greater than tangible costs and equal $943.37 (million) in FY 80, $193.60 in FY 81, $134.20 in FY 82, and $110.02 in FY 83. These amounts are combined to form a depreciation value in the same manner as Sadlerochit unit of production depreciation accounting. See note 5, Table 9.

(8) Operating costs and all other deductions are assumed for this analysis to total $1.00 per barrel of oil produced. (Col. 8) = (Col. 2) * 365 * $1.00.

(9) Total taxable income equals gross revenue less all deductions. (Col. 9) = (Col. 3) * (Col. 5) - (Col. 6) - (Col. 7) - (Col. 8).

(10) (Col. 10) = (Col. 9) * .094. These estimates must be lagged one quarter to be on the same payment basis as state revenues. See Table 16.

TABLE 11

TRANS ALASKA PIPELINE
INCOME TAX ESTIMATES
(IN MILLIONS OF DOLLARS EXCEPT AS NOTED)

Fiscal Year	(1) PIPELINE THRUPUT (Millions B/day)	(2) TARIFF ($/B)	(3) TOTAL REVENUE	(4) OPERATING COSTS	(5) DEPRECIATION EXPENSE
1981	1.500	6.21	3399.98	350.18	348.15
1982	1.502	6.21	3404.51	382.22	348.15
1983	1.600	5.46	3188.64	443.78	352.15
1984	1.625	4.71	2791.62	491.28	352.15
1985	1.625	4.71	2793.62	535.53	352.15

Fiscal Year	(6) UNCAP INTEREST	(7) PROPERTY TAX	(8) NET INCOME	(9) TAX LIABILITY
1981	543.57	167.0	1991.08	187.16
1982	459.94	174.8	2039.40	191.70
1983	376.32	184.8	1831.59	172.17
1984	292.69	192.6	1464.90	137.70
1985	209.07	200.4	1496.47	140.67

NOTES TO TABLE 11

(1) Oil thruput volumes combine Sadlerochit production estimates (Col. 1, Table 1) with Kuparuk production estimates (Col. 2, Table 10).

(2) TAPs tariff estimates assume current tariff rates till January 1, 1983 at which point a $1.50 reduction takes place.

(3) Total revenue equals annual thruput times the effecitve tariff. (Col. 3) = (Col. 1) * 365 * (Col. 2).

(4) Operating cost estimates include maintenance charges and are based on 1979 actual amounts of $306.6 million. This amount, equaling 56¢ a barrel at 1.5 million B/day is adjusted for increases in thruput and is inflated at 9% per year.

(5) Depreciation expense assumes a $9.4 billion base depreciated straight line for 27 years, with an additional $100 million for expanded pump capacity in the base, beginning in FY 1983.

(6) Uncapitalized interest was estimated by the Department of Revenue.

(7) An estimated property tax valuation base of $8.35 billion on January 1, 1981, was adjusted for inflation (9%) and depreciated over a remaining assumed useful life of 25 years.

(8) (Col. 8) = (Col. 3) - (Col. 4) - (Col. 5) - (Col. 6) - (Col. 7).

(9) (Col. 9) = (Col. 8) * .094.

TABLE 12

COOK INLET OIL AND GAS
PRODUCTION, ROYALTY AND TAX ESTIMATES
(IN MILLIONS OF DOLLARS EXCEPT AS NOTED)

Fiscal Year	(1) WELLHEAD OIL PRICE ($/B)	(2) OIL PRODUCTION (MMB/Day)	(3) GAS PRICE ($/M)	(4) GAS PRODUCTION (M/day)	(5) GROSS REVENUE	(6) STATE ROYALTY
1981	13.59	.0878	.33	491627	494.74	60.39
1982	36.74	.0753	.39	546958	1088.01	113.78
1983	40.60	.0666	.45	554883	1078.08	129.10
1984	44.86	.0605	.50	553373	1091.61	131.82
1985	49.57	.0516	.55	553373	1044.69	125.28

Fiscal Year	(7) PRODUCTION TAX	(8) OPERATING EXPENSES	(9) OTHER DEDUCTIONS	(10) PROPERTY TAX	(11) TAXABLE INCOME	(12) TAX LIABILITY
1981	26.76	88.70	60.00	11.22	247.67	23.28
1982	43.44	89.00	50.00	12.62	779.17	73.24
1983	46.11	89.00	48.00	13.63	752.24	70.71
1984	46.13	89.00	48.00	14.77	761.89	71.62
1985	38.21	89.00	45.00	15.37	731.83	68.79

NOTES TO TABLE 12

(1) Wellhead oil prices are posted field prices for Cook Inlet oil. Forecast assumes the current field price of $33.25 increases by 10.5 percent per year. Low average fiscal year 1981 price due to oil price controls in effect for part of that year.

(2) Oil production forecast by Petroleum Revenue Division, Department of Revenue.

(3) Gas prices were estimated by the Petroleum Revenue Division on the basis of reported gas contract prices.

(4) Gas production was also estimated by Petroleum Revenue Division.

(5) Gross revenue includes both oil and gas (Col. 5) = [(Col. 1) * (Col. 2) * 365] + [(Col. 3) * (Col. 4) * 365].

(6) & (7) State royalty and production taxes from oil and gas were projected using the Petroleum Revenue Division's Cook Inlet Forecast Model.

(8) FY 1981 operating expense estimate was prepared by the Department of Revenue. Following years were assumed constant.

(9) Generalized estimate of all other Cook Inlet deductions prepared by Department of Revenue.

(10) Property tax estimates are based on the January 1, 1981, appraisal and a capital expenditure forecast provided by property tax section of the Petroleum Revenue Division.

(11) (Col. 11) = (Col. 5) - (Cols. 6-10).

(12) (Col. 12) = (Col. 11) * .094.

TABLE 13

SUMMARY OF ESTIMATES FOR EXISTING
TAXES FROM TABLES 1-12
(MILLIONS OF DOLLARS)

		Sadlerochit	Kuparuk	Cook Inlet	TAPs
Source		Col. 13, Table 9	Col. 10, Table 10	Col. 12, Table 12	Col. 9, Table 11
	FY				
Income	81	698.78		23.28	187.16
Tax	82	944.70	9.83	73.24	191.70
AS 43.21*	83	1091.76	68.33	70.71	178.17
	84	1191.76	96.81	71.62	137.70
	85	1295.60	108.70	68.79	140.67
Source		Col. 7, Table 5	Col. 5, Table 10	Col. 7, Table 12	
	FY				
Produc-	81	1108.44	-	26.76	-
tion Tax	82	1396.40	18.55	43.44	-
AS 43.55	83	1570.48	104.30	46.11	-
	84	1676.96	139.27	46.13	-
	85	1842.17	153.00	38.21	-
Source		Col. 4, Table 6	Col. 6, Table 10	Col. 10, Table 12	Col. 7, Table 11
	FY				
Hardware	81	75.17	17.15	11.22	167.00
Property	82	105.99	21.47	12.62	174.80
Tax	83	151.34	24.87	13.63	184.80
AS 43.56	84	202.85	29.05	14.77	192.60
	85	245.60	30.16	15.37	200.40

*Note: Income tax data given here in on an accrual basis. For adjusted data, see Table 16.

TABLE 14

SADLEROCHIT RESERVES VALUATION
(BILLIONS OF DOLLARS)

Discount Rates	July 1, 1981 (FY 82)	July 1, 1982 (FY 83)	July 1, 1983 (FY 84)	July 1, 1984 (FY 85)	July 1, 1985 (FY 86)	REFERENCE
13%	95.627	102.396	109.005	114.753	119.749	-
15%	82.186	88.800	95.350	101.166	106.332	-
19%	63.025	69.188	75.456	81.150	86.386	Col. 9, Table 8
Sadlerochit Property Valuation as of Jan. 1, same calendar year (Prior FY)	3.758	5.299	7.567	10.143	12.280	Col. 3, Table 6
	Reserves net of hardware property					
13%	91.869	97.097	101.438	104.610	107.469	
15%	78.428	83.501	87.793	91.023	94.052	
19%	59.267	63.889	67.889	71.007	74.106	

TABLE 15

COOK INLET & KUPARUK
RESERVES VALUATION
(BILLIONS OF DOLLARS)

Discount Rates	July 1, 1981 (FY 82)	July 1, 1982 (FY 83)	July 1, 1983 (FY 84)	July 1, 1984 (FY 85)	July 1, 1985 (FY 86)
Cook Inlet	Pritchard & Abbott Estimates				
13%	1.294				
15%	1.228	1.085	.861	.716	.583
19%	.94*	.85*	.68*	.57*	.47*
Discount Rates Kuparuk	Pritchard & Abbott Estimates				
13%	4.32**	5.54	6.01	6.38	6.73
15%	3.70**	4.92	5.44	5.83	6.23
19%	2.74**	3.94	4.50	4.92	5.39

* These values were estimated by multiplying the Cook Inlet valuations in year $\pm$ at 15 percent discount by the following factor (Sadlerochit 19% valuation in year +/Sadlerochit 15% valuation in year +).

** Not in production.

Note: Since the above valuations assumed a deduction for the reserves tax payments equal to 8% of producer's gross, the valuation values are lower than they would be if calculated on a basis consistent with the Sadlerochit valuation. Therefore to compensate for this different valuation approach no deductions are made for hardware tax valuations.

TABLE 16

SUMMARY OF INCOME TAX ESTIMATES
AS ACCRUED AND COLLECTED
(MILLIONS OF DOLLARS)

	FY 1981	FY 1982	FY 1983	FY 1984	FY 1985	REFERENCE
Sadlerochit 43:21 unadjusted	698.78	944.70	1091.46	1191.76	1295.60	Col. 13, Table 9
Cook Inlet 43:21 unadjusted	23.28	73.24	70.71	71.62	68.79	Col. 12, Table 12
Kuparak 43:21 unadjusted	-	9.83	68.33	96.81	108.70	Col. 10, Table 10
TAPs 43:21 unadjusted	187.16	191.10	172.17	137.70	140.67	Col. 9, Table 11
Total 43:21 unadjusted	909.22	1219.47	1402.67	1497.89	1613.76	
Total 43:21 adjusted	767.80	1141.91	1356.87	1474.09	1584.79	

Note: For FY 81 the collection adjustment was made by multiplying the actual collections made during the first three quarters of the fiscal year by 4/3. FY 82-FY 85 were adjusted by dropping 1/4 of the amount and replacing it with 1/4 of the prior year's accrual.

TABLE 17

WINDFALL PROFITS TAX DEDUCTIONS
(MILLIONS OF DOLLARS)

	FY 1981	FY 1982	FY 1983	FY 1984	FY 1985	REFERENCE
43:21 Sadlerochit unadjusted	698.78	944.70	1091.46	1191.76	1295.60	Col. 13, Table 9
WPT Deduction value (9.4% X WPT Liability)	169.86	319.77	392.79	412.04	467.52	Col. 9, Table 7
Saddlerochit net 43:21 unadjusted	528.92	624.93	698.67	779.72	828.08	
Cook Inlet 43:21	23.28	73.24	70.71	71.62	68.79	Col. 12, Table 1
WPT Deduction value (9.4% X WPT Liability)	6.36	31.40	33.95	34.38	32.95	footnote (3)
Cook Inlet net 43:21 unadjusted	16.92	41.84	36.76	37.24	35.84	
TAPs 43:21 unadjusted	187.16	191.70	172.17	137.70	140.67	Col. 9, Table 11
Kuparuk 43:21 unadjusted	-	9.83	68.33	96.81	108.70	Col. 10, Table 10
Total Net 43:21 with WPT deduction unadjusted	733.00	868.30	975.93	1051.47	1113.29	
Total Net 43:21 with WPT deduct. adjusted	616.68 1/	834.48 2/	940.02	1032.59	1097.84	
Total Net 43:21 adjusted	767.80	1141.91	1356.87	1474.09	1584.79	From Table 16
Value of WPT adjusted	151.12	307.43	407.85	441.50	486.95	

1/ Values lagged one quarter. 2/ Includes $18.95 from last quarter, FY 80.

3/ Cook Inlet Windfall Tax estimated separately.

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May 20, 1981

Honorable Tom Williams, Commissioner
Department of Revenue
State of Alaska
Pouch 5
Juneau, Alaska 99811

Dear Commissioner Williams:

In recent weeks our firm has had extensive discussions with employees and consultants of your department regarding work on your legislative proposal to enact an oil and gas reserves property tax. Our firm was asked to give our views on valuation planning estimates made as a part of that work. We were not asked to make our own independent valuation estimate nor to verify whether we would have used the same approach and assumptions and obtained the same results.

Specifically we were asked to review the valuation planning estimates and advise as to whether (1.) the valuation estimating approach taken was valid; (2.) the assumptions used in making the valuation estimates were reasonable; and (3.) the results obtained were consistent with, and followed correctly from, the approach taken and the assumptions used.

We have concluded that the approach was valid, that the assumptions are within a range of reasonableness and that the results were consistent with and correctly followed from the application of the approach and assumptions.

First, with respect to the approach used in making the valuation estimates, we are satisfied that the methodology and procedures used are proper and commonly used in the industry. As we discussed with your employees and consultants, the valuation approach should include a deduction for any net reserves property tax that would be paid after the application of an income tax credit.

Second, we have reviewed the assumptions used in making the valuation estimates and think they are reasonable. This is not to say that these are the only assumptions that could be made or that they are the ones we ourselves would make. As you know, property valuation is not an exact science and property appraisers do reasonably differ on valuation assumptions.

However, such differing assumptions by appraisers fall within a range of reasonableness and in our view the assumptions which we reviewed fall within that range. Reasonable differences of opinion are particularly significant with regard to a few key assumptions, such as the appropriate discount rate and the rate of oil price inflation. For example, the recent softening of world oil prices has led experts to differ on their opinions about the long term outlook on oil price. The price inflation assumption that was used is not unreasonable and is within the range of divergent expert opinions.

Third, we have reviewed the results obtained and find that they are consistant with and correctly follow from the approach taken and the assumptions used.

We have appreciated the opportunity to help in this effort and believe that it will be helpful for making judgments on the legistative proposal. As you know, however, this work is not a substitute for the actual valuation process itself necessary to support a property tax assessment. That will require additional study and research and will be based upon factors as they exist at the time of assessment.

Very truly yours,

PRITCHARD & ABBOTT

Gerald McNeill

Gerald McNeill, P.E.

cc: John Messenger
Gerald Beier
Lawrence C. Eppenbach

A SOUND STRATEGY FOR PROTECTING ALASKA'S OIL AND GAS REVENUES:

An Analysis of the Backstop Tax Legislation

prepared for

The Alaska State Legislature
Joint Gas Pipeline Committee

By

PRESTON, THORGRIMSON, ELLIS & HOLMAN

May 27, 1981

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May 27, 1981

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May 27, 1981

The Honorable Terry Gardiner
The Honorable Jalmar M. Kerttula
Co-Chairmen
Joint Gas Pipeline Committee
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Dear Senator Kerttula and Representative Gardiner:

I am pleased to transmit to you our report to the Joint Gas Pipeline Committee entitled "A Sound Strategy for Protecting Alaska's Oil and Gas Revenues: An Analysis of the Backstop Tax Legislation."

I trust that this report will be useful to the Committee in its consideration of tax legislation now before the Committee. We have appreciated the opportunity to work for the Committee on this subject of vital importance to the State.

Sincerely,

PRESTON, THORGRIMSON,
ELLIS & HOLMAN

By
John R. Messenger

JRM/mmm
Enclosure

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I. INTRODUCTION

In early April our firm and Gregg Erickson & Associates were asked to review and report on the options available to the legislature for implementing the goals established in the "Joint Statement on Oil Taxes" issued on March 18, 1981, by the Governor, the President of the Senate, the Speaker of the House, the Finance Chairmen of the House and Senate and other legislative leaders. The preeminent goal set out in that Joint Statement was a commitment by the Governor and the legislative leadership to find a sound strategy for protecting oil and gas revenues.

Taking this as our charge, we prepared a report to the Joint Gas Pipeline Committee which identified several options available to the legislature. Our report contained a preliminary legal, economic and fiscal analysis of those options, in order to permit an informed choice by the legislature of which options should receive further consideration. Finally, our report contained our recommendation as to which option was most likely to meet the goal of the Joint Statement. In particular, we recommended for further consideration backstop legislation consisting of:

1. a reserves property tax or a combination of a reserves property tax and a severance tax increase; with

2. a credit mechanism which would allow payments made under the oil and gas corporate income tax to be credited against the new tax or taxes.

Although we observed that additional analysis would be required before a final decision could be made, we stated that we were reasonably confident that the option recommended would, after further work, prove to be the one most likely to meet the objective of the Joint Statement and the criteria discussed in our report. We have now completed our additional analysis and we have concluded that the option recommended is indeed the best available strategy for protecting the State's oil and gas revenues.

Since completion of our Report on April 15, 1981, considerable analysis has proceeded on several of the options identified in the Report. There has been extensive discussions of the backstop option with members of the legislature, the Governor, legislative staff, administration officials and other consultants of the legislature and the Department of Revenue. The Department of Revenue has conducted an intensive fiscal and economic analysis of the backstop option. The mutual drafting efforts of the Commissioner of Revenue, committee staff, Legislative Affairs staff, the Attorney General's office and members of our firm have resulted in putting the backstop option in concrete legislative form.

This report will review the analysis which has culminated in the introduction by the Governor of Sponsor Substitute for House Bill No. 200, and explain why we believe that bill meets the goal set forth in the Joint Statement.

II. BACKSTOP CRITERIA

Our April 15 report identified several criteria which should be met by the backstop option in order for it to be a sound strategy for protecting the State's oil and gas revenues. The primary criteria were that the backstop must (1) have sufficient fiscal horsepower to cover the revenues at risk, and (2) be legally secure. In addition, other secondary criteria identified were that the backstop must (1) minimize adverse effects on the current lawsuit, (2) provide administrative convenience, (3) be simple, (4) not overcollect, (5) minimize the likelihood of adverse federal reaction, (6) provide symmetry, (7) have certainty of revenue effect, and (8) minimize spillover effects.

We believe that the backstop option as set out in SSHB 200 meets both the primary and secondary criteria. Our reasons for this conclusion follow:

A. Fiscal Horsepower

After extensive analysis the Department of Revenue has concluded that the imposition of a reserves property tax will generate sufficient revenue to cover fully the revenues currently at risk and those expected to be at risk in the future. The Department has concluded that an annual millage rate of 25 mills will achieve the desired level of revenues. The supporting detail for these conclusions are contained in the fiscal note accompanying SSHB 200 and in the report of Gregg Erickson & Associates to the Department of Revenue.

The reserves property tax estimates made by the department and its consultants were reviewed by the nationally recognized engineering valuation firm of Pritchard & Abbott. In a letter to Commissioner of Revenue, Thomas K. Williams, dated May 20, Pritchard & Abbott concluded after its review of such work that the approach taken was valid, the assumptions used were reasonable, and that the conclusions were consistent with and correctly followed from the approach and assumptions.

B. Legal Security

We have completed our analysis of the potential constitutional challenges that might be raised against the reserves property tax, when it is used as a backstop, and have concluded that the new tax will withstand constitutional challenge and that the reserves property tax as set out in SSHB 200 stands on strong legal footing. The detailed legal analysis of the various constitutional issues is contained in Part IV of this report.

C. Effects On Current Lawsuit

Quite possibly, any change in the State's tax laws could have an effect on the present litigation over A.S. 43.21. A backstop tax could be said to raise questions about the State's confidence in its case and perhaps reduce the urgency of the State's cause. However, the amount of revenue at stake and the disastrous consequences to the State if the State were to lose the litigation require that the State take some action to insure sufficient revenues to

meet its needs even if the State's chances of winning the lawsuit are excellent. Even a small chance of losing is a matter of serious concern because of the financial crisis which would befall the State. These adverse consequences certainly outweigh the intangible effects which tax changes could possibly have on the lawsuit.

D. Administrative Convenience

Although a reserves property tax requires a high degree of technical expertise, it is an easily administered tax. It's administration requires only a minimum number of administrative staff who are supported by retained expertise. As shown in the fiscal note by the Department of Revenue, the new reserves tax can be easily accomodated into the State's existing tax program at minimal cost.

In its 1977 tax study entitled "Alaska's Oil and Gas Tax Structure: A Study with Recommendations for Improvement" the Department of Revenue observed that although the previous reserves property tax proved successful, it contained certain provisions which made its administration more difficult than necessary. One difficulty lay in the fact that the reserves property tax was imposed upon non-producing properties for which there was a lack of economic and engineering information. Another administrative difficulty sprang from the fact that the millage rate was set before the assessment was set. This was felt to put an unwholesome pressure on the assesor to meet budget needs through the assessment valuation.

Both of these difficulties have been removed in SSHB 200. The new reserves property tax is imposed only upon producing properties and the millage rate can be varied after the valuation is determined as it is done in most property taxing jurisdictions.

The previous claims by the oil industry that the imposition of a reserves property tax would result in an administrative nightmare and a huge bureaucracy are not supported either by the experience of other states or by the State's own experience in 1976 and 1977.

E. Simplicity

A property tax on oil and gas reserves is a tried and true tax imposed in other oil and gas producing states. It has also been used successfully in Alaska in the past and, as a property tax, is easily understood.

F. Overcollecting

Once the legislature decides upon the level of revenue that is desired, the reserves property tax can collect the desired revenue without going beyond the legislature's wishes. As shown by the Department of Revenue's fiscal note and the report of Gregg Erickson & Associates to the Department of Revenue, a 25 mill reserves property tax with a credit for income tax payments will yield currently projected revenues.

In addition, SSHB 200 has been structured so that if the reserves property tax at 25 mills will generate more revenue than is desired the legislature can adjust the

millage rate downward to approximate more accurately the desired level of revenue. Of course, each legislature is free to make its own decision as to the level of revenue that is desired.

G. Minimize the Likelihood of Adverse Federal Reaction

Any tax which a state may impose which goes beyond the norm in other states incurs some risk of inviting Congressional restrictions simply because it has gone too far. This risk is probably more significant when the tax is perceived as being passed on to consumers in other states.

Bills have been introduced in Congress in recent years which would place limits on state income taxes and severance taxes. Although none of these bills have become law, a limitation on the way states may tax multistate income or on resource severance tax rates is a real possibility.

The 25 mill property tax contained in SSHB 200 is within the range of property tax rates imposed throughout the nation. The notion of taxing the value of oil and gas reserves is not a novel idea; rather it is a common tax vehicle used in other oil and gas producing states. Unlike income taxes and severance taxes, there are no current Congressional proposals to limit property taxes. Although it cannot be said that the reserves property tax is immune from federal restriction, the likelihood of federal restriction is minimal when compared to other taxes that might be imposed.

H. Symmetry

As reported by the Department of Revenue and its consultants, the reserves property tax collections in SSHB 200 will correspond closely with the oil and gas corporate income tax collections. This will help avoid disturbing previous tax policy judgments by the legislature concerning the tax burden on the oil industry. Although there is not perfect symmetry, the allowance of the income tax credits will help assure that the overall burden on the oil industry will remain relatively stable.

I. Certainty of Revenue Effects

All oil and gas taxes are difficult to estimate with certainty because such taxes are affected by fluctuation in world oil prices and production rates. The Department of Revenue and its consultants Gregg Erickson & Associates, have observed, however, that the reserves property tax is not as sensitive to short term swings in oil prices and production rates as are the severance tax and the oil and gas corporate income tax. Unlike estimates of an apportioned income tax which depend upon judgements about the world wide tax position of individual taxpayers, a reserves tax estimate is more directly keyed to instate activities which are capable of more accurate forecasting.

J. Minimize Spillover Effects

Perhaps the most serious potential adverse spillover effect is the discouragement of future exploration for oil

and gas in Alaska. To mitigate this effect SSHB 200 contains several moderating features. First, the tax is imposed only upon producing oil and gas properties. This will avoid taxing a property before it becomes a viable income producing property. Second, gas reserves are exempt because of the present uncertainty surrounding gas development in the State. As stated by the Governor in his letter of transmittal to SSBH 200, the State should avoid even the possibility that a new tax might effect the economics of currently stalled gas projects. Third, the operation of the credit should prevent the reserves property tax from significantly increasing the overall burden on the oil industry.

III. THE BACKSTOP LEGISLATION

The proposed backstop legislation is contained in Section 8 of SSHB 200. Essentially, it consists of the imposition of a property tax on oil and gas reserves with an allowance of a credit for income tax payments which may be applied against the reserves property tax liability.

A. Tax Imposition (Sec. 48.58.021)

The new tax is an ad valorem tax which begins on July 1, 1981. Unlike other taxes which are imposed on a calendar year basis, this tax would be imposed on a fiscal year basis from July 1 to June 30 of each year commencing with July 1, 1981.

The tax is imposed upon the full and true value of property made taxable under the statute. Property which is taxable includes a broad category of property interests in oil and gas from which there is commercial production. These property interests run the full gamut of potential oil and gas property interests including fee interests, leaseholds, royalty interests, overriding royalty interests, net profit interests and so forth. Thus, to be taxable the property must be a property interest in oil or gas and such property must have commenced commercial production of oil or gas.

These properties are not currently taxed by either the State or municipalities by reason of exemptions contained in both the severance tax statute and the oil and gas hardware tax statute.

The taxable property is taxed at the rate of 25 mills (2.5 percent) each year unless the legislature enacts a different tax rate by the end of February of each taxable year. Section 12 of SSHB 200 sets a 30 mill (3 percent) rate for the first tax year which coincides with the State's 1982 fiscal year.

B. Exemptions (Sec. 43.58.031)

Three catagories of property that would otherwise be taxable under the statute are made exempt. The property interests of the United States or the State are made exempt as provided for in Article IX, Section 4 of the Alaska Constitution. Third party interests in such exempt property, such as leases held by other persons, are not exempt. Thus, federal or state leases to third parties are taxable, but the royalty interest and the retained mineral interest of the federal and state governments are exempt. Similiarly, property required to be exempt under federal law, such as the property interests conveyed under the Alaska Native Claims Settlement Act, are exempt under this bill but only for the length of time required by the Settlement Act. Private interests, such as private leases in exempt Native land, however, are taxable to the extent of such interests. Finally, that portion of the property value attributable to gas reserves is exempt from the tax.

C. Assessment (Sec. 43.58.051)

Taxable property which is not exempt is assessed each year at its full and true value as it existed at the beginning

of the fiscal year. Full and true value is defined, as it is for municipal property tax, as being the estimated price which the property would bring for its proven reserves in an open market and under the then prevailing market conditions in a sale between a willing seller and a willing buyer, both conversant with the property and with prevailing values.

Because property of this nature is seldom traded upon the open market, a valuation method known as the capitalized net income approach is most frequently used. Under this method, the annual net income from the property is projected over the life of the property, using estimates of recoverable reserves of oil and gas in the ground, production rates, prices and expenses. An appropriate discount rate is then chosen and the annual net incomes are discounted to their present value. The sum of these present value net incomes is the market value of the property. A detailed discussion of this method and estimated values for Alaska properties is contained in the report of Gregg Erickson & Associates to the Department of Revenue.

The department in assessing these properties is given the discretion to consider all factors which may affect the value of the property. If the department uses the capitalized net income approach, it has discretion to consider all factors which would affect the value under this approach, such as oil prices, estimated reserves, production rates and expenses. The department's discretion in choosing a discount factor is limited, however, to a standard set by the

legislature. This standard is 10 percentage points above the rate of inflation in the implicit GNP deflator over the five calendar years prior to each assessment date.

D. Tax Calendar

Each tax year begins July 1. That date is the key date for valuation purposes. Although no assessment or other action takes place on July 1, the assessment actions taken later in the tax year are keyed to the valuation of the property as it existed on July 1.

The first date requiring action is August 1. On that date, tax returns must be filed with the Department of Revenue by the owner of the property or the person who controls the property on behalf of the owner. The tax return must include all taxable properties and their value existing on July 1.

After the tax returns have been filed on August 1, but before October 15, the Department of Revenue conducts its own independent valuation work and prepares an assessment roll which contains the identity of all taxable property, its assessed value and the identity of those persons owning the property.

On October 15, the Department of Revenue is required to send an assessment notice to every person owning property which has been included in the assessment roll.

If a taxpayer disagrees with the assessment, he may appeal it by filing written objections with the department within 20

days after the mailing of the assessment notice. A person filing an appeal is entitled to a formal hearing before the department in accordance with the standard hearing procedure applicable to appeals for other taxes. If after a hearing, the department determines that a correction of the assessment is warranted, the department corrects the assessment roll. If the department determines that no correction is warranted, the aggrieved person may appeal the department's action to the Superior Court within 30 days after the department's decision.

On February 1 of the following calendar year, but within the same fiscal year, the Department of Revenue certifies the final assessment roll.

On March 15, after the time for enacting a different tax rate has expired, the department is required to send to every owner of taxable property on the certified assessment roll, a statement of the amount of tax due.

The tax is due at the end of the tax year on June 30, and is payable on that date even if the assessment or the statute is being challenged before the department or the courts. Prepayments or installment payments may be required under regulations of the department.

E. Credits (Sec. 43.58.041)

Persons subject to the tax may credit against their tax liability the amount of tax paid under the Oil and Gas Corporate Income Tax (AS 43.21). The allowable credit is separated into two parts. The first credit consists of

income tax payments made during each taxable year commencing with July 1, 1981 and which income tax payments reflect tax liabilities for tax periods under AS 43.21 after December 31, 1980. The second credit consists of income tax payments made prior to July 1, 1981. Taxpayers who are subject to the new tax but not to AS 43.21 because they are not corporations, are allowed to credit taxes paid under AS 43.20 if they would have been subject to AS 43.21 had they been corporations.

The first credit for current income tax payments is applied in reducing the reserves property tax liability. Any excess credit is not refundable and may not be carried over or carried back to offset reserves tax liability in any other tax year. The second credit for income tax payments made prior to July 1, 1981 may be applied in reducing the reserves tax liability after the first credit has been applied. The second credit, however, may not be taken to the extent that the combined credits will exceed 75 percent of the reserves property tax liability. The excess amount of the second credit, unlike the first credit, may be carried forward to subsequent tax years and applied to reduce that subsequent year's reserves property tax liability.

F. Readjustment of Tax Liability and Credits (Sec. 43.58.041(d); Sec. 43.58.121)

If an income tax liability is adjusted subsequent to the time that it has been credited to reduce the reserves

property tax liability, then the former reserves property tax liability must be readjusted to take into account the readjusted income tax liability and resultant credit. For example, if a person's income tax payments for 1981 are refunded subsequent to the time that those payments have been used to reduce reserves property tax liability, then the reserves property tax must be readjusted to reflect the readjusted income tax payments and the resulting tax liability would then become due. Such readjustments are not subject to the general time limitations on assessment, collection and refund of taxes.

IV. CONSTITUTIONAL PRINCIPLES

The remainder of this report addresses in some detail the constitutional principles underlying the backstop tax legislation. These principles and how the tax conforms to them are extremely important. No additional legal security would be gained if the tax were unconstitutional. We would not recommend legislation which would raise serious constitutional questions. Accordingly, State and federal constitutional principles have provided the necessary guidance and framework for structuring the law.

We have assumed that a taxpayer challenge to the law is likely and that such challenge will raise the maximum number of objections possible. Thus, we expect possible objections based upon equal protection, burden on interstate commerce, lack of a public purpose and violation of due process, among others. We expect a challenge on each of these grounds will be made under both the Alaska Constitution and the United States Constitution, wherever possible. Accordingly, in the discussion which follows we have addressed each of these substantive areas from both a State and federal constitutional law perspective where differences exist.

Generally speaking, the reserves property tax is much less likely to violate constitutional standards, than are taxes which are imposed upon: (1) income derived from interstate commerce, (2) the privilege of conducting inter-

state commerce, or (3) property used in conducting interstate commerce. The reasons for this are more fully discussed below. Reduced vulnerability to constitutional infirmity is extremely important to the State since this tax is a backstop tax. Even if the Oil and Gas Corporate Income Tax should be found unconstitutional, it does not follow that the reserves property tax also will be unconstitutional. In fact, most likely the opposite will be true.

Finally, we point out that the reserves property tax is a traditional tax and its constitutional unassailability well established. However, certain taxpayers have raised the argument that Alaska's entire tax system (not its particular taxes) is unconstitutional because the system in the aggregate results in a confiscation of their property. This is a novel argument. There are no Supreme Court cases which support this argument. In fact, where the argument has been used to challenge single taxes it has received short shrift from the Court. For the taxpayers to prevail on this argument the Supreme Court would have to overrule entire lines of cases and reverse the trend in State tax cases which has allowed the States more and more latitude in fashioning their taxing systems to meet the needs of the local people and economies. Perhaps the taxpayers are making this argument with the hope that this quantum leap by the Supreme Court will come in the case now pending before the Court involving the Montana coal servance tax. That case could be

important to Alaska; it could either add additional support to Alaska's constitutional right to impose this reserves property tax, or it could raise some doubts which do not now exist as to the tax's validity.

A. Commerce Clause

1. Burden on Interstate Commerce

In attacking the Oil and Gas Corporate Income Tax, the taxpayer plaintiffs have asserted that the tax exacts from them more than Alaska's fair share of the profits of the interstate oil and gas industry, and thereby violates the commerce clause of the U.S. Constitution (Article I, § 8). It is likely that similar claims will be raised against the reserves property tax. However, as the following paragraphs explain, the U.S. Supreme Court has consistently upheld similar taxes in the face of such commerce clause challenges.

The United States Constitution, Article I, § 8, states that Congress shall have the power "to regulate commerce with foreign nations, and among the several states, and with the Indian Tribes." The taxpayers may argue, as some have argued in opposing the Oil and Gas Corporate Income Tax, that since almost all Alaskan oil is sold interstate, Alaska's reserves property tax creates an impermissible burden on interstate commerce. However, the U.S. Supreme Court has rejected identical arguments on numerous occasions. A variety of State and local taxes falling on the mining of coal or the producing of oil and gas have been upheld against commerce clause attacks for the simple reason that the taxes were imposed before the resources entered interstate commerce.

An early example of such rulings is the case of Heisler v. Thomas Colliery Co., 260 U.S. 245 (1922). A stockholder of an anthracite coal company challenged Pennsylvania's 1 1/2% tax on the value of all anthracite ready for shipment

or market. Several northeastern states, as amicus curiae, pointed to the fact that 80% of the anthracite was bound for interstate markets and argued that Pennsylvania was seeking to use its monopoly on anthracite production to "compel the inhabitants of other states to pay a tax to Pennsylvania." Id., 260 U.S. at 251-52. In phrases now echoed by the complaints challenging Alaska's Oil and Gas Corporate Income Tax, the consumer states asserted:

> If the tax be upheld, it is inevitable that every State which possesses natural resources essential to other States will impose similar taxes in order to make those whom it cannot directly and constitutionally tax contribute to its exchequer through the channels of commerce. Indeed, several States may combine so as to create absolute monopolies by the enactment of uniform laws exacting taxes similar to this. Such a situation would bring back the commercial conflicts between the States which the commerce clause was enacted to prevent. A result so absolutely repugnant to both the letter and the purpose of the commerce clause ought not to be permitted.

Id., 260 U.S. at 252-53. Compare Paragraphs 70, 72 of the ARCO complaint challenging Alaska's Oil and Gas Corporate Income Tax:

> The keystone of the United States Constitution is the commerce clause, which allowed the Nation to achieve economic unity by limiting the power of any State to exact an exploitative price from other parts of the Nation for use of its resources, markets, or transportation facilities.
>
> . . . .
>
> . . . Alaska has exceeded the bounds of state taxing power by attempting to use the fortuitous presence of a national resource within its borders as a means for exploiting other states and their citizens.

Atlantic Richfield Co. v. Alaska, No. 3AN-79-1903 Civil (3rd Judicial District, filed October 6, 1980). In Heisler the Supreme Court concluded that the plaintiffs' contentions amounted to the assertion that the products of a state are subject to commerce clause regulation even before production or preparation if such products are destined for the interstate market. The Court summarily rejected this contention, saying,

> The reach and consequences of the contention repel its acceptance. If the possibility, or indeed, certainty of exportation of a product or article from a State determines it to be in interstate commerce before the commencement of its movement from the State, it would seem to follow that it is in such commerce from the instant of its growth or production, and in the case of coals, as they lie in the ground. The result would be curious. It would nationalize all industries, it would nationalize and withdraw from state jurisdiction and deliver to federal commerical control the fruits of California and the South, the wheat of the West and its meats, the cotton of the South, the shoes of Massachusetts and the woolen industries of other States, at the very inception of their production or growth, that is, the fruits unpicked, the cotton and wheat ungathered, hides and flesh of cattle yet "on the hoof," wool yet unshorn, and coal yet unmined, because they are in varying percentages destined for and surely to be exported to States other than those of their production.

Heisler, 260 U.S. at 259-60.

The Court held that such articles are not entered into interstate commerce until "they are committed to the common carrier for transportation out of the State to the State of their destination, or have started on their ultimate passage to that State." Id., 260 U.S. at 261. Thus a tax on coal "prepared for shipping" was held not to violate the commerce clause because the coal was not yet in interstate commerce. If a tax on coal prepared for shipping is permissible, then

certainly a tax on oil still in the ground does no violence to the commerce clause because the oil is not yet in interstate commerce.

Less than a year after Heisler, the U.S. Supreme Court reviewed a Minnesota occupation tax on the mining of ore, measured by the value of the ore mined during the preceding year. Oliver Iron Mining Co. v. Lord, 262 U.S. 172 (1923). As in Heisler, plaintiffs argued that since most of the iron ore mined in the State was destined for interstate commerce, the tax burdened that commerce and therefore violated the commerce clause. Again the Supreme Court rejected the argument, citing numerous precedents:

> Plainly the facts do not support the contention. Mining is not interstate commerce, but like manufacturing, is a local business, subject to local regulation and taxation. Its character in this regard is intrinsic, is not affected by the intended use or disposal of the product, is not controlled by contractual engagements, and persists even though the business be conducted in close connection with interstate commerce.
>
> The ore does not enter interstate commerce until after the mining is done, and the tax is imposed only in respect of the mining. No discrimination against interstate commerce is involved. The tax may indirectly and incidentally affect such commerce, just as any taxation of railroad and telegraph lines does, but this is not a forbidden burden or interference.

Id., 262 U.S. at 178-79 (citations omitted). Like the Minnesota ores, Alaskan oil is not in interstate commerce until "after the mining is done," and therefore the reserve property tax does not discriminate against or burden interstate commerce.

In yet a third natural resource tax case, the Supreme Court upheld a West Virginia privilege tax measured by the gross proceeds of the sale of various natural resources produced in the State. Hope Natural Gas Co. v. Hall, 274 U.S. 284 (1927). The Court held that computation of the tax, based on the value of the natural gas at the wellhead (before entering interstate commerce), did not violate the commerce clause. Id. 274 U.S. at 288.

The above trilogy of natural resource tax cases is still controlling precedent today. In 1961, Justice Douglas compared the taking and freezing of fish in Alaska's coastal waters to the extraction of ore in Oliver Iron Mining. Alaska v. Arctic Maid, 366 U.S. 199, 203-4 (1961). He found Oliver to be controlling precedent and upheld Alaska's occupation tax on the taking and freezing of the fish (all bound for interstate commerce) against a commerce clause attack. In Merrion v. Jicarilla Apache Tribe, 617 F.2d 537 (1980), the Tenth Circuit found Oliver Iron Mining and Arctic Maid controlling in upholding the tribe's oil and gas severance tax against a commerce clause challenge. Finally, the Montana Supreme Court has relied on the trilogy of Heisler, Oliver and Hope Gas in sustaining Montana's 30% severance tax on coal. The Montana Court found that the cases on taxation of goods produced in a state all establish a common theme:

> [P]roduction of personal property within a state is a local activity which precedes the entry of the property into interstate commerce, and is therefore subject to state regulation and taxation.

> . . . [W]e have found no United States Supreme Court case, and none has been cited to us, which implicitly or directly overthrows the rule that the several states have the reserved power to tax intrastate manufacturing, extraction, and production of goods.

Commonwealth Edison Co. v. State, 615 P.2d 847, 851 (Sup. Ct. Mont. 1980).

Summary

A tax on property before that property enters interstate commerce does not create a burden within the scope of the commerce clause. The many commerce clause tests evolved by the U.S. Supreme Court in reviewing state taxes all apply to taxes which are imposed, directly or indirectly, upon interstate commerce, such as:

a) taxes on property used in interstate commerce, Fargo v. Hart, 193 U.S. 490 (1904), Johnson Oil Co. v. Oklahoma, 290 U.S. 158 (1933);

b) taxes on the privilege of conducting interstate commerce within a state, Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977), Washington Revenue Dept. v. Stevedoring Ass'n., 435 U.S. 734 (1978); and

c) taxes on net income derived from an interstate business, Mobil Oil Corp. v. Commissioner of Taxes of Vermont, 445 U.S., 425 (1980), Exxon Corp. v. Wisconsin Dept. of Revenue, 447 U.S. 207 (1980).

In contrast, Arctic Maid and the other cases cited demonstrate clearly that the Court refuses to apply those tests to taxes on locally mined, produced, or manufactured goods which have not yet entered interstate commerce. Taxes on such products do not raise any commerce clause question. This is an important factor in our decision to recommend the

reserves property tax as a backstop tax.

The reserves property tax is imposed upon oil even before severance and hence clearly precedes the commodity's entrance into interstate commerce. It seems clear that the reserves property tax does not violate the commerce clause, unless the Supreme Court were to overturn a long and well established line of cases.

2. Discrimination Against Interstate Commerce

The proposed reserves property tax cannot be said to burden interstate commerce because the property taxed is not yet in commerce. Neither does the tax discriminate against interstate commerce by treating property bound for interstate commerce in a different way than property bound for intrastate commerce. With the exception of specific classes of property for which tax exemptions are required by State and federal law, all oil reserves under producing properties are taxed equally, without regard to the final destination of the oil.

The constitutional rule against laws which discriminate against interstate commerce was well stated in a recent U.S. Supreme Court case, Boston Stock Exchange v. State Tax Commission, 429 U.S. 318 (1977). In that case, the court struck down a New York tax on securities transactions under which out-of-state sales were taxed more heavily than most sales within the State. Justice White stated the rule of the decision as follows:

> No State, consistent with the Commerce Clause, may "impose a tax which discriminates against interstate commerce. . . by providing a direct commercial advantage to local business." °quoting from Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 458 (1959)] See also Halliburton Oil Well Co. v. Reily, 373 U.S. 64 (1963); Nippert v. Richmond, 327 U.S. 416 (1946); I.M. Darnell & Son v. Memphis, 208 U.S. 113 (1908); Guy v. Baltimore, 100 U.S. 434, 443 (1880); Welton v. Missouri, 91 U.S. 275 (1876). The prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause. Permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state business "would invite a multiplication of preferential trade areas destructive" of the free trade which the Clause protects. Dean Milk Co. v. Madison, 340 U.S. 349, 356 (1951).

Boston Stock Exchange v. State Tax Commission, 429 U.S. at 329.

Even as this report was being typed, the Supreme Court invoked the same commerce clause discrimination standard to invalidate a Lousiana first-use tax. The Court ruled that the tax and related credits operated to protect local taxpayers from the first-use tax, imposing the tax solely on out-of-state consumers of gas produced on the outer continental shelf. Maryland v. Louisiana, No. 83, Orig. (Sup. Ct. May 26, 1981). Unlike the taxes in Boston Stock Exchange and Maryland v. Louisiana, Alaska's proposed reserves property tax does not discriminate against interstate commerce. Owners of reserves are treated equally, without regard to the final destination of the oil. Unlike the Louisiana

first-use tax, there is no system of exemptions and credits designed to protect intrastate oil producers and users from the effects of the tax.

Some taxpayers may argue that the proposed tax effectively discriminates against interstate commerce simply because most of the oil will eventually be sold interstate. This argument has no merit and was specifically rejected in Heisler and Arctic Maid, discussed elsewhere. Even if none of the oil were used in Alaska, the tax would be valid so long as it was not designed to favor intrastate commerce.

B. Equal Protection

Among the few constraints on Alaska's broad authority to design whatever tax system it deems appropriate, are the equal protection clauses found in the State Constitution and in the Fourteenth Amendment of the U.S. Constitution, and even these do not greatly confine the State's power to tax certain groups more or less than others. In some states an additional constraint is imposed by a constitutional "uniformity clause" requiring all property be taxed at the same rate. Alaska's constitution, however, contains no such clause, and therefore the only limit on the State's ability to differentiate taxpayers into distinct tax categories is the equal protection clause of the State and federal constitutions.

Provided the classifications contained in the tax statute are related to the purposes of such classifications in the manner required by the U.S. and State Constitutions, Alaska may choose to enact a reserves property tax on producing oil and gas properties. There is no constitutional prohibition against taxing one industry and not another or against taxing one industry at a higher rate than another.

The reserves property tax is a constitutional distribution of the tax burden of the State. The tax falls equally on resident and nonresident taxpayers and the exemptions from the tax meet constitutional standards.

Further, the use of the funds derived from this new tax to meet a variety of the State's pressing needs is consistent with the equal protection standards of both the Federal and State constitutions.

1. Distribution of Tax Burden Under the U.S. Constitution

The State of Alaska is free to apportion its tax burden in any fair and just manner that the legislature may choose. The equal protection clause of the Fourteenth Amendment of the U.S. Constitution requires no strict rule of equality. As the Supreme Court of the United States has stated,

> It is inherent in the exercise of the power to tax that a state be free to select the subjects of taxation and to grant exemptions. Neither due process nor equal protection imposes upon a state any rigid rule of equality of taxation. This Court has repeatedly held that inequalities which result from a singling out of one particular class for taxation or exemption, infringe no constitutional limitation.

Carmichael v. Southern Coal & Coke Co., 301 U.S. 495, 509 (1936) (citations omitted); quoted with approval in Lenhausen, 410 U.S. at 363 n.5. The equal protection clause requires only that "the selection [of a class for taxation] is neither capricious nor arbitrary and rests on some reasonable consideration of difference or policy[.]" Allied Stores of Ohio, Inc. v. Bowers, 358 U.S. 522, 527 (1959); cited with approval in Lehnhausen, 410 U.S. at 359-60. Equal protection under the law is not violated so long as members of a given class are taxed equally. Charleston Federal Savings & Loan Association v. Alderson, 324 U.S. 182, 190 (1954).

The State of Alaska may elect to place a reserves property tax on oil while excluding quarries, forests, and other properties. See Lake Superior Consol. Iron Mines v. Lord, 271 U.S. 577, 582 (1926). The findings and purposes in section 43.58.0]] establish that such a classification is not arbitrary and capricious but rests on sound considerations of public policy. Alaska's economy is based on the extraction of the State's abundant natural resources, primarily oil. In an effort to raise money for needed public services and to dampen the uncontrolled oscillations of the State's economy, the legislature may devise a tax system which encourages diversification of the economy, and holds the pace of exploration and development of oil and gas at a desired level. See Magnano Co. v. Hamilton, 292 U.S. 40 (1934); Alaska Fish Co. v. Smith, 255 U.S. 44 (1921). These considerations of policy, articulated in Sec. 43.58.011, are not "hostile and oppressive" (Lehnhausen v. Lake Shore Auto Parts Co., supra) to the oil and gas industry. Rather, they reflect a balanced approach to diversifying the State's economy in preparation for the future when the oil fields will be depleted. Being grounded on sound principles of public policy, the reserves property tax does not violate the equal protection clause of the Fourteenth Amendment.

In a similar instance of natural resource taxation, the Supreme Court upheld a Pennsylvania statute that placed a 1 1/2% tax on the value of anthracite coal mined in the state

but placed no similar tax on bituminous coal. Heisler v. Thomas Colliery Co., 260 U.S. 245 (1922). The anthracite producers clamored that they were denied equal protection under the law. Invoking the "clear and hostile discrimination" test, the Court easily upheld the statute saying,

> Any classification is permissible which has a reasonable relation to some permitted end of governmental action. . . It is enough, for instance, if the classification is reasonably founded in "the purposes and policy of taxation."

Heisler, 260 U.S. at 255 quoting from Watson v. State Comptroller, 254 U.S. 122, 124-25 (1920). In another case the Supreme Court has said:

> Where the public interest is served one business may be left untaxed and another taxed, in order to promote the one, . . . or to restrict or surpress the other[.]

Carmichael v. Southern Coal & Coke Co., 301 U.S. 495, 512 (1937) (citing nine earlier Supreme Court decisions). Like the Pennsylvania anthracite tax, the reserves property tax on producing fields is reasonably founded in the stated purposes and policy of Alaska's taxation system. Just as it was permissible for Pennysylvania to distinguish between anthracite coal and bituminous coal, Alaska may distinguish between oil reserves and other kinds of property, so long as the classification is reasonably related to some permitted end of government action. The government ends served are clearly set forth in the purposes and findings section of the bill. This section makes clear the legislature's objectives

of raising adequate revenues while at the same time encouraging economic diversification, doing so without discouraging oil and gas exploration and development to the maximum extent possible.

Once the legislature has stated the purpose for a given tax classification, the Supreme Court will not override such findings. The Court has said,

> [I]t makes no difference that the facts may be disputed or their effect opposed by argument and opinion of serious strength. It is not within the competency of the courts to arbitrate in such contrariety. Rast v. Van Deman & Lewis Co., 240 U.S. 342, 357 and cases there cited.

Heisler v. Thomas Colliery Co., 260 U.S. 245, 255 (1922).

While the justification for a distinction between producing and nonproducing property is clearly contemplated under the principles discussed above, it is worth pointing out that such a distinction was specifically upheld by the U.S. Supreme Court in Oliver Iron Mining Co. v. Lord, 262 U.S. 172, 180 (1923):

> Equality [under the Fourteenth Amendment] does not require that unproductive mining be taxed along with productive mining. Besides, . . ., the tax will be imposed when the ore is mined.

2. Distribution of Tax Burdens Under The Alaska Constitution

The Constitution of the State of Alaska, unlike some other states, has no uniformity of taxation provision which requires that all property in the State be taxed equally. Therefore, the legislature's power to differentiate types of property for tax purposes is guided only by the Fourteenth

Amendment, discussed above, and the similar provision in Article I, § 1 of the Alaska Constitution. With respect to classification for tax purposes, the Alaska Supreme Court has interpreted the equal protection clause of the State Constitution as follows:

> [T]he classification in question [must] "be reasonable, not arbitrary, and must rest upon some ground of difference having a fair and substantial relation to the object of the legislation so that all persons similarly circumstanced shall be treated alike."

State v. Reefer King Co., Inc., 559 P.2d 56, 65 (Alaska 1977) quoting from Isakson v. Rickey, 550 P.2d 359, 362 (Alaska 1976) See also Williams v. Zobel, 619 P.2d. 422 (Alaska 1980). Although this equal protection standard is different from the federal standard enunciated in Lehnhausen and Carmichael, the basic principles of the federal cases are similar. For example, in Reefer King, supra, the Alaska Supreme Court approved of a tax scheme which imposed a 4% tax on floating processors and only a 1% tax on shorebased processors because the Court deemed the different tax treatment was fairly and substantially related to the State's objective "of encouraging societal contributions of the type made by 'shorebased' processors. . ." Id., 559 P.2d at 66. The contributions made included a contribution to local economies not made by the floating processors. It is an established principle of Alaskan constitutional law that the State may,

> legitimately encourage, through tax incentives or exemptions, industries or types of industries which it considers desirable, and this method of encouragement does not deprive other taxpayers, who do not qualify for the benefit, of their equal protection rights.

Id., 559 P.2d at 66; see also K & L Distributors, Inc. v. Murkowski, 486 P.2d 351, 359 (Alaska 1971). Applying the principle of Reefer King and K & L Distributors, it should be clear that a classification of producing oil properties for tax purposes is a legitimate classification. As the findings state, it is the legislature's judgement that taxes on other industries are undesireable because of the adverse impacts such taxes may have upon those industries and would be counterproductive to efforts to encourage economic diversification but that a reserves property tax is not expected to have any unacceptable adverse consequences on the oil industry in Alaska. In the light of established equal protection standards and the legislature's stated purposes, the reserves property tax does not violate the State Constitution's guarantee of equal protection.

3. Equal Burden Within the Class of Taxpayers

Within a constitutionally permissible class of taxpayers, all such taxpayers must be treated equally or the tax is deemed to violate the equal protection clause of the United States Constitution. Charleston Federal Savings & Loan Association v. Alderson, 324 U.S. 182, 190 (1954). Since the bill does treat all owners of producing oil and

gas properties equally, there is no basis for an equal protection complaint on these grounds.

The reserves property tax falls equally on resident and nonresident taxpayers. The statute makes no distinction whatsoever based on the residency of the taxpayer, and thus is secure from attack under either the privileges and immunities clause of Article IV, § 2 of the United States Constitution; Article IX, § 2 of the Alaska Constitution; or the equal protection clause of the Fourteenth Amendment.

4. Exemptions

The reserves property tax contains tax exemptions for property interests owned by the United States or the State of Alaska, for property exempted from taxation by the laws of the United States, and for natural gas reserves. Each of these exemptions is consistent with the Constitution and laws of the United States and with the Constitution of the State of Alaska.

a. Exemption for Federal Property

Section 4 of the Alaska Statehood Act declares,

> [N]o taxes shall be imposed by said State upon any lands or other properties now owned or hereafter acquired by the United States. . . .

Pub. L. No. 85-508, § 4, 48 USCA § 4, note prec. § 21. Therefore, under the supremacy clause of the U.S. Constitution (Article VI), Alaska may not tax federal property. This prohibition is repeated in Article XII, § 12 of the Alaska Constitution. The exemption of federal property from

taxation is proper under both the federal and State constitutions.

Although property of the United States is exempt, third party interests such as leaseholds in such exempt property is taxable to the extent of those interests. This taxation of leasehold and other third party interests in federal property has consistently been upheld as not violating the United States' constitutional immunity from State taxation under the supremacy clause. United States v. Detroit, 355 U.S. 466 (1958); City of Detroit v. Murray Corp., 355 U.S. 489 (1958); United States v. Township of Muskegon, 355 U.S. 484 (1958); United States v. County of Fresno, 429 U.S. 452 (1977).

b. Exemption for State Property

The Alaska Constitution, Article IX, § 4 states:

> The real and personal property of the State or its political subdivisions shall be exempt from taxation under conditions and exceptions which may be provided by law.

The provision of the bill which exempts property interests owned by the State (Sec. 43.58.031(1)) is in compliance with the Alaska Constitution. Similarly, the taxation of third party interests in property of the State is constitutional. Article IX, § 5 of the Alaska Constitution states:

> "Private leaseholds, contracts, or interests in land or property owned or held by the United States, the State, or its political subdivisions shall be taxable to the extent of the interests."

c. Exemption for Lands Conveyed to Native Corporation Pursuant to the Alaska Native Claims Settlement Act

The bill contains an exemption from the tax for Native Corporations which have an interest in producing oil reserves situated on lands that were conveyed to Alaska Native Corporations pursuant to the Alaska Native Claims Settlement Act (ANCSA). This exemption is required by federal law.

Section 21(d) of ANCSA states:

> (d) Real property interests conveyed, pursuant to this Act, to a Native individual, Native group, or Village or Regional Corporation which are not developed or leased to third parties, shall be exempt from State and local real property taxes for a period of twenty years after the date of enactment of this Act: Provided, That municipal taxes, local real property taxes, or local assessments may be imposed upon leased or developed real property within the jurisdiction of any governmental unit under the laws of the State: Provided further, That easements, rights-of-way, leaseholds, and similar interests in such real property may be taxed in accordance with State or local law. All rents, royalties, profits, and other revenues or proceeds derived from such property interests shall be taxable to the same extent as such revenues or proceeds are taxable when received by a non-Native individual or corporation.

Pub. L. No. 92-203, § 21(d), 43 U.S.C.A. § 1620(d) (Supp. 1981).

The first sentence of this section exempts unleased or undeveloped property from taxation. The implication of that sentence is that leased or developed property may be taxed by State and local governments. However, the first proviso

expressly authorizes local governments to tax developed property. This seems redundant and raises doubts as to whether Congress did intend to grant the taxing authority implied by the first sentence. Section 21(d) is, at best, ambiguous concerning the State's authority to impose a property tax upon leased or developed property owned by Native Corporations.

The legislative history of § 21(d) is of little help in resolving this ambiguity. An earlier version of the Act contained the following language:

> (c) Lands to which a Native village acquires title pursuant to sections 10-12, inclusive, or section 15 hereof, lands to which a regional corporation acquires title pursuant to section 12, and mineral rights to which any Native corporation acquires title pursuant to sections 12 or 15 hereof, shall be exempt from State and local real property taxes: Provided, That municipal taxes or assessments may be imposed upon individually owned real property within its jurisdiction by any Native village incorporated as a governmental unit under the laws of the State of Alaska: And provided further, That easements, rights-of-way, leaseholds and similar interests in such real property may be taxed in accordance with State or local law. All rents, royalities, profits, and other revenues or proceeds derived from such lands and mineral rights shall be taxable to the same extent as such revenues or proceeds are taxable when received by a non-Native individual or corporation.

H.R. 7039 92d Cong. 1st Sess. (March 31, 1971) See also S. 835, 92d Cong. 1st Sess. (Feb 17, 1971) which was identical to H.R. 7039 except that it limited the tax exemption to a period of fifty years.

Analysis of the transition from this version to the final version of § 21(d) does not reveal the drafters' intent. In general, the exemptions were made less broad; more taxation was allowed. But the only new express statement is that municipalities and local governments of all types may tax leased or developed property. Having allowed municipal taxation of leased or developed property by broadening the proviso, perhaps the drafters then changed the first sentence to read "unleased or undeveloped property is exempt" from "municipal taxation", because this seemed more symmetrical or complementary, not realizing that they had made an implicit statement about the state's taxing power as well.

An alternative scenario, equally convincing but not more so, is that the drafters intended to narrow the exemptions so that both states and municipalities could tax leased or developed property. If they set out to do this while also making as few changes in the original text as possible, they could have crossed out a few phrases and added a few phrases, metamorphosing the first version into the final language. Having altered the first sentence to exempt only undeveloped or unleased property, the drafters might have realized that the first proviso was no longer necessary. Still, it is possible they preferred to alter it slightly, making it merely redundant, to removing it entirely, which might have aroused concern among municipal and local governments.

In the end, one is left with two alternatives: either the drafters overlooked the full implications of the change in the first sentence or they chose to retain a proviso which is redundant and creates ambiguity. Neither hypothesis seems more compelling.

Section 21(d) of ANCSA, was recently amended by Congress in the Alaska National Interest Lands Conservation Act, Pub. L. No. 96-487, § 904, 94 Stat. 2371, 2434 (Dec. 2, 1980), and reads as follows:

> (d)(1) Real property interests conveyed, pursuant to this Act, to a Native individual, Native Group, Village or Regional Corporation or corporation established pursuant to section 14(h)(3) which are not developed or leased to third parties or which used solely for the purposes of exploration shall be exempt from State and local real property taxes for a period of twenty years from the vesting of title pursuant to the Alaska National Interest Lands Conservation Act or the date of issuance of an interim conveyance or patent, whichever is earlier, for those interests to such individual, group, or corporation: Provided, That municipal taxes, local real property taxes or local assessments may be imposed upon any portion of such interest within the jurisdiction of any governmental unit under the laws of the State which is leased or developed for purposes other than exploration for so long as such portion is leased or being developed: Provided further, That easements, rights-of-way, leaseholds, and similar interests in such real property may be taxed in accordance with State or local law. All rents, royalties, profits and other revenues or proceeds derived from such property interests shall be taxable to the same extent as such revenues or proceeds are taxable when received by a non-Native individual or corporation.

Though small changes have been made to classify land used only for exploration as tax exempt, the essential ambiguity created by the leading sentence and the first proviso remains.

The proviso explicitly grants municipal and local governments the authority to levy real property taxes on leased and developed Native Land. No such explicit grant of authority is made to the State. In analyzing this ambiguity further, we have resorted to more general principles of statutory construction.

The proper rules of construction can be derived from several recent cases which clarify the standard of review for laws taxing dependent Indians generally and which apply that standard to cases involving ambiguities in ANCSA. In Bryan v. Itasca County, 426 U.S. 373 (1976), the Supreme Court reviewed a challenge to Minnesota's state and county property taxes on the mobile home of a reservation Indian. Minnesota contended that 28 U.S.C. § 1360, which grants to the states civil jurisdiction over Indian reservations, implicitly authorized property taxation (a form of civil law). The Court found that the statute was ambiguous with respect to taxation and invoked the following standard of review:

> Finally, in construing this "admittedly ambiguous" statute, Board of Comm'rs v. Seber, 318 U.S., at 713, we must be guided by that "eminently sound and vital canon," Northern Cheyenne Tribe v. Hollowbreast, 425 U.S. 649, 655 n. 7 (1976), that "statutes passed for the benefit of dependent Indian tribes . . . are to be liberally construed, doubtful expressions being resolved in favor of the Indians." Alaska Pacific Fisheries v. United States, 248 U.S. 78, 89 (1918). See Choate v. Trapp, 224 U.S. 665, 675 (1912); Antoine v. Washington, 240 U.S. 194, 199-200 (1975). This principal of statutory construction has particular force in the face of claims

> that ambiguous statutes abolish by implication Indian tax immunities. McClanahan v. Arizona State Tax Comm'n, 411 U.S., at 174 Squire v. Capoeman, 351 U.S. 1, 6-7 (1956); Carpenter v. Shaw, 280 U.S. 363, 366-367 (1930). "This is so because . . Indians stand in a special relation to the federal government from which the states are excluded unless the Congress has manifested a clear purpose to terminate [a tax] immunity and allow states to treat Indians as part of the general community." Oklahoma Tax Comm'n v. United States, 319 U. S. 598, 613-614 (1943) (Murphy, J., dissenting).

Bryan, 426 U.S. at 392. The Court held that Minnesota had no authority to tax the reservation Indians.

In a footnote in Bryan, however, the Court said that its analysis might yield a different result for tribal Indians "who have left or never inhabited federally established reservations." Id., 426 U.S. at 376-377, n.2. In Organized Village Of Kake v. Egan, 369 U.S. 60 (1962), the Supreme Court considered whether Alaska's anti-fishtrap laws applied to the non-reservation Thlinget Indians in Alaska. The Court decided the case on the basis of § 4 of the Alaska Statehood Act, saying that Congress had prohibited the State from taxing Indian property, but not from regulating aboriginal fishing rights; therefore, the anti-fishtrap laws were validly applied to the Thlinget Indians. Kake, 369 U.S. at 68. The rule of Kake was summarized in a later case as follows:

> Absent express federal law to the contrary, Indians going beyond reservation boundaries have generally been held subject to nondiscriminatory state law otherwise applicable to all citizens of the State.

Mescalero Apache Tribe v. Jones, 411 U.S. 145, 148-149 (1973). Of course, if Kake had involved a state property tax on restricted Native land, there would have been "express federal law to the contrary" since § 4 of the Statehood Act prohibited State taxation of Indian lands. Section 4 only allowed the State of Alaska to tax Native lands that "are held by individual natives in fee without restrictions on alienation".

The United States District Court for Alaska has adopted the Bryan standard of review for resolving ambiguities in the interpretation of ANCSA. Alaska Public Easement Defense Fund v. Andrus, 435 F. Supp. 664, 670 (D. Ak. 1977). In that case, Natives challenged the Secretary of the Interior's interpretation of the reserved easement provisions of ANCSA. Native plaintiffs argued that the Bryan rule should apply and that doubtful expressions should be resolved in their favor. The Secretary of the Interior argued that the Bryan rule should not apply to Alaska Natives because they are "not dependent Indians, but rather are well financed, profit making corporations." Id., 435 F. Supp. at 670. Further, the Secretary argued that two rules of statutory construction supported his interpretation: (a) The Secretary's interpretation of a statute delegating authority to him should be accorded great deference, Udall v. Tallman, 380 U.S. 1 (1965), and (b) public land grants are to be construed favorably to the government, United States v. Union Pacific Ry. Co., 353 U.S. 112, 116 (1957). After consideration, the

court adopted the Natives' position:

> While it is true that the Alaska Native Corporations are well financed that financing and the corporations themselves are the result of the Act. Prior to the Act, Congress had the power totally to extinguish aboriginal land title without compensation. United States v. Atlantic Richfield Co., 435 F. Supp. 1009, 1029-1030 (D. Alaska 1977); Tee-Hit-Ton Indians v. United States, 348 U.S. 272, 279 & 285, 75 S. Ct. 313, 99 L. Ed. 314 (1955). Thus, although generally the Alaska Natives were not dependent in the sense that they were on reservations, their fate rested in the hands of Congress and they were dependent upon its protection and good faith. In these circumstances the language used, if ambiguous, should be resolved in their favor. Squire v. Capoeman, 351 U.S. 1, 6-7, 76 S.Ct. 611, 100 L. Ed. 883 (1956).
>
> The court's approach, therefore, will be to analyze the statutory language and the legislative intent to determine these issues. If ambiguities remain, they will be resolved in favor of the Natives.

Alaska Public Easement Defense Fund v. Andrus, 435 F. Supp. 664, 670-671 (1977).

The U.S. District Court for Alaska applied the same standard of review to a tax dispute in People of South Naknek v. Bristol Bay Borough, 466 F. Supp. 870 (1979). The Borough had levied real and personal property taxes on restricted lands held in trust for the use and benefit of the Natives. Id., 466 F. Supp. at 872. The Court applied the following rule of construction:

> The focus of the court's inquiry must be whether the power of the Borough to levy the taxes challenged in this has been pre-empted by the relevant federal statutes. In reviewing these statutes the court must follow the general rule that statutes passed for the benefit of

> Indians are to be liberally construed, doubtful expressions being resolved in favor of the Indians. This rule of construction has particular force in determining whether Indians and their property enjoy tax immunity.

Id., 466 F. Supp. at 873 (citations omitted). The Court held that the Native Allotment Act, the Native Townsite Act, and § 4 of the Alaska Statehood Act pre-empted the Borough's authority to tax real property, but that personal property could be taxed.

Applying the principles of law discussed above, it appears that the State's authority to levy a property tax on oil reserves situated on Native Corporation lands remains pre-empted by federal law. Prior to the passage of ANCSA the State's authority to tax Native land was pre-empted by § 4 of the Alaska Statehood Act which states, in pertinent part:

> [N]o taxes shall be imposed by said State upon any lands or other property now owned or hereafter acquired by the United States or which, as hereinabove set forth, may belong to said natives, except to such extent as the Congress has prescribed or may hereafter prescribe, and except when held by individual natives in fee without restrictions on alienation.

Pub. L. No. 85-508, § 4, 48 U.S.C.A. § 4, note prec. § 21.

The section is, of course, silent as to lands held in fee by Native Corporations since these Corporations had not yet been created by ANCSA. Turning to ANCSA to see if the state has been granted authority to tax real property owned by Natives, we arrive at § 21(d). That section expressly

grants to municipal and local governments, the power to tax leased and developed property but is ambiguously silent about the State's authority. The first sentence of § 21(d) and the following proviso raise conflicting inferences; the legislative history is also unclear. Under these circumstances, it seems likely that a federal court following the rule of construction set out in the cases discussed, would resolve the ambiguity in favor of the Natives and hold that the State may not tax leased and developed property.

d. Exemption for Natural Gas

As discussed above, producing oil reserves are a separate and distinct class of property for tax purposes. There is no requirement that other types of natural resources also be taxed. The bill is structured to impose a tax on both producing oil and gas reserves but then grants an exemption for natural gas reserves.

e. Summary of Exemptions

The above discussion shows that the exemptions to the reserves property tax for federal, state, and Native Corporation properties are in response to requirements of the U.S. Constitution and laws and the Constitution of the State of Alaska. Certainly such exemptions have a rational basis and do not offend the equal protection clause of the Fourteenth Amendment of the U.S. Constitution. As stated in Carmichael v. Southern Coal & Coke Co., 301 U.S. 495, 509 (1937):

> This Court has repeatedly held that inequalities which result from a singling out of one particular class for taxation or exemption,

infringe no constitutional limitation. . . .

> Like considerations govern exemptions from the operation of a tax imposed on the members of a class. A legislature is not bound to tax every member of a class or none. It may make distinctions of degree having a rational basis, and when subjected to judicial scrutiny they must be presumed to rest on that basis if there is any conceivable state of facts which would support it.

(citations omitted) Distinctions based on the mandates of State and Federal laws and constitutions must be presumed to be rational and in compliance with the equal protection clause of the U.S. Constitution.

Similarly, such distinctions should also not offend the equal protection clause of the State Constitution since the distinctions simply follow requirements of the U.S. Constitution and laws and the Constitution of the State of Alaska.

The exemption for gas property is not founded upon federal and state mandates but upon legitimate State policies to avoid discouraging gas development in the State. The Governor in his letter of transmittal with SSHB 200 stated, "Because of the somewhat precarious economic situation with respect to natural gas production and transportation, evidenced in part by the difficulties that have attended efforts to obtain financing for a natural gas pipeline from the Prudhoe Bay fields, I am reluctant to impose any possible additional tax burdens on natural gas at this time." Accordingly, the purpose for exempting gas property as stated in SSHB 200 is "to avoid discouraging. . . the development of natural gas production in the State."

As discussed above, the exemption of certain industries to encourage their development does not run afoul of the equal protection clauses of the United States and State Constitutions. State v. Reefer King Co., Inc., 559 P.2d 56 (Alaska 1977); K & L Distributors, Inc. v. Murkowski, 486 P.2d 351 (Alaska 1971); Carmichael v Southern Coal & Coke Co., 301 U.S. 492 (1937).

C. Public Purpose

1. The Backstop Tax

The reserves property tax on producing oil properties will serve numerous valid public purposes of the State of Alaska, which are listed in Sec. 43.58.011 (Findings and Purposes) of the bill. Because the money raised by the tax will be expended for valid public purposes, the tax is immune from challenge under either Article IX, § 6 of the Alaska Constitution or the Fourteenth Amendment of the U.S. Constitution.

a. Review Under the Alaska Constitution

Article IX, § 6 of the Alaska Constitution states:

> No tax shall be levied, or appropriation of public money made, or public property transferred, nor shall the public credit be used, except for a public purpose.

This constitutional requirement has been interpreted by the Supreme Court of Alaska on several occasions. The Court has adopted the following standard for reviewing statutes which allegedly violate § 6:

> In determining the question presented this court adopts for its guidance the general rule, supported by the great weight of authority, that where the legislature has found that a public purpose will be served by the expenditure or transfer of public funds or the use of the public credit, this court will not set aside the finding of the legislature unless it clearly appears that such finding is arbitrary and without any reasonable basis in fact.

DeArmond v. Alaska State Development Corp., 376 P.2d 717, 721 (Alaska 1962).

Applying this standard, the Court approved the expenditure of public money for industrial development loans. In a subsequent case the Court applied the same standard in approving a statute that granted public money to retire the mortgages of those whose homes were destroyed in the 1964 earthquake. Suber v. Alaska State Bond Committee, 414 P.2d 546 (Alaska 1966). Also in 1966, the Court invoked the DeArmond standard verbatim in approving the creation of the Alaska State Mortgage Association, which used public funds to finance private housing. Walker v. Alaska State Mortgage Association, 416 P.2d 245, 251 (Alaska 1966). Finally, in Wright v. City of Palmer, 468 P.2d 326 (Alaska 1970), the Court upheld the city's issuance of general obligation bonds to encourage industrial development. Quoting the Suber opinion, the Court said:

> The basic objective of government is to protect and promote the health, safety and general welfare of the people. When a condition of affairs appears in the state which presents a threat to the accomplishment of that objective, the government has the right, and the obligation, to cope with such threat by whatever measures, within constitutional limits, that are necessary or appropriate.

Wright, 468 P.2d at 331.

As listed in the legislative findings, Sec. 43.58.011(a), the legislature perceives several inadequacies in the level of the public services in this State. To correct these inadequacies in transportation, health care, communications, energy, and justice facilities, to name but a few, the State requires a secure and substantial source of tax revenues.

The State now finds that the Oil and Gas Corporate Income Tax, a significant source of revenue, is being challenged in court, presenting a threat to the accomplishment of the State's various objectives. As stated by the Supreme Court in Wright, "The government has the right, and the obligation, to cope with such threat by whatever measures, within constitutional limits, that are necessary or appropriate." Wright, 468 P.2d at 331.

Assuming that the reserves property tax does not offend the federal constitution (discussed below), the findings and purposes stated in Sec. 43.58.011 are well within the scope of Art. IX, § 6 of the Alaska Constitution, requiring that taxes be levied only for public purposes. The various uses proposed for the tax revenues have been endorsed by the State Supreme Court.

b. Review Under the U.S. Constitution

With the adoption of the Fourteenth Amendment, the U.S. Constitution limited the authority of the states to impose taxes. In Green v. Frazier, 253 U.S. 233, 238 (1920) the Court explained the limitation of the Fourteenth Amendment as follows:

> The due process of law clause contains no specific limitation upon the right of taxation in the states, but it has come to be settled that the authority of the states to tax does not include the right to impose taxes for merely private purposes.

Green, 253 U.S. at 238. In a subsequent case, rejecting a claim that the State of Washington had imposed a tax on the

sale of margaerine within the State purely for the purpose of protecting the State's butter industry, the Supreme Court said of the "public purpose requirement,"

> [T]hat requirement has regard to the use which is to be made of the revenue derived from the tax, and not to any ulterior motive or purpose which may have influenced the legislature in passing the act. And a tax designed to be expended for a public purpose does not cease to be one levied for that purpose because it has the effect of imposing a burden upon one class of business enterprises in such a way as to benefit another class.

Magnano Co. v. Hamilton, 292 U.S. 40, 43 (1934). Thus, the Supreme Court has adopted the principle that the Fourteenth Amendment places a limit on State taxing power similar to that of the "public purpose clause" in Article IX, § 6 of the Alaska Constitution and in testing the validity of State taxes, the court will look to the uses to be made of the taxes collected.

In Carmichael v. Southern Coal & Coke Co., 301 U.S. 495 (1937), the Supreme Court adopted a public purpose standard that foreshadowed the test adopted by the Alaska Supreme Court in DeArmond:

> This Court has long and consistently recognized that the public purposes of a state, for which it may raise funds by taxation, embrace expenditures for its general welfare. The existence of local conditions which, because of their nature and extent, are of concern to the public as a whole, the modes of advancing the public interest by correcting them or avoiding their consequences, are peculiarly within the knowledge of the legislature, and to it, and not to the courts, is committed the duty and responsibility of making choice of the possible

> methods. As with expenditures for the general welfare of the United States, whether the present expenditure serves a public purpose is a practical question addressed to the law-making department, and it would require a plain case of departure from every public purpose which could reasonably be conceived to justify the intervention of a court.

Carmichael, 301 U.S. at 514-15 (emphasis added; citations omitted). So saying, the Court approved an Alabama tax on employers of more than eight persons to be used for unemployment benefits. Thus, the Supreme Court defers to the wisdom of State legislatures in the matter of defining public purposes, and will uphold a taxation scheme if the resultant expenditures are related to any conceivable public purpose.

The Alaskan Government has listed many public purposes which the reserve property tax will serve. These purposes are valid public purposes and the raising of revenues to meet these purposes through a reserves property tax is rational. The tax, therefore, should withstand a challenge under both the public purpose requirement of Article IX, § 6 of the Alaska Constitution and the due process requirements of the Fourteenth Amendment to the U.S. Constitution.

2. Credit for Oil and Gas Corporate Income Taxes

a. Under Alaska's Constitution

Section 43.58.041 of the reserves property tax grants two distinct types of credits against the tax to those who have paid taxes under the Oil and Gas Corporate Income Tax.

It may be argued that these tax credits amount to an unconstitutional gift of public funds. This argument is not valid since the credits serve a public purpose.

As discussed above, Article IX, § 6 of the Alaska Constitution prohibits the appropriation of money or transfer of public property except for a public purpose. Under similar constitutional provisions, the courts of neighboring states have scrutinized statutes which retroactively cancel delinquent taxes or provide a credit against future taxes. In Japan Line, Ltd. v. McCaffree, 558 P.2d 211 (Wash. 1977) plaintiffs challenged the constitutionality of a county tax law which retroactively cancelled a previous tax. They contended that the repeal of a valid tax constituted a gift of public funds, in violation of the Washington Constitution, Article 8, §§ 5 and 7 which state:

> § 5 The credit of the state shall not, in any manner be given or loaned to, or in aid of any individual, association, company or corporation.
>
> § 7 No county. . . shall hereafter give any money, or property, or loan its money, or credit to or in aid of any individual, association, company, or corporation. . .

The Washington Supreme Court rejected plaintiff's contentions because the cancelled tax was replaced by a new and more burdensome tax. Japan Lines, Ltd., 558 P.2d at 214. In San Bernardino County v. Way, 117 P.2d 354 (Cal. 1941), the Court upheld a County resolution cancelling the delinquent property taxes in a road improvement district. The

resolution was challenged by the county surveyor who charged that the resolution violated Article IV, § 31 of the California Constitution:

> Sec. 31. The Legislature shall have no power . . . to make any gift or authorize the making of any gift, of any public money or thing of value to any individual, municipal or other corporation whatever. . . .

The court upheld the resolution, stating that in determining whether any appropriation of public funds is an unconstitutional gift,

> The primary and fundamental subject of inquiry is as to whether the money is to be used for a public or a private purpose. If it is for a public purpose, it is not, generally speaking, to be regarded as a gift.

San Bernardino County, 117 P.2d at 359. Because the county resolution served the public purpose of restoring property to the tax rolls, it was held not to be an unconstitutional gift of public money. See also City of Ojai v. Chaffee, 140 P.2d 116 (Dist. Ct. App. Cal. 1943); Delta Cty. Levee Improvement Dist. No. 2 v. Leonard, 559 S.W.2d 387 (Civ. App. Tex. 1977); Community Television of Southern California v. County of Los Angeles, 45 Cal. App.3d 276 (197[illegible].

These cases must be contrasted with cases such as City of Yakima v. Huza, 407 P.2d 815 (Wash. 1965), in which the Court found unconstitutional an initiative ordinance which would have repealed a recent tax increase and would have allowed taxes already paid under the repealed ordinances to be credited against future taxes. The court found this

repeal-and-credit scheme, unbalanced by any new tax and unsupported by any public purpose, to be in violation of the state constitution. City of Yakima, 407 P.2d at 820.

The determinative factor in each of the cases cited above was whether the cancellation, credit, or refund of a tax owed or already paid served a valid public purpose. If it did, the court permitted the cancellation, credit or refund, notwithstanding that a private benefit was granted to certain taxpayers. If no public purpose could be found, then the refund or credit was found to be an unconstitutional. In evaluating the validity of the tax credit provisions of SSHB 200, we must look to the public purpose served by the credit. In doing this, it is also important to distinguish between the credit allowed for current taxes payable under the Oil and Gas Corporate Income Tax and the credit allowed for taxes already paid under that Act. There can be little doubt that the credit for current taxes is constitutional. The credit is obviously designed to meet the secondary objective stated in the bill, namely to the extent possible and consistent with ensuring adequate revenues in the event the Oil and Gas Corporate Income Tax is declared invalid, the credit avoids increasing the tax burden on the oil and gas industry. This is, of course, a valid public purpose since increasing the burden may discourage desired economic activity.

Credit for Oil and Gas Corporate Income Tax already paid also serves the same public purpose because without

such credit, the State could ensure the desired level of revenues only by collecting more taxes in the short term, or by increasing taxes after (and if) the State should lose the pending lawsuit. Both alternatives, while certainly possible, are less attractive than the allowance of a credit for taxes already paid because those alternatives may discourage development in the future and the credit approach avoids this problem. Nonetheless, the existence of these alternatives may give rise to an argument that the credit for taxes already paid serves no valid public purpose and is therefore unconstitutional. It is for this reason, that SSHB 200 contains two separate credit provisions and a clear severability clause. These indicate the legislature's choice to increase the tax burden (and accept whatever adverse effects occur) rather than risk substantial diminution of revenues in the event the State loses the pending lawsuit (and incur the adverse consequences of such diminution).

b. Under the U.S. Constitution

The credit provisions also are constitutional when judged by the provisions of the U.S. Constitution. At the outset, it should be stated that there is some doubt that the U. S. Constitution contains any provision prohibiting tax refunds. Professor Sekula, in Retroactive Remedial Tax Legislation and the Statute of Limitations--The Silenced Claimant v. I.R.S., 9 Duquesne L.Rev. 1, 27 (1970) hypothe-

sized that a retroactive tax refund could be challenged under the U. S. Constitution, if at all, only on the grounds that it constitutes an unjustifiable classification that discriminates between taxpayers similarly situated, and thus violates the equal protection clause of the Fourteenth Amendment (in the case of State laws). Id. at 44. As discussed in the separate section on equal protection, the Supreme Court will not invalidate a state's choice of objects for taxation, exemption, or credit where the classification bears a rational relation to a valid public purpose. Because the tax credit provisions of the proposed bill are designed to achieve valid public purposes, this federal standard is met.

D. Due Process

1. Excessive Taxes

No doubt it will be asserted that the proposed reserves property tax constitutes a confiscation of a taxpayer's property in violation of the due process clause of the Fourteenth Amendment. A review of the many Supreme Court cases testing property taxes against the due process standard reveals that such an assertion would be without merit. The proposed tax is not arbitrary in its design and we have found no decided cases that invalidate a general property tax statute on the grounds that the rate is too high. Indeed, a recent decision of the Supreme Court confirms that a tax high enough to destroy a business entirely is not constitutionally infirm for that reason.

a. Procedural Due Process

One of the early cases decided under the due process clause of the Fourteenth Amendment was Davidson v. New Orleans, 96 U.S. 97 (1877). In that case, the Court set the following standard for reviewing taxes under the due process clause,

> That whenever by the laws of a State, or by State authority, a tax, assessment, servitude, or other burden is imposed upon property for the public use, whether it be for the whole State or of some more limited portion of the community, and those laws provide for a mode of confirming or contesting the charge thus imposed, in the ordinary courts of justice, with such notice to the person, or such proceeding in regard to the property as is appropriate to the nature of the case, the judgement in such proceedings cannot be said to deprive the owner of his property without due process of law, however obnoxious it may be to other objections.

Id., 96 U.S. at 104-5. This formula suggests that due process is basically a procedural requirement. The taxpayer must be allowed some procedural means to appeal his assessment. No substantive standard for measuring the tax is suggested. In Davidson, certain New Orleans landowners protested an assessment against their property for the purpose of draining several swamps within the city. The Court stated,

> Before the assessment could be collected, or become effectual, the statute required that the tableau of assessments should be filed in the proper District Court of the State; that personal service of notice, with reasonable time to object, should be served on all owners who were known and within reach of process, and due advertisement made as to those who were unknown, or could not be found. This was compiled with; and the party complaining here appeared, and had a full and fair hearing in the court of the first instance, and afterwards in the Supreme Court. If this be not due process of law, then the words can have no definite meaning as used in the Constitution.

Id., 96 U.S. at 105-6. This interpretation of "due process" refers only to lawful procedures. Alaska's proposed reserves property tax contains procedures for appealing assessments and, therefore, satisfies the due process requirements of Davidson. See Sec. 43.58.081.

b. Substantive due process: burdens v. benefits

Later Supreme Court decisions have evolved new ways of applying the due process standard. One group of early cases reviewed a series of special assessment taxes. These taxes

were levied to finance local projects and often fell most heavily on properties that were particularly benefited. Heavily burdened property owners complained that their property was being taken for public purposes without just compensation. In these cases, the due process clause of the Fourteenth Amendment was held to limit state governments in the same way that the due process clause of the Fifth Amendment limits the federal government.

The lengthy opinion and dissent in French v. Barber Asphalt Paving Company, 181 U.S. 324 (1901), illustrate well the application of the due process clause to special assessments. Barber Asphalt Paving Company had constructed new streets in Kansas City, Missouri, and was suing abutting property owners to enforce the lien of a special assessment tax bill. The majority in French upheld the special assessment, which apportioned the cost of new streets to abutting landowners according to a "front footage" rule. The majority found that there had been a legislative determination of the proper apportionment and that this legislative determination could not be reviewed. Id., 181 U.S. at 343-346.

Writing the dissent in French, Justice Harlan argued that the assessments violated due process because no opportunity was given the taxpayer to appeal his assessment on the ground that it was significantly in excess of the benefits conferred on his property. However, Justice Harlan

noted that this strict proportionality was only required for special assessments for local improvements:

> Special assessments are a peculiar species of taxation, standing apart from the general burdens imposed for state and municipal purposes, and governed by principles that do not apply generally. The general levy of taxes is understood to exact contributions in return for the general benefits of government, and it promises nothing to the persons taxed beyond what may be anticipated from an administration of the laws for individual protection and the general public good. Special assessments, on the other hand, are made upon the assumption that a portion of the community is to be specially and peculiarly benefited in the enhancement of the value of property peculiarly situated as regards a contemplated expenditure of public funds; and, in addition to the general levy, they demand that special contributions, in consideration of the special benefit, shall be made by the person receiving it. The justice of demanding the special contribution is supposed to be evident in the fact that the persons who are to make it, while they are made to bear the cost of a public work, are at the same time to suffer no pecuniary loss thereby, their property being increased in value by the expenditure to an amount at least equal to the sum they are required to pay. This is the idea that underlies all these levies." Cooley on Taxation, 416, c. 20, § 1; Cooley on Taxation, 2d ed. 606, § 1.

French, 181 U.S. at 362 (emphasis added). The notion that general levies promise "nothing to the persons taxed beyond what may be anticipated from an administration of the laws for individual protection and the general public good" is repeated with force in Carmichael v. Southern Coal & Coke Co., 301 U.S. 495, 522-523 (1937). There, several employers protested the levy of an Alabama tax to provide benefits to unemployed workers. The Court in Carmichael repudiated the

idea that general levies may only burden taxpayers in proportion to the benefit conferred:

> Nothing is more familiar in taxation than the imposition of a tax upon a class or upon individuals who enjoy no direct benefit from its expenditure, and who are not responsible for the condition to be remedied.
>
> A tax is not an assessment of benefits. It is as we have said, a means of distributing the burden of the cost of government. The only benefit to which the taxpayer is constitutionally entitled is that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes. See Cincinnati Soap Co. v. United States, supra. Any other view would preclude the levying of taxes except as they are used to compensate for the burden on those who pay them, and would involve the abandonment of the most fundamental principle of government - that it exists primarily to provide for the common good.

Carmichael, 301 U.S. at 521-523 (in footnote 14 the Court lists numerous taxes which confer no direct benefit on the persons taxed). As recited in the statements of legislative findings and purpose, Alaska's proposed reserves property tax serves a variety of public purposes. Being a general levy for the common good, it is unassailable on the ground that it burdens certain taxpayers more than it benefits them. This is not a violation of the due process clause of the Fourteenth Amendment.

c. Substantive due process: taxes that impair a business

On various occasions it has been argued that a state tax which is so oppressive as to destroy a particular busi-

ness is a taking of property without due process. The U.S. Supreme Court has consistently refused to strike down such a tax.

In Alaska Fish Co. v. Smith, 255 U.S. 44 (1921), the territorial legislature of Alaska had imposed a tax on the manufacture of oil and fertilizer from fish with the purpose of preserving herring as a food supply for men and salmon. The Alaska Fish Company complained that the tax effectively prohibited and confiscated it's business without due process. The Court upheld the tax saying,

> If Alaska deems it for its welfare to discourage the destruction of herring for manure and to preserve them for food for man or for salmon, and to that end imposes a greater tax upon that part of the plaintiff's industry than upon similar use of other fish or of the offal of salmon, it hardly can be said to be contravening a Constitution that has known protective tariffs for a hundred years. Rast v. Van Deman & Lewis Co., 240 U.S. 342, 357. Even if the tax should destroy a business it would not be made invalid or require compensation upon that ground alone. Those who enter upon a business take that risk. We know of no objection to exacting a discouraging rate as the alternative to giving up a business, when the legislature has the full power of taxation.

Id., 255 U.S. at 48-49.

In Magnano Co. v. Hamilton, 292 U.S. 40 (1934), appellant, a margarine manufacturer, challenged a statute of the State of Washington which placed an excise tax of fifteen cents per pound on all butter substitutes sold in the state. Magnano Co. claimed that the tax totally erased

its profits in the state, forcing the company to discontinue its business there. Following the principle set forth in Alaska Fish Co. v. Smith, the Court upheld the Washington statute, saying,

> If a contrary conclusion were reached in the present case, it could rest upon nothing more than the single premise that the amount of the tax is so excessive that it will bring about the destruction of appellant's business, a premise which, standing alone, this court heretofore has uniformly rejected as furnishing no juridical ground for striking down a taxing act.

Magnano, 292 U.S. at 47.

The principle of Alaska Fish Co. and Magnano was reaffirmed in City of Pittsburgh v. Alco Parking Corp., 417 U.S. 369 (1974). Alco complained that Pittsburgh's 20% tax on the gross receipts of private parking lots was destroying the profitability of those businesses. Nine of the fourteen private lots in the city were rendered unprofitable and the rest made only marginal profits as a result of the tax. Id., 417 U.S. at 372. The Supreme Court of Pennsylvania ruled that the tax was unreasonably high and violated the due process clause of the Fourteenth Amendment. Relying on Alaska Fish Co. and Magnano, the U.S. Supreme Court reversed saying,

> The claim that a particular tax is so unreasonably high and unduly burdensome as to deny due process is both familiar and recurring, but the Court has consistently refused either to undertake the task of passing on the "reasonableness" of a tax that otherwise is within the power of Congress or of state legislative authorities, or to hold that a tax is unconstitutional because it renders a business unprofitable.

Id., 417 U.S. at 373.

Therefore, the taxpayers may not complain that the proposed reserves property tax violates the due process clause because it is oppressively high. The above cases demonstrate that the power to tax may well be exercised in such a way as to make a business entirely unprofitable without violating the due process clause. By comparison, the taxpayers cannot demonstrate that the proposed reserves property tax would drive them out of business. The oil industry in Alaska remains profitable despite payment of equivalent taxes under the Oil and Gas Corporate Income Tax. A due process challenge against the reserves property tax would be even less persuasive than the unsuccessful challenges in Alaska Fish Co., Magnano, and City of Pittsburgh.

d. Summary

The reserves property tax does not violate the due process clause of the Fourteenth Amendment on any of the other grounds that historically have been presented to the Supreme Court. The tax is not a special assessment and so is not held to any test of fair ratio between the benefit conferred on a taxpayer and the burden imposed. Carmichael v. Southern Coal & Coke Co., supra.

2. Excessive Assessment

The reserves property tax is to be assessed on the basis of the "full and true value" of the subject property interests. Sec. 43.58.021(a). This full and true value is

defined as the market price of the property's proven reserves, which the Department of Revenue shall determine after considering all factors affecting the value of the property, including the discounted present value of the expected future net income from the reserves. Sec. 43.58.051(b). If a taxpayer challenges the statutory discount rate, the bill provides that he bear the burden of showing that use of that discount rate would result in constructive fraud. Sec. 43.58.051(d). Each of these provisions is consistent with the United States Constitution and the Alaska Constitution and with the decisions of the respective Supreme Courts.

a. Property assessment and the fourteenth amendment

There have been several cases decided by the U.S. Supreme Court in which the methods or the result of property assessment were challenged. Generally, the challenges are grounded in the Fourteenth Amendment, though it is not always clear whether the due process clause or the equal protection clause of that amendment is the basis of the Court's holding. In either case, the Court's formula for testing the constitutionality of property assessments has remained more or less consistent. As phrased by the Court in Chicago, Burlington & Quincy Ry. Co. v. Babcock, 204 U.S. 585, 596 (1907):

> It is said that this valuation is absurd and due to misunderstanding of the table. But we have nothing to do with complaints of that nature, or with anything less than fraud, or a clear adoption of a fundamentally wrong principle.

So saying, the Court upheld Nebraska's method of assessing railroad property against a challenge founded on the Fourteenth Amendment. Nebraska's assessors had considered, among other things, the capitalization of the railroad's net earnings within the state.

In 1923, the Supreme Court considered a challenge to the assessment of a mine tailings dump. South Utah Mines & Smelters v. Beaver County, 262 U.S. 325 (1923). In that case the court found no constitutional fault with the statutory method of capitalizing the net income of a metaliferous mine to estimate its present value:

> The value of property bears a relation to the income which it affords. If it be property whose production is uniform and of indefinite duration the capitalization of the net income derived from it at the going rate of interest, in the absence of a more certain method, will furnish a reasonable measure of the value.

Id., 262 U.S. at 330. The Court said in dictum, however, that to use such a method on a tailings pile which, unlike an underground ore deposit, has no reserves hidden in the earth would result in "flagrant and palpaple injustice" and would be of doubtful constitutionality. Id., 262 U.S. at 331. Presumably a flagrant and palpaple injustice, is similar to "fraud or the clear adoption of a fundamentally wrong principle", the Fourteenth Amendment test in Chicago, Burlington & Quincy Ry. Co., though that case was not cited. South Utah Mines was decided on other grounds, that is by construing the Nebraska mine assessment statute such that it did not apply to the tailings pile. Id., 262 U.S. at 333.

The Utah legislature could constitutionally require that a fixed multiple of the net income of a mine be used to provide a "reasonable measure" of the property value, when the reserves were uncertain. Alaska proposes to use projected income figures to discount to present value oil reserves that are known to exist. This method too will produce a "reasonable measure" of the value of the reserves and is not "altogether fictitious" or a "flagrant and palpable injustice." South Utah Mines, 262 U.S. at 331.

In a second mineral valuation case, decided by the U.S. Supreme Court in 1931, petitioners claimed that the method of assessing their coal reserves violated the equal protection clause of the Fourteenth Amendment. Cumberland Coal Co. v. Board of Revision, 284 U.S. 23 (1931). The county assessors used a flat rate of $260 per acre of coal land in assessing property values, notwithstanding the well-known fact that coal close to the river was worth much more and other reserves were worth less. The result was that some properties were assessed at 100% of the value of the coal reserves and others were assessed at as little as 25% of their actual value. Id., 284 U.S. at 30. The Court held that this "intentional, systematic undervaluation by state officials of taxable property of the same class" violated the equal protection clause of the Fourteenth Amendment. Id., 284 U.S. at 28 (emphasis added). The reserves property tax proposed by Alaska will be assessed only after consi-

deration of all factors which may be known by the Department to affect the taxable value of the property, thus avoiding the problem of intentional undervaluation which was found unconstitutional in Cumberland Coal Co..

While the Cumberland Court found intentional undervaluation of some (but not all) properties in a class to be a violation of the equal protection clause of the Fourteenth Amendment, the court in Great Northern Ry. v. Weeks, 297 U.S. 135 (1936) held that intentional or fraudulent overassessment violates the due process clause of that same amendment. In Great Northern Ry. Co., the railroad company complained that North Dakota's method of assessment did not reflect the decline in property values that resulted from the Great Depression. The state's witness essentially admitted this, saying, "If all assessments had been reduced to conform to actual market value, the State and its subdivisions would have ceased to function, as the revenue would not even approximate necessary expenses." Id. 297 U.S. at 150.

Expanding on the importance of a finding of intent or fraud as part of the constitutional test, the Court said,

> Courts decline to disturb assessments for taxation unless shown clearly to transgress reasonable limits. Overvaluation is not of itself sufficient to warrant injunction against any part of the taxes based on the challenged assessment; mere error of judgment is not enough; there must be something that in legal effect is the equivalent of inten-