1122 HRES HB 963

1122

(d) No cost for the taxpayer's general overhead or administrative expense and no cost that is to be amortized or depreciated under secs. 250-260 of this chapter may be included in this section.

Authority: AS 43.05.080
AS 43.19.010 (Art. IV, sec. 18)
AS 43.21.020
AS 43.21.090

Proposed Regulation 900(31) and (32) should read:

(31) "sales delivery point" means

(1) for a taxpayer's oil and gas sold in a bona fide, arm's-length sale to a third party, the point of delivery under the terms of the contract or agreement for that sale, except in the cause of a sale to which Sec. 132(d) of this chapter applies;

(2) for a taxpayer's oil not sold in a bona fide, arm's-length sale to a third party, th gate of the refinery to which that oil is ultimately transported; and

(3) for a taxpayer's gas not sold in a bona fide, arm's-length sale to a third party, the point of delivery under the terms of the sales contract being used as the reference for the sales price of the taxpayer's gas under Secs. 122 and 124 of this chapter.

(32) "sales price" is defined in Sec. 122 of this chapter.

AGO 785825

Thomas K. Williams, Commissioner
Department of Revenue

December 4, 1979

Robert M. Johnson, Director
Petroleum Revenue Division

Required Annual Report on Income Tax

Attached for your review and recommended use are letters to the Legislature setting out an annual report of the Oil and Gas Corporate Income Tax required under AS 43.21.110(a). The report consists of text and a chart, and should presumably be sent around January 1, 1980, although no specific date is set by law.

Attachments

RMJ/rdm

AGO 785832

STATE OF ALASKA

DEPARTMENT OF REVENUE

DIVISION OF PETROLEUM REVENUE

JAY S. HAMMOND, GOVERNOR

201 E. 9th AVENUE
ANCHORAGE, ALASKA 99501
PHONE (907) 276 1363
(907) 277 5627

December 3, 1979

The Honorable Clem V. Tillion
President of the Senate
Alaska State Legislature
Pouch Y
Juneau, Alaska 99811

Oil and Gas Corporate
Income Tax Act

Dear Sir:

Pursuant to AS 43.21.110(a), I am transmitting to you an annual consolidated report of State revenues and taxation policies under the Oil and Gas Corporate Income Tax Act (AS 43.21).

The amounts reported here and collected during 1979 relate to obligations arising during Tax Year 1978. The total amounts paid by corporations under the Act and the aggregate income and deductions are set out in the attached chart.

With respect to policies under the Act during 1979, the Department has promulgated an extensive set of regulations implementing the statutes. See, 15 AAC 12.001 et seq. Modifications to certain of those regulations have been proposed. Audits of corporations subject to the Act have commenced. The Act itself is the subject of litigation in the case of ARCO et al v. State, Superior Crt No. 3 AN 79-1903.

I hope this information is useful to you.

Sincerely,

Thomas K. Williams
Commissioner

Attachment

TKW/RMJ/rdm

AGO 785833

04-D7LH

STATE OF ALASKA

DEPARTMENT OF REVENUE

DIVISION OF PETROLEUM REVENUE

JAY S. HAMMOND, GOVERNOR

201 E. 9th AVENUE
ANCHORAGE, ALASKA 99501
PHONE (907) 276-1363
(907) 277-5627

December 3, 1979

The Honorable Terry Gardiner
Speaker of the House
Alaska State Legislature
Pouch Y
Juneau, Alaska 99811

Oil and Gas Corporate
Income Tax Act

Dear Sir:

Pursuant to AS 43.21.110(a), I am transmitting to you an annual consolidated report of State revenues and taxation policies under the Oil and Gas Corporate Income Tax Act (AS 43.21).

The amounts reported here and collected during 1979 relate to obligations arising during Tax Year 1978. The total amounts paid by corporations under the Act and the aggregate income and deductions are set out in the attached chart.

With respect to policies under the Act during 1979, the Department has promulgated an extensive set of regulations implementing the statutes. See, 15 AAC 12.001 et seq. Modifications to certain of those regulations have been proposed. Audits of corporations subject to the Act have commenced. The Act itself is the subject of litigation in the case of ARCO et al v. State, Superior Crt No. 3 AN 79-1903.

I hope this information is useful to you.

Sincerely,

Thomas K. Williams
Commissioner

Attachment

TKW/RMJ/rdm

AGO 785834

04-07LH

Attachment A

		Activity in Thousands of Dollars			
		Production	Pipeline	Apportioned[1]	Total
1.	Gross Income	$5,512,723	$2,384,714	$17,305,523	$25,202,960
2.	Deductions	4,605,205	1,623,201	17,250,301	23,478,707
3.	Taxable Income	$ 907,518	$ 761,513	$ 55,222	$ 1,724,253
4.	Total Tax				$ 170,393[2]
5.	Less:				
	Payments				172,112
	Credits				2,899
6.	Total Payments and Credits				175,011
7.	Taxes Overpaid (line 6 - line 4)				4,618
8.	Less:				
	Amounts Applied To 1979 Estimated Tax				2,277
9.	Remainder Refunded To Taxpayers (line 7 - line 8)				$ 2,341

[1] The gross income reported in this column is total apportionable taxable income and the deductions represent the amount apportioned to jurisdictions other than the State of Alaska.

[2] The effective tax rate for 1978 is 9.88%, which is greater than the statutory rate of 9.4%. Because this is so, some taxpayers reported losses in 1978. Since a carryback period is not available to these taxpayers at this time, the tax impact attributable to these losses will be realized in some period subsequent to 1978. See, AS 43.21.020(d).

AGO 785835

Joseph K. Donohue, Deputy Commissioner
Department of Revenue

October 29, 1979

Robert M. Johnson, Director
Petroleum Revenue Division

Impact of Allowing Intangible Drilling Expenses as a Direct Deduction

You have asked for an analysis of the financial impact of allowing intangible drilling costs (IDCs) as a deduction to derive taxable production income under the Oil and Gas Corporate Income Tax Act (AS 43.21).

As you know, drilling costs (intangible or tangible) incurred by oil and gas producers are not specifically allowed as an operating expense deduction in deriving taxable production income. Intangible drilling costs are, however, an allowable deduction under § 263 of the Internal Revenue Code. Prior to enactment of the Oil and Gas Corporate Income Tax (AS 43.21), § 263 was incorporated by reference into the Net Income Tax Act (AS 43.20) which applied to the oil and gas producers. That incorporation by reference disappeared with enactment of AS 43.21. The law does not now specifically address IDCs, but does permit as deductions to derive oil and gas production income such items as dry hole expenses, interest expense not capitalized by the corporation up to a certain amount, and amortization of lease acquisitions. See, AS 43.21.020(b). Under the original regulations implementing that provision, "drilling costs" may be deducted to derive taxable production income only as a portion of acquisition and development costs. Those allowable costs are limited. 15 AAC 12.250 and 12.260. Operating expenses, which are generally deductible to the full extent of the expenses incurred, exclude "drilling costs."

The Department is presently proposing to promulgate regulations which would allow IDCs, as a drilling cost, to be directly deducted as an operating expense.1/ Such a change in regulations would impose a significant impact on taxes received. Our preliminary calculation of taxes paid under AS 43.21 indicates that, as an example, the 1978 tax base of $1,780,402,000 would drop by $672,653,000 or 38%.2/ The taxes produced would consequently drop by a similar percentage or approximately $63,596,000. While the tax benefit to the covered taxpayers is a decrease in tax obligations of 38% industry wide, some taxpayers, depending on their unique circumstances, would stand to save over 100% of their tax obligations (resulting in a net operating loss) while others would see only minor savings. However, a weighted average among all taxpayers clearly places the bulk of the tax savings at between 30 and 40%, as noted.

AGO 85826

1/ Whether a regulation alone can permit this change is the subject of an opinion request to the Attorney General.

2/ Because of the nature of reporting taxes, the estimates of IDCs are based only on those reported under development cost deductions. 15 AAC 12.260. There also may be IDCs claimed under the present acquisition cost deductions (15 AAC 12.250) but these figures cannot be readily extracted. However, for purposes of calculating impact, the percentage figures, ratios and adjusted tax receipts would remain about the same as estimated or would show a slightly greater benefit for the taxpayer.

AGO 785827

ALASKA STATE LEGISLATURE - HOUSE OF REPRESENTATIVES

REPRESENTATIVE JOE McKINNON
POUCH V, JUNEAU, ALASKA 99811

February 4, 1980

Thomas K. Williams, Commissioner
Department of Revenue
Pouch S
Juneau, Alaska 99811

Dear Tom:

Re: Proposed changes to 15 AAC 12; regulations on the Oil and Gas Corporate Income Tax

We are very concerned, as you know, over the proposed changes to the regulations on the Oil and Gas Corporate Income Tax (15 AAC 12). We urge you to postpone any action on these regulation changes until we have had more time to review them. Our specific concerns are the proposed changes to sections 240, 250 and 260, which provide for the direct deduction of drilling costs as operating costs. We are also concerned about allowing methods other than unit-of-production depreciation, which is the method specifically mentioned in the statutes.

During deliberations over the Oil and Gas Corporate Income Tax legislation, the Department of Revenue relied on work by Jerome M. Zeifman and Kenneth G. Ainsworth. In their January 1977 report entitled The Taxation of the Petroleum Industry Under Alaska's Corporate Income Tax, Ziefman and Ainsworth cite two major problems. The first was what they called an "eroded tax base". This was due to Federal tax subsidies historically provided to the petroleum industry. The second problem was that Alaska was using an apportionment formula, which did not fairly reflect the true amount of business being done in the state.

Both these problems stemmed from the fact that Alaska had delegated to Congress the responsibility for determining the corporate income tax base. By adopting certain provisions of the Internal Revenue Code, the State was inadvertently

adopting Federal deductions designed as tax subsidies. The most notable of these, as Ziefman and Ainsworth pointed out, was the "expensing of intangible drilling costs." Furthermore, by adopting an apportionment formula based on the Uniform Division of Income for Tax Purposes Act, the State was not taxing the petroleum industry on a manner which truly reflected their profits made in the State. The effect, as stated by Richard Kilgore of the Walter J. Levy Consultants Corporation before a joint House-Senate Resources Committee hearing on March 21, 1977, was "an effective rate of taxation instead of something like 9.4% a rate of taxation, roughly a quarter of that, two to two and a half percent."

That the intent of SCS CSHB 322 was to solve both of these problems is clear. In a letter dated July 5, 1978 to the House Speaker and Senate President, Governor Hammond wrote:

> Oil and gas corporations have been paying an effective tax rate substantially below the nominal tax rate of 9.4 per cent and substantially below what other local corporations would pay on the same income earned on the same assets in the state. The passage of this bill culminates three years of joint effort by the executive and legislative branches to rectify substantial defects in the former taxation scheme which, by incorporating various federally available tax loopholes and by using an inappropriate apportionment formula, allowed oil and gas corporations to avoid their fair share of the state tax burden. (1978 House Journal Final Supplement, p. 13).

To now reincorporate the "federally available tax loophole" of expensing of intangible drilling costs by regulation appears to be directly in conflict with the intent of AS 43.21. (ch 110 SLA 1978).

Plus, the fact that this proposed change to the regulations is of questionable legality is evident in the request for a legal opinion from Joseph K. Donohue, Deputy Commissioner of Revenue to Wilson Condon, Deputy Attorney General, dated November 2, 1979. The Department of Revenue claims the question of law centers around an interpretation of AS 43.21.020(c)(4), which defines operating expenses allowed as direct deductions. Under AS 43.21.020(c)(4), there is no specific reference to drilling costs. The Department has apparently mistakenly concluded that if drilling cost are not indirect costs, they may be deducted.

We would like to bring to the Department's attention AS 43.21.020(c)(8) which provides the only reference in the statutes which directly relates to "drilling costs." This subsection explicitly states that "dry hole" costs are allowed as direct deductions. We emphasize here that this apples only to "dry hole" costs and not drilling costs per se.

Returning to the legislative history on taxes in general, it is clear that SCS CSHB 322 was not the first attempt to rid the state tax base of "federally available tax loopholes." On February 25, 1975, Governor Hamm . wrote to the House Speaker regarding HB 208:

> I am submitting this bill for the purpose of closing certain corporate tax loopholes. The bill would eliminate the foreign tax credit, the depletion allowance, and the exemptions for domestic international sales corporations (DISC), and would place a limit on the amount of investment credit for Alaska income tax purposes. (1975 House Journal 295).

After the passage of CSHB 208 (Fi .. am S (ch 153 SLA 1975), the only other significant "tax loophole" left was expensing of intangibles.

We understand that a large measure of your concern arises from the current lawsuit over AS 43.21. We believe that many of the complaints in the lawsuit can be rendered moot by changes to the statutes which will have little impact on revenue. We remind you of the letter the Attorney General wrote to Governor Hammond on June 22, 1978, in which Avrum Gross concluded, that:

> We herefore simply reiterate our advice to the Department of Revenue and state that, in our view there are no constitutional or legal issues which would be fatal to the implementation of the new income tax.

I think you can understand our concerns. We are available at any time to discuss them with you further, and also to work with you on statutory changes to which address substantive legal points concerning the lawsuit over AS 43.21. Please send us a copy of the latest annual consolidated

report of state revenues and taxation policies required under AS 43.21.110.

Sincerely,

Joe McKinnon

cc: Joseph K. Donohue, Deputy Commissioner of Revenue
Rob Johnson, Director, Div. of Petroleum Revenue
Representative Terry Gardiner
Representative Russ Meekins

STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

DEPARTMENT OF REVENUE

DIVISION OF PETROLEUM REVENUE

201 E. 9th AVENUE
ANCHORAGE, ALASKA 99501
PHONE (907) 276-1363
(907) 277-5627

January 31, 1980

The Honorable Joseph H. McKinnon
Alaska House of Representatives
Pouch Y, State Capitol
Juneau, Alaska 99811

Attn: Bob Williams

Re: Income Tax Regulations

Dear Sir:

Attached as requested by your staff is a copy of statements submitted by the petroleum industry at recent hearings on Oil and Gas Corporate Income Tax regulations.

Sincerely,

Robert M. Johnson
Director

Attachments

RMJ/rdm

04-D7LH

AGO 785836

Comments By Mark I. Hazelwood
On Behalf of the Alaska Oil and Gas Association
At Hearings On Proposed Alaska Oil and Gas Corporate
Income Tax Regulations
Anchorage, Alaska
January 24, 1980

Introduction

My name is Mark L. Hazelwood and I am an attorney in the Tax Department of Atlantic Richfield Company. I have been requested by the Alaska Oil and Gas Association (AOGA) to present the Association's views regarding the proposed regulations issued by the Department of Revenue on December 17, 1979 to amend existing regulations under Chapter 21 of Title 43 of the Alaska Statutes, the Alaska Oil and Gas Corporate Income Tax.

Inasmuch as the Alaska income tax has a significant impact on our industry's activities in the stat   we tru t that our testimony at this hearing will evidence our continuing interest and concern not only with respect to the subject matter covered in the proposed regulations but also all other aspects of the oil and gas corporate income tax.

AOGA recognizes the difficulties associated with implementing this tax law, considering its unique and complex nature, and commends your efforts to draft and adopt, within the parameters of the existing law, well-reasoned regulations. We welcome the opportunity to present our views at this hearing and hope that our comments and suggestions will be of assistance to the

AGO 785837

Department in promulgating final regulations.

The Association, by participating in this hearing, does not concede, however, that the corporate income tax law as enacted in Chapter 21 is constitutional or otherwise legal In our opinion, Chapter 21 as enacted is unconstitutional because it results in impermissible duplicative taxation and an improper burden on interstate commerce in violation of the Commerce Clause of the United States Constitution and because it violates the restrictions on extraterritorial taxation embodied in the Due Process Clause of the Fourteenth Amendment of the United States Constitution and Article I, Section 7 of the Alaska Constitution. Furthermore, we believe Chapter 21 unlawfully discriminates against members of this Association by subjecting them to a method of taxation more burdensome than that imposed on any other industry in the state thereby violating the Equal Protection of the Laws and the Due Process Clauses of the United States and Alaska Constitutions. Accordingly, our comments and suggestions are offered with the understanding that participation in this hearing will not prejudice any rights of the Association or any of its members in any court or other proceeding to contend that Chapter 21 and the regulations adopted pursuant thereto are unconstitutional or invalid.

AGO 785838

AOGA'S OBJECTIVE AT THIS HEARING IS TO ASSIST THE DEPARTMENT IN THE DEVELOPMENT OF REGULATIONS WHICH (1) WOULD RESULT IN A FAIR AND EQUITABLE INTERPRETATION OF THE STATUTE CONSISTENT WITH LEGISLATIVE INTENT, (2) WOULD PROMOTE EASE OF ADMINISTRATION TO ALLOW EACH TAXPAYER TO DISCHARGE ITS INCOME TAX LIABILITY WITH A REASONABLE DEGREE OF CERTAINTY BASED ON INFORMATION AVAILABLE TO THE TAXPAYER AND (3) WOULD AVOID THE PROSPECT OF FURTHER CONTROVERSY BETWEEN OUR INDUSTRY AND THE STATE OF ALASKA.

MOST OF OUR TESTIMONY TODAY WILL BE DEVOTED TO COMMENTS AND SUGGESTED CHANGES PERTAINING TO SPECIFIC SECTIONS OF THE PROPOSED REGULATIONS. WE DO NOT INTEND, HOWEVER, TO ADDRESS IN OUR ORAL TESTIMONY SUGGESTED WORD CHANGES WHICH ARE BELIEVED NOT TO BE OF A CONTROVERSIAL OR SUBSTANTIVE NATURE.

BEFORE TURNING TO THE PROPOSED REGULATIONS, WE FIRST WOULD LIKE TO MAKE TWO COMMENTS RELATIVE TO OUR OVERALL ASSESSMENT OF THE PROPOSED REGULATIONS. FIRST, AOGA IS DEEPLY CONCERNED ABOUT CERTAIN PROPOSED CHANGES TO THE DETERMINATION OF GROSS VALUE AT THE POINT OF PRODUCTION FOR A TAXPAYER'S OIL AND GAS. THE PROPOSED REGULATIONS PRESENT SERIOUS QUESTIONS CONCERNING (1) THE CONCEPT OF PREVAILING VALUE AS EMPLOYED BY THE DEPARTMENT ESPECIALLY WITH RESPECT TO ITS SCOPE OF APPLICATION, AND (2) THE POTENTIAL TAXATION OF ARTIFICIALLY CREATED INCOME IN CONTRAVENTION OF WELL-ESTABLISHED PRINCIPLES OF STATE INCOME

AGO 785839

TAXATION. SUCH SERIOUS QUESTIONS, IF LEFT UNADDRESSED, INVITE CONTROVERSY AND INCREASE THE POTENTIAL OF FUTURE LITIGATION. WE BELIEVE CHANGES CAN BE MADE TO ELIMINATE THESE POTENTIAL PROBLEMS IN A MANNER WHICH IS CONSISTENT WITH THE UNDERLYING INTENT OF THE STATUTE AND WITH THE BEST INTERESTS OF BOTH THE STATE AND OUR INDUSTRY.

SECOND, AOGA IS ENCOURAGED BY THE DEPARTMENT'S ACTION IN PROPOSING REGULATIONS WHICH SPECIFICALLY AUTHORIZE DEDUCTIONS FROM BOTH GROSS PRODUCTION INCOME AND PIPELINE OPERATING REVENUES SIMILAR TO DEDUCTIONS ALLOWED TAXPAYERS UNDER CHAPTER 20, TITLE 43 OF THE ALASKA STATUTES. THIS IS CONSISTENT WITH THE STATUTE AND REPRESENTS A SIGNIFICANT STEP TOWARD MITIGATING THE DISCRIMINATORY TAXATION TO WHICH THE OIL AND GAS INDUSTRY CURRENTLY IS SUBJECTED EVEN THOUGH SUCH PROPOSALS AFFECT ONLY THE TIMING OF PAYMENT BUT NOT THE TOTAL AMOUNT OF TAXES ULTIMATELY TO BE PAID TO THE STATE OF ALASKA.

FOR THE CONVENIENCE OF THE DEPARTMENT, WE WOULD LIKE TO PRESENT COPIES OF OUR SUGGESTED CHANGES TO THE PROPOSED REGULATIONS AT THIS TIME. COPIES OF OUR TESTIMONY WILL BE FURNISHED AT THE CONCLUSION OF THIS PRESENTATION.

THIS CONCLUDES OUR INTRODUCTORY REMARKS AND I NOW WOULD LIKE TO BEGIN OUR DETAILED TESTIMONY WITH SECTION 120, "VALUE AT THE POINT OF PRODUCTION."

AGO 785840

SECTION 120

WE BELIEVE THAT SUBSECTION (A) OF SECTION 120 IS NOT NECESSARY AND IS SOMEWHAT MISLEADING AND CONFUSING IN THE CONTEXT OF AN INCOME TAX. ACCORDINGLY, WE ARE SUGGESTING THAT IT BE DELETED AND THE SUBSEQUENT SUBSECTIONS RE-LETTERED.

THE GENERAL APPROACH OF THE REGULATIONS IS TO BEGIN WITH THE PRICE OR OTHER VALUE IN THE MARKET AND NET BACK TO THE POINT OF PRODUCTION BY AN ALLOWANCE FOR TRANSPORTATION COSTS AND, IN THE CASE OF GAS, CERTAIN OTHER COSTS. SUBSECTION (B) OF THE PROPOSED REGULATIONS REFLECTS THIS GENERAL APPROACH WHERE THE VALUE IS BASED ON THE SALES PRICE. IN THE DEPARTMENT'S PROPOSED REGULATIONS, PREVAILING VALUE AT THE POINT OF USE MAY BE SUBSTITUTED FOR SALES PRICE UNDER CERTAIN CIRCUMSTANCES. WE BELIEVE THAT APPROPRIATE LANGUAGE SHOULD BE INSERTED IN PARAGRAPH (1) TO REFLECT THE NETBACK CONCEPT IN SITUATIONS WHERE PREVAILING VALUE IS USED. OUR SUGGESTED LANGUAGE IS CONTAINED IN THE INDUSTRY DRAFT YOU HAVE BEFORE YOU.

A BRIEF EXPLANATION OF OUR SUGGESTED LANGUAGE IS IN ORDER. UNDER THE PROPOSED REGULATIONS, PREVAILING VALUE IS DETERMINED AT THE POINT OF USE OF THE OIL IN THE REFINING PROCESS. ANY NETBACK NECESSARILY MUST REFLECT TRANSPORTATION COSTS FROM THE POINT OF PRODUCTION TO THE POINT OF USE. IT WILL NOT ALWAYS BE TRUE THAT THE POINT OF DELIVERY BY THE SELLER WILL BE THE POINT

AGO 785841

OF USE. THUS, IT IS NECESSARY THAT THE REASONABLE COSTS OF TRANSPORTATION ADJUSTMENT BE WORDED TO REFLECT A PROPER ALLOWANCE FOR ALL TRANSPORTATION, WHETHER PAID FOR BY THE SELLER OR ANOTHER PARTY. A SIMPLE EXAMPLE WILL ILLUSTRATE. IN A THIRD PARTY SALE CALLING FOR DELIVERY AT THE PORT OF VALDEZ THE PRICE THE PURCHASER WOULD PAY WOULD TAKE INTO ACCOUNT HIS COST OF TRANSPORTATION FROM THAT POINT TO THE INLET OF THE REFINERY. LIMITING THE COST OF TRANSPORTATION ADJUSTMENT TO TRANSPORTATION FROM THE WELL TO VALDEZ CLEARLY WOULD NOT ADEQUATELY REFLECT ALL TRANSPORTATION COSTS FROM THE POINT OF PRODUCTION TO THE INLET OF THE REFINERY. WE BELIEVE THE SUGGESTED LANGUAGE WILL APPROPRIATELY PERMIT A PROPER ADJUSTMENT FOR ALL TRANSPORTATION.

THE TAX IMPOSED UNDER CHAPTER 21 IS GENERALLY RECOGNIZED AS AN INCOME TAX. WE SEE NO REASON OR STATUTORY BASIS FOR THE FLOOR INSERTED AS PARAGRAPH (2) IN THE PROPOSED REGULATION. WE FURTHER BELIEVE THAT ITS INCLUSION WOULD RAISE SERIOUS CONSTITUTIONAL IMPLICATIONS IN VIEW OF THE NATURE OF THIS TAX. ACCORDINGLY, WE SUGGEST THAT IT BE STRICKEN.

WE TURN NOW TO ONE OF THE MOST IMPORTANT PARTS OF OUR PRESENTATION TODAY, NAMELY THE CONCEPT OF PREVAILING VALUE AND ITS PLACE, IF ANY, IN THE ADMINISTRATION OF AN INCOME TAX LAW. SUBSECTION (C) OF THE PROPOSED REGULATIONS ADDRESSES THE QUESTION OF WHEN PREVAILING VALUE APPLIES.

WE CANNOT URGE TOO STRONGLY OUR BELIEF THAT PREVAILING VALUE AS A CONCEPT HAS NO PLACE IN INCOME TAX LAW. THE TAX, UNDER CHAPTER

AGO 785842

21, WHICH IS IMPOSED AS AN INCOME TAX, MUST BE BASED IN ALL INSTANCES ON INCOME ACTUALLY REALIZED BY THE TAXPAYER AND NOT ON ARTIFICIALLY CREATED INCOME. WE ARE PARTICULARLY CONCERNED ABOUT THE APPLICATION OF ANY SUCH STANDARD AS PREVAILING VALUE ON A HINDSIGHT BASIS YEARS AFTER THE FACT. THIS IS PARTICULARLY TRUE IN TODAY'S MARKET WHERE PRICES MOVE RAPIDLY AND PROBABLY NOT IN ANY DISCERNABLE AND EASILY DEFINED PATTERN. WE BELIEVE THAT ANY SIGNIFICANT RELIANCE ON PREVAILING VALUE RAISES SUBSTANTIAL CONSTITUTIONAL QUESTIONS.

THE ASSOCIATION RECOGNIZES, HOWEVER, THAT THE DEPARTMENT IS CHARGED WITH THE RESPONSIBILITY OF PROMULGATING REGULATIONS WHICH DETERMINE A UNIFORM METHOD OF ESTABLISHING GROSS VALUE AT THE POINT OF PRODUCTION, AND THAT ONE OF THE OPTIONS AFFORDED BY THE GOVERNING LEGISLATION IS TO CONSIDER PREVAILING PRICE OR VALUE. IF PREVAILING VALUE IS TO BE RECOGNIZED IN THE REGULATIONS AT ALL, ITS USE SHOULD BE ON AN EXCEPTION BASIS ONLY. WE ARE CONCERNED, HOWEVER, THAT YOUR LANGUAGE MAY BE APPLIED INDISCRIMINATELY AND RESULT, FOR EXAMPLE, IN THE EXAMINATION OF EVERY TRANSACTION AGAINST A HYPOTHETICAL PREVAILING VALUE STANDARD. THE RESULT WOULD BE ENDLESS DISPUTES WITH TAXPAYERS ON A TRANSACTION BY TRANSACTION BASIS IRRESPECTIVE OF WHETHER THE TAXPAYER HAS FULLY AND CORRECTLY RECORDED AND REPORTED ITS REALIZATION FROM THE TRANSACTION.

THE PROPOSED REGULATIONS RELY ON A TWO PART TEST, WHICH

AGO 785843

INVOLVES (I) A PRICE SUBSTANTIALLY LOWER THAN THE DEPARTMENT'S DETERMINATION OF PREVAILING VALUE AT THE POINT OF USE AND (II) THE EXISTENCE OF ONE OF FOUR CONDITIONS. WE DO NOT BELIEVE THAT THE FIRST THREE CONDITIONS REPRESENT REALISTIC TESTS. FURTHERMORE, AS PREVIOUSLY MENTIONED, WE FEEL THAT YOUR PROPOSAL WILL, IN APPLICATION, CAUSE YOUR AUDITORS TO TEST TRANSACTIONS AGAINST THE PREVAILING VALUE STANDARD AND THEN TO DETERMINE WHETHER ONE OF THE FOUR CONDITIONS APPLIES OR MIGHT APPLY. THIS APPROACH IS UNREALISTIC AND SHOULD BE OF ADMINISTRATIVE CONCERN TO THE DEPARTMENT.

THE ASSOCIATION IS CONVINCED THAT THE STATE WOULD BE ADEQUATELY PROTECTED BY LANGUAGE PERMITTING THE APPLICATION OF PREVAILING VALUE ONLY WHERE THE CIRCUMSTANCES SHOW FRAUD OR AN INTENT TO EVADE TAXES. AOGA'S SUGGESTED CHANGES SO PROVIDE.

WE RECOGNIZE THE DEPARTMENT'S RESPONSIBILITY TO AUDIT A TAXPAYER'S RETURN AND TO DETERMINE THAT THE RETURN PROPERLY REFLECTS THE AMOUNTS ACTUALLY REALIZED IN THE TAXPAYER'S TRANSACTIONS. AOGA IS CONCERNED, HOWEVER, THAT IF THE APPLICATION OF THE REGULATIONS GOES BEYOND ACTUAL REALIZATION OF INCOME AND THUS VIOLATES THE CONCEPTS OF INCOME TAXATION, THERE WILL BE FREQUENT AND SERIOUS CONFLICTS BETWEEN THE INDUSTRY AND THE STATE.

OUR FINAL COMMENT WITH RESPECT TO SECTION 120

AGO 785844

RELATES TO SUBSECTION (D). THE SAME LANGUAGE IS CONTAINED IN SECTION 110 OF THE EXISTING REGULATIONS. TO AVOID DUPLICATION WE SUGGEST THAT SUBSECTION (D) BE STRICKEN.

SECTION 122

THE ASSOCIATION HAS NO COMMENTS WITH RESPECT TO SECTION 122 OF THE PROPOSED REGULATIONS OTHER THAN THE SUGGESTED TECHNICAL CHANGE AT THE END OF SUBSECTION (B)(1).

SECTION 124

AS WE STATED EARLIER IN OUR TESTIMONY, THE BASIC CONCEPT EMPLOYED IN THE REGULATIONS IS TO DETERMINE GROSS VALUE AT THE POINT OF PRODUCTION BY A NETBACK FROM THE POINT OF SALE OR USE. PREVAILING VALUE IS A SUBSTITUTE FOR SALES PRICE AND ITS DETERMINATION SHOULD NOT INVOLVE A NETBACK CALCULATION. TO CONFORM WITH SECTION 122, AND TO BE CONSISTENT WITH THIS CONCEPT, WE SUGGEST THAT THE LANGUAGE RELATING TO REASONABLE COSTS OF TRANSPORTATION IN SUBSECTIONS (A) AND (B) OF THE PROPOSED REGULATIONS BE DELETED.

SECTION 130

SECTION 130 OF THE PROPOSED REGULATIONS SPECIFIES TWO METHODS FOR DETERMINING THE REASONABLE COSTS OF TRANSPORTATION WHICH MAY BE DEDUCTED IN ARRIVING AT THE GROSS VALUE AT THE

AGO 785845

POINT OF PRODUCTION. EXCEPT IN UNUSUAL CIRCUMSTANCES, THE PROPOSED REGULATIONS WILL LIMIT THE TAXPAYER'S TRANSPORTATION DEDUCTION TO THE ACTUAL COSTS DETERMINED UNDER SECTION 132. IN CASES WHERE THE UNUSUAL CONDITIONS SET FORTH IN SECTION 130(B) EXIST, THE TRANSPORTATION DEDUCTION WILL BE THE FAIR MARKET VALUE OF SUCH TRANSPORTATION DETERMINED IN THE MANNER PRESCRIBED IN SECTION 132. AS A PRACTICAL MATTER, ACTUAL COSTS WILL BE REQUIRED TO BE USED IN MOST, IF NOT ALL, CASES.

WE BELIEVE THAT TAXPAYERS SHOULD BE PERMITTED AN ELECTION TO USE FAIR MARKET VALUE IN LIEU OF ACTUAL COSTS. OUR PROPOSED LANGUAGE WOULD PROVIDE THE TAXPAYER WITH AN ELECTION WHICH COULD BE CHANGED ONLY UPON APPROVAL BY THE DEPARTMENT. WE THINK THIS CHANGE IS NECESSARY TO PREVENT THE INCOME (OR LOSS) OF THE TAXPAYER'S MARINE TRANSPORTATION OPERATIONS FROM IMPROPERLY INCREASING (OR DECREASING) THE GROSS VALUE AT THE POINT OF PRODUCTION. THE INCLUSION OF VALUE ADDED BY MARINE TRANSPORTATION IN THE GROSS VALUE AT THE POINT OF PRODUCTION IS INCONSISTENT WITH THE SEPARATE ACCOUNTING CONCEPT FOR TAXATION OF OIL AND GAS PRODUCTION INCOME UNDER CHAPTER 21.

THE PROVISION FOR A REASONABLE RATE OF RETURN ON THE ACQUISITION COST OF A VESSEL OVER ITS EXPECTED LIFE DOES NOT, IN AND OF ITSELF, REFLECT THE CURRENT INCOME ATTRIBUTABLE TO A VESSEL'S OPERATION. FURTHERMORE, THE INCLUSION OF VESSEL FACTOR DATA IN THE FACTORS USED TO APPORTION ALL OTHER INCOME

AGO 185846

OF THE TAXPAYER SIMPLY COMPOUNDS THE INEQUITY. OUR PROPOSED LANGUAGE WOULD PROVIDE A TAXPAYER WITH AN ELECTION TO ADOPT THE FAIR MARKET VALUE APPROACH TO AVOID INCLUDING ANY INCOME (OR LOSS) ATTRIBUTABLE TO MARINE TRANSPORTATION IN THE GROSS VALUE AT THE POINT OF PRODUCTION CALCULATION AND WOULD HELP TO REDUCE FUTURE CONTROVERSIES IN THIS AREA. WHILE THE ARGUMENT FOR SUCH AN ELECTION HAS BEEN MADE BEFORE IN A PRODUCTION TAX CONTEXT, THE PRINCIPLE IS EVEN MORE SOUND IN AN INCOME TAX CONTEXT.

SECTION 132

WITH RESPECT TO SECTION 132 OF THE REGULATIONS, WE HAVE SEVERAL CHANGES TO SUGGEST. AOGA BELIEVES THE LIMITING LANGUAGE IN SUBPARAGRAPH (B) OF SUBSECTION (B)(3) SHOULD BE REMOVED BECAUSE IT IS NEITHER LOGICAL NOR EQUITABLE TO LIMIT POSITIONING COSTS TO ONE SIDE OF A TRANSACTION IF THE TAXPAYER IS OBLIGATED BY THIRD PARTY CONTRACT TO PAY POSITIONING COSTS UPON CESSATION OF USE OF A VESSEL IN THE ALASKA TRADE. MOREOVER, THE LANGUAGE WHICH WE SUGGEST BE DELETED IS INCONSISTENT WITH THE DEFINITION OF THE TERM "POSITIONING COST" SET FORTH IN SUBSECTION (G).

IN SUBPARAGRAPH (D)(I) OF SUBSECTION (B)(3), THE ASSOCIATION FEELS IT IS IMPORTANT THAT THE WORDS "BUT NOT", WHICH EXPRESSLY PROHIBIT THE INCLUSION OF COSTS OF IMPROVEMENTS IN THE DEFINITION OF "ACQUISITION COSTS", BE DELETED. TO DIFFERENTIATE BETWEEN ACQUISITION COSTS AND COSTS OF IMPROVEMENTS FOR PURPOSES OF CALCULATING DEPRECIATION AND RETURN ON INVESTMENT IS ILLOGICAL, INEQUITABLE AND INCONSISTENT WITH THE STATE'S

AGO 785847

POLICY OF ENCOURAGING, IF NOT MANDATING, THE RETROFITTING AND FURTHER IMPROVEMENT OF TANKERS USED IN THE ALASKA TRADE. THIS PROVISION NOT ONLY DENIES THE TAXPAYER A RETURN ON ITS INVESTMENT IN IMPROVEMENTS, BUT ALSO DENIES THE TAXPAYER ANY DEPRECIATION ON THOSE IMPROVEMENTS BECAUSE OF THE INTERRELATIONSHIP OF THE DEPRECIATION AND RATE OF RETURN PROVISIONS OF THE REGULATIONS. WE CAN SEE NO RATIONALE FOR EXCLUDING THESE COSTS FROM THE CALCULATION OF REASONABLE TRANSPORTATION COSTS AND URGE THE REMOVAL OF THE LIMITATION. UNDER OUR SUGGESTED LANGUAGE, ANY DEPRECIATION OR RETURN ON INVESTMENT ALLOWED THE TAXPAYER WOULD BE LIMITED TO THAT WHICH IS ATTRIBUTABLE SOLELY TO THE EMPLOYMENT OF THE VESSEL IN THE ALASKA TRADE. FOR THE SAME REASONS NOTED ABOVE, WE HAVE INSERTED SIMILAR SUGGESTED CHANGES TO THE PROVISIONS COVERING THE TRANSPORTATION OF LNG.

WITH RESPECT TO SUBSECTION (C) OF SECTION 132, WE SUGGEST THAT THE TERMS "AND (C)" BE ADDED FOLLOWING THE REFERENCE TO SECTION 130(B) TO CONFORM WITH OUR EARLIER SUGGESTION REGARDING THAT SECTION. WE ALSO SUGGEST THAT THE REGULATIONS PROVIDE THAT THE DEPARTMENT MAY AUTHORIZE TAXPAYERS TO USE ONE OF THE TWO METHODS FOR DETERMINING THE FAIR MARKET VALUE OF LIKE TRANSPORTATION. IN OUR PROPOSED SUBPARAGRAPH (A), WE HAVE ADDED LANGUAGE THAT WOULD MAKE CLEAR THAT THE THIRD PARTY CHARTERS UTILIZED FOR COMPARISON PURPOSES WOULD BE CHARTERS OF "LIKE VESSELS". IN OUR PROPOSED SUBPARAGRAPH (B), WE ARE SUGGESTING THE ADDITION OF AN ALTERNATIVE APPROACH WHICH WOULD UTILIZE

AGO 785848

RATES PUBLISHED BY THE ASSOCIATION OF SHIPBROKERS AND AGENTS, U.S.A., INC. WE BELIEVE EITHER OF THESE STANDARDS SHOULD BE AVAILABLE FOR USE, WITH THE PERMISSION OF THE DEPARTMENT, IN DETERMINING FAIR MARKET VALUE FOR MARINE TRANSPORTATION.

AGO 785849

SECTION 240

IN PRIOR HEARINGS, THE ASSOCIATION HAS ADVOCATED THAT COSTS INCURRED FOR AND IN SUPPORT OF DRILLING CONSTITUTE PROPER ITEMS OF DIRECT OPERATING COSTS UNDER THE STATUTE. WE ARE PLEASED TO NOTE THAT SECTION 240 OF THE PROPOSED REGULATIONS EXPRESSLY AUTHORIZES DEDUCTION OF THESE COSTS. WITH RESPECT TO SECTION 240(c) AS PROPOSED, WE HAVE SUGGESTED THE ADDITION OF TWO ITEMS TO BE INCLUDED AS DIRECT OPERATING COSTS AFTER COMMENCEMENT OF COMMERCIAL PRODUCTION. IN THE ASSOCIATION'S SUGGESTED LANGUAGE, THESE APPEAR AS PARAGRAPHS (1) AND (2) OF SECTION 240(c).

PARAGRAPH (1) SIMPLY ADDS THE COSTS OF GEOLOGICAL AND GEOPHYSICAL WORK CONDUCTED ON THE LEASE OR PROPERTY AND IS, IN ESSENCE, SIMPLY AN EXTENSION OF THE SAME TYPE OF DEDUCTION ALLOWED UNDER SUBSECTION(B)(1) WHEN SUCH WORK IS DONE PRIOR TO COMMENCEMENT OF COMMERCIAL PRODUCTION. WE SEE NO REASON FOR ALLOWING THESE TYPES OF COSTS BEFORE COMMERCIAL PRODUCTION COMMENCES WHILE NOT ALLOWING THEM AFTER COMMERCIAL PRODUCTION COMMENCES. ALTHOUGH IT IS PROBABLY TRUE THAT MOST OF THIS TYPE OF WORK OCCURS PRIOR TO THE COMMENCEMENT OF COMMERCIAL PRODUCTION, IT IS NOT UNCOMMON FOR A TAXPAYER TO ENGAGE IN "G&G" WORK ON A LEASE OR PROPERTY TO TEST CONDITIONS FOR OTHER POTENTIAL PRODUCTION THAT MIGHT EXIST AT DIFFERENT DEPTHS OR IN DIFFERENT AREAS FROM THE EXISTING PRODUCTION.

PARAGRAPH (2) OF SECTION 240(c) MERELY ADDS RENTALS

AGO 785850

AND SHUT-IN ROYALTIES AS A DEDUCTIBLE COST. THE PROVISION BEING ADDED IS IN FACT IDENTICAL TO THE LANGUAGE OF PARAGRAPH (2) OF SECTION 240(B). AS IN THE CASE OF "G&G" WORK, WE SEE NO REASON WHY THIS ITEM SHOULD NOT ALSO BE DEDUCTIBLE AFTER COMMENCEMENT OF COMMERCIAL PRODUCTION. A LEASE AGREEMENT COULD PROVIDE FOR SHUT-IN ROYALTIES AND, WHILE IT MAY NOT BE A VERY COMMON SITUATION, THESE COULD BECOME PAYABLE IN THE EVENT OF AN EXTRAORDINARY SHUT-DOWN OF PRODUCTION.

OTHER THAN THE TWO CHANGES JUST NOTED, OUR DRAFT MAKES VERY MINOR CHANGES IN WORDING TO THE REMAINDER OF PROPOSED SECTION 240(C).

SECTION 250

ALTHOUGH SECTION 250 WAS NOT CONTAINED IN THE PROPOSED REGULATIONS, AOGA IS SUGGESTING THE ADDITION OF LANGUAGE TO SECTION 250(G)(2). EXCEPT FOR THE WORDS "NOT DEDUCTED UNDER SEC. 240 OF THIS CHAPTER", THIS PROVISION IS IDENTICAL TO SECTION 250(G)(2) OF THE EXISTING REGULATIONS. THIS PROVISION, WITH THE ADDED WORDS, HAS BEEN INSERTED TO ENSURE THAT ANY DRILLING COSTS NOT DEDUCTED UNDER SECTION 240 WILL REMAIN AS A PART OF THE "ACQUISITION COSTS" OF A LEASE OR PROPERTY AND BE SUBJECT TO A DEDUCTION FOR ABANDONMENT OR AMORTIZATION UNDER SECTION 250.

AGO 785851

SECTION 260

SECTION 260 OF THE PROPOSED REGULATIONS PERTAINS TO THE DEDUCTION FOR DEVELOPMENT COSTS. SUBSECTION (c) OF THE REGULATION PROVIDES THAT AFTER THE COMMENCEMENT OF COMMERCIAL PRODUCTION THE TAXPAYER'S DEVELOPMENT COSTS FOR A LEASE OR PROPERTY MUST BE DEPRECIATED. THE PROPOSED REGULATIONS CONTAIN SEVERAL CHANGES IN THE METHODOLOGY HERETOFORE ALLOWED IN DETERMINING THE TAXPAYER'S DEPRECIATION DEDUCTION FOR DEVELOPMENT COSTS. THESE PROPOSED CHANGES ARE CONSISTENT WITH THE AUTHORITY GRANTED THE DEPARTMENT UNDER A.S. 43.21.020(c)(5). ALTHOUGH WE ARE SUPPORTIVE OF THE DEPARTMENT'S OBJECTIVES IN MAKING THE PROPOSED CHANGES, WE OFFER THE FOLLOWING COMMENTS AND SUGGESTIONS FOR YOUR CONSIDERATION.

IT FIRST SHOULD BE RECOGNIZED THAT, ALTHOUGH THE DEDUCTION FOR DEPRECIATION IS DERIVED FROM A MATHEMATICAL FORMULA, THERE ARE A MYRIAD OF INTRICACIES RELATING TO THE APPLICATION OF SUCH A FORMULA THAT CAN LEAD TO COMPLEX PROBLEMS. ACCORDINGLY, EXTREME CARE MUST BE EXERCISED SO AS TO ENSURE THAT INTENDED RESULTS ARE ACHIEVED. AS WRITTEN, THE PROPOSED REGULATION COULD LEAD TO UNINTENDED RESULTS. FOR EXAMPLE, THE REGULATIONS CORRECTLY DESCRIBE THE MANNER OF COMPUTING DEPRECIATION UNDER THE UNIT OF PRODUCTION, SUM OF THE YEARS-DIGITS, DOUBLE DECLINING BALANCE AND STRAIGHT-LINE METHODS OF DEPRECIATION. HOWEVER, THESE METHODS, WHEN USED IN

AGO 785852

CONJUNCTION WITH THE OTHER PROVISIONS OF SECTION 260, POSE SIGNIFICANT PROBLEMS.

ONE PROBLEM ARISES FROM THE FACT THAT THE PROPOSED REGULATION IMPLICITLY, IF NOT EXPLICITLY, PROVIDES FOR A SINGLE OPEN-ENDED COMPOSITE ACCOUNT FOR PURPOSES OF COMPUTING DEPRECIATION. A COMPOSITE ACCOUNT IS ONE WHICH INCLUDES ALL THE ASSETS OF A BUSINESS IN ONE DEPRECIATION ACCOUNT. THE COMPOSITE ACCOUNT PROVIDED FOR IN THE PROPOSED REGULATIONS IS OPEN-ENDED BECAUSE IT INCLUDES ON A CUMULATIVE BASIS DEVELOPMENT COSTS THAT MAY HAVE BEEN INCURRED OVER SEVERAL TAXABLE YEARS. THE USE OF AN OPEN-ENDED COMPOSITE ACCOUNT CAN LEAD TO SUBSTANTIAL PROBLEMS IN DETERMINING THE DEPRECIATION DEDUCTIONS ALLOWED UNDER THE SUM OF THE YEARS-DIGITS, DOUBLE DECLINING BALANCE AND STRAIGHT-LINE METHODS OF DEPRECIATION BECAUSE THE ESTIMATED REMAINING LIFE OF THE COMPOSITE ACCOUNT IS CONSTANTLY CHANGING. FURTHERMORE, THE USE OF AN OPEN-ENDED ACCOUNT CAN RESULT IN MUCH HIGHER DEPRECIATION DEDUCTIONS THAN DEDUCTIONS CALCULATED USING CLOSED-END ACCOUNTS. A CLOSED-END OR "VINTAGE" COMPOSITE ACCOUNT IS AN ACCOUNT WHICH WOULD INCLUDE ALL OF THE TAXPAYER'S DEVELOPMENT COSTS FIRST ELIGIBLE FOR DEPRECIATION IN A PARTICULAR TAXABLE YEAR.

AS AN EXAMPLE OF THE DIFFERENCES BETWEEN THE TWO TYPES OF ACCOUNTS, ASSUME THAT A TAXPAYER HAD AT THE BEGINNING OF THE TAXABLE YEAR $1,000 OF DEVELOPMENT COSTS WHICH WERE FULLY DEPRECIATED AND THAT DURING THE TAXABLE YEAR HE INCURRED

AGO 785853

AN ADDITIONAL $200 OF DEVELOPMENT COSTS WHICH WERE ELIGIBLE FOR DEPRECIATION. IN DETERMINING THE TAXPAYER'S DEPRECIATION DEDUCTION USING THE STRAIGHT-LINE METHOD AND ASSUMING A 10-YEAR USEFUL LIFE, THE DEPRECIATION WOULD BE CALCULATED AS FOLLOWS:

(1) IF AN OPEN-ENDED ACCOUNT IS USED, THE AVERAGE ORIGINAL DEVELOPMENT COSTS IN THE DEPRECIATION ACCOUNT WOULD AMOUNT TO $1100 WHICH IS THEN MULTIPLIED BY A 10% DEPRECIATION RATE, PROVIDING A DEPRECIATION DEDUCTION OF $110 IN THE FIRST YEAR BASED ON ONLY AN ADDITIONAL $200 OF DEPRECIABLE DEVELOPMENT COSTS.

(2) IF A CLOSED-END DEPRECIATION ACCOUNT IS USED, THE AVERAGE ORIGINAL DEVELOPMENT COSTS IN THE CURRENT YEAR VINTAGE ACCOUNT WOULD EQUAL $100 WHICH WHEN MULTIPLIED BY THE 10% DEPRECIATION RATE PROVIDES A DEDUCTION OF $10 IN THE FIRST YEAR.

THUS, THE EXAMPLE ILLUSTRATES THAT UNDER CERTAIN CIRCUMSTANCES THE USE OF AN OPEN-ENDED RATHER THAN A CLOSED-END DEPRECIATION ACCOUNT CAN RESULT IN SIGNIFICANTLY GREATER AMOUNTS OF DEPRECIATION.

ALTHOUGH THE USE OF AN OPEN-ENDED COMPOSITE ACCOUNT YIELDS GREATER DEPRECIATION DEDUCTIONS, THE ASSOCIATION RECOGNIZES THAT THIS RESULT IS UNINTENDED AND SUGGESTS THAT THE PROPOSED REGULATIONS SHOULD BE CHANGED. ACCORDINGLY, SECTION 260(D) OF AOGA'S SUGGESTED CHANGES PROVIDES THAT EACH TAXPAYER MUST ESTABLISH A CLOSED-END VINTAGE ACCOUNT FOR DEVELOPMENT COSTS FIRST ELIGIBLE FOR DEPRECIATION DURING THE TAXABLE YEAR. "DEVELOPMENT COSTS FIRST ELIGIBLE FOR

AGO 785854

DEPRECIATION" DURING A PARTICULAR TAXABLE YEAR WOULD INCLUDE (1) DEVELOPMENT COSTS PAID OR INCURRED DURING THAT YEAR WITH RESPECT TO A LEASE OR PROPERTY THAT HAD COMMERCIAL PRODUCTION FROM (OR ALLOCATED TO) IT AND (2) DEVELOPMENT COSTS PAID OR INCURRED IN PRIOR TAXABLE YEARS WITH RESPECT TO A LEASE OR PROPERTY THAT FIRST HAD COMMERCIAL PRODUCTION FROM (OR ALLOCATED TO) IT DURING THAT TAXABLE YEAR.

AS AN ILLUSTRATION, SUPPOSE A TAXPAYER INCURS DEVELOPMENT COSTS ELIGIBLE FOR DEPRECIATION OF $10 MILLION IN 1982 AND $20 MILLION IN 1983. FOR THE TAXABLE YEAR 1982, THE TAXPAYER WOULD CALCULATE DEPRECIATION FOR ITS 1982 VINTAGE ACCOUNT BASED ON $10 MILLION OF DEVELOPMENT COSTS. FOR THE TAXABLE YEAR 1983, THE TAXPAYER WOULD CALCULATE DEPRECIATION SEPARATELY FOR THE 1982 VINTAGE ACCOUNT BASED ON $10 MILLION OF DEVELOPMENT COSTS AND FOR THE 1983 VINTAGE ACCOUNT BASED ON $20 MILLION OF DEVELOPMENT COSTS. IF THE TAXPAYER INCURRED $30 MILLION OF DEVELOPMENT COSTS IN 1984 FOR A LEASE OR PROPERTY WHICH WOULD NOT HAVE COMMERCIAL PRODUCTION FROM (OR ALLOCATED TO) IT UNTIL 1985, THE $30 MILLION WOULD FALL IN THE 1985 VINTAGE ACCOUNT FOR PURPOSES OF CALCULATING THE TAXPAYER'S DEPRECIATION.

ANOTHER PROBLEM PERTAINING TO THE CALCULATION OF DEPRECIATION USING A METHOD PRESCRIBED IN SECTION 260(C) AND AN OPEN-ENDED COMPOSITE ACCOUNT WILL OCCUR WHEN THE TAXPAYER

AGO 785855

CHANGES ITS METHOD OF COMPUTING DEPRECIATION UNDER SECTION 260(D). THE EXAMPLE IN THE PROPOSED REGULATIONS MAKES IT CLEAR THAT IN SWITCHING TO THE STRAIGHT-LINE METHOD, IT IS INTENDED THAT THE TAXPAYER USE ITS AVERAGE ORIGINAL DEVELOPMENT COSTS IN DETERMINING ITS DEPRECIATION DEDUCTION. SUCH A DEDUCTION WOULD GREATLY EXCEED THAT WHICH WOULD BE CALCULATED USING THE UNDEPRECIATED BALANCE OF THE ACCOUNT DEPRECIATED OVER ITS REMAINING USEFUL LIFE. ACCORDINGLY, SECTION 260(E) OF AOGA'S SUGGESTED CHANGES PROVIDES, IN PART, THAT WHEN A CHANGE OF METHOD IS MADE FOR A VINTAGE ACCOUNT, ONLY THE TAXPAYER'S UNDEPRECIATED DEVELOPMENT COSTS (OFFSET BY SALVAGE VALUE, IF ANY) SHALL BE RECOVERED OVER THE REMAINING USEFUL LIFE OF THAT ACCOUNT USING THE NEW METHOD OF DEPRECIATION.

AOGA FURTHER RECOMMENDS IN SECTION 260(E) OF ITS SUGGESTED CHANGES THAT THE TERM "SALVAGE VALUE" BE DEFINED AS THE AMOUNT ESTIMATED TO BE REALIZABLE UPON THE DISPOSITION OF AN ASSET WHEN IT IS NO LONGER USEFUL IN THE TAXPAYER'S TRADE OR BUSINESS AND IS TO BE RETIRED FROM SERVICE BY THE TAXPAYER, BUT ONLY TO THE EXTENT THAT THE ESTIMATED SALVAGE VALUE OF A VINTAGE ACCOUNT EXCEEDS AN AMOUNT EQUAL TO 10% OF THE ORIGINAL DEVELOPMENT COSTS FOR THAT VINTAGE ACCOUNT. THE 10% ADJUSTMENT TO ESTIMATED SALVAGE VALUE IS INTENDED TO REDUCE CONFLICTS BETWEEN TAXPAYERS AND THE DEPARTMENT INASMUCH AS OUR EXPERIENCE INDICATES THAT MOST ASSETS USED IN ALASKA HAVE AN ESTIMATED

AGO 785856

SALVAGE VALUE OF LESS THAN 10% AT THE TIME THEY ARE RETIRED FROM SERVICE. THIS SALVAGE ADJUSTMENT IS SIMILAR TO ONE CURRENTLY AFFORDED TAXPAYERS UNDER CHAPTER 20.

THE PROPOSED REGULATIONS DO NOT PROVIDE A DEPRECIABLE LIFE FOR DEVELOPMENT COSTS, WHICH IS ESSENTIAL TO THE CALCULATION OF DEPRECIATION UNDER THE STRAIGHT-LINE, SUM OF THE YEARS-DIGITS AND DOUBLING DECLINING BALANCE METHODS OF DEPRECIATION. AOGA RECOMMENDS IN SECTION 260(F) OF ITS SUGGESTED CHANGES THAT THE DEPRECIABLE LIFE BE DETERMINED BY USING THE LOWER LIMIT ASSET DEPRECIATION RANGE GUIDELINE LIFE SET FORTH IN IRS REVENUE PROCEDURE 77-10 (AS AMENDED OR SUPERSEDED) FOR THE ASSET GUIDELINE CLASS PERTAINING TO ASSETS USED IN THE EXPLORATION FOR AND PRODUCTION OF PETROLEUM AND NATURAL GAS DEPOSITS. WE FEEL THAT REFERENCE TO THIS REVENUE PROCEDURE IS APPROPRIATE INASMUCH AS IT CURRENTLY IS BEING USED TO DETERMINE USEFUL LIFE BY CHAPTER 20 TAXPAYERS. SECTION 260(F) OF OUR SUGGESTED CHANGES FURTHER PROVIDES THAT IF REVENUE PROCEDURE 77-10 (AS AMENDED OR SUPERSEDED) IS NULLIFIED DUE TO THE IMPLEMENTATION OF A FEDERAL CAPITAL COST RECOVERY ALLOWANCE, THE DEPRECIABLE LIFE FOR PURPOSES OF CALCULATING DEPRECIATION FOR DEVELOPMENT COSTS WOULD BE THE CAPITAL RECOVERY PERIOD THAT WOULD APPLY TO CHAPTER 20 TAXPAYERS FOR SIMILAR ASSETS.

SECTIONS 260(G) AND (I) OF AOGA'S SUGGESTED CHANGES ADD BACK REFERENCES TO DRILLING COSTS SO AS TO ALLOW EITHER AN ABANDONMENT LOSS DEDUCTION OR A DEPRECIATION DEDUCTION FOR

AGO 785857

DRILLING COSTS OR COSTS RELATED TO DRILLING WHICH WERE NOT DEDUCTED UNDER SECTION 240 OF THE PROPOSED REGULATIONS. THIS IS CONSISTENT WITH OUR SUGGESTED CHANGES TO THE DEFINITION OF ACQUISITION COSTS UNDER SECTION 250 OF THE PROPOSED REGULATIONS.

AOGA HAS RECOMMENDED CHANGES IN SECTION 260(H) OF ITS SUGGESTED CHANGES TO MAKE IT CLEAR THAT, IN THE CASE OF A TRANSFER OF A PRODUCTION INTEREST OR PROPERTY DURING THE TAXABLE YEAR, THE TAXPAYER IS TO CALCULATE DEPRECIATION FOR THE PORTION OF THE YEAR PRIOR TO THE TRANSFER AND FOR THE PORTION OF THE YEAR AFTER THE TRANSFER USING ONE OF THE METHODS OF DEPRECIATION PRESCRIBED IN SECTION 260(G). FURTHERMORE, OUR SUGGESTED CHANGE IS DESIGNED TO MAKE IT CLEAR THAT PARAGRAPHS (1) AND (2) UNDERLYING SECTION 260(H) APPLY ONLY TO A TAXPAYER USING THE UNIT OF PRODUCTION METHOD OF DEPRECIATION.

SECTION 260(H) OF THE PROPOSED REGULATIONS HAS LIMITED APPLICABILITY IN CONSIDERATION OF THE METHODS OF DEPRECIATION AVAILABLE TO THE TAXPAYERS UNDER SECTION 260(C). ACCORDINGLY, AOGA RECOMMENDS THAT IT BE DELETED.

SECTION 260(J) OF AOGA'S SUGGESTED CHANGES PROVIDES A TRANSITION RULE FOR DEVELOPMENT COSTS FIRST ELIGIBLE FOR DEPRECIATION PRIOR TO JANUARY 1, 1979. THE TRANSITION RULE PROVIDES THAT DEPRECIABLE DEVELOPMENT COSTS INCURRED PRIOR TO JANUARY 1, 1979 ARE TO BE PLACED IN A CLOSED-END COMPOSITE

AGO 785858

ACCOUNT. UNDER THIS SUGGESTED TRANSITION RULE, THE TAXPAYER WOULD SELECT ONE OF THE METHODS PRESCRIBED UNDER SECTION 260(C) AND DEPRECIATE ITS UNDEPRECIATED DEVELOPMENT COSTS OVER THE REMAINING USEFUL LIFE OF THE ACCOUNT CONSISTENT WITH THE CHANGE OF METHOD RULES PRESCRIBED UNDER SECTION 260(E). THE REMAINING USEFUL LIFE WOULD BE EQUAL TO 11 YEARS MINUS 1 YEAR FOR EACH TAXABLE YEAR AFTER 1977 TO THE BEGINNING OF THE TAXABLE YEAR. SECTION 260(J) IS DESIGNED TO PROVIDE A SIMPLE TRANSITION INTO THE NEW DEPRECIATION RULES PROVIDED UNDER SECTION 260 WITHOUT CREATING BURDENSOME ADMINISTRATIVE DIFFICULTIES FOR EITHER THE DEPARTMENT OR THE TAXPAYER.

AGO 785859

SECTION 320

THE ASSOCIATION HAS NO SPECIFIC COMMENTS WITH RESPECT TO SECTION 320 OTHER THAN TO SAY WE ARE PLEASED TO NOTE THAT, CONSISTANT WITH THE STATUTE, THE PROPOSED REGULATION INCORPORATES THE TREATMENT AFFORDED PIPELINE DISMANTLING, REMOVAL AND RESTORATION COSTS BY THE FEDERAL ENERGY REGULATORY COMMISSION.

SECTION 710

AOGA RECOMMENDS THAT SECTION 710(F)(2)(A) BE AMENDED TO REFER SPECIFICALLY TO 9:00 A.M. JUNEAU TIME FOR NOTIFYING THE ALASKA STATE TREASURY OF THE AMOUNT OF THE TAXPAYER'S PAYMENT. THE ASSOCIATION FURTHER RECOMMENDS THAT SECTION 710(F)(2)(C) REQUIRING THE TAXPAYER TO MAKE ITS TAX PAYMENT IN ONE LUMP SUM FROM ONE BANK IS UNNECESSARY AND COULD POSSIBLY BE INCONVENIENT FOR TAXPAYERS MAKING SUBSTANTIAL PAYMENTS. THUS THIS PROVISION SHOULD BE DELETED. WE HAVE ALSO SUGGESTED CHANGES TO SECTION 710(F)(2)(D) OF THE PROPOSED REGULATIONS TO CLARIFY THE SITUATION WHEN THE DUE DATE IS NOT A BANKING DAY.

SECTION 900

SECTION 900(24) OF THE PROPOSED REGULATIONS PERTAINING TO THE DEFINITION OF THE TERM "POINT OF PRODUCTION" HAS BEEN REVISED TO CONFORM TO THE DEFINITIONS SET FORTH IN AS 43.55.140 (12)(A). UNDER OUR INTERPRETATION OF THE STATUTE, THE POINT OF PRODUCTION IN THE CASE OF OIL SHOULD BE THE FIRST POINT DOWNSTREAM OF THE WELL WHERE THE OIL IS ACCURATELY MEASURED IN

AGO 785860

A CONDITION OF PIPELINE QUALITY REGARDLESS OF WHETHER THERE IS A CUSTODY TRANSFER METER OR UNIT. IN THE CASE OF GAS, WE BELIEVE THAT THE DISTINCTION SET FORTH IN THE STATUTE BETWEEN GAS WELL GAS AND CASINGHEAD GAS SHOULD BE RECOGNIZED IN THE REGULATIONS.

AOGA ALSO SUGGESTS AS AN ADDITION TO THE DEFINITION OF SALES DELIVERY POINT UNDER SECTION 900(31) OF THE PROPOSED REGULATION, PARAGRAPH (C), WHICH APPARENTLY HAD BEEN INADVERTENTLY OMITTED. PARAGRAPH (C) PERTAINS TO A TAXPAYER'S GAS NOT SOLD AND DELIVERED IN A BONA FIDE, ARM'S-LENGTH SALE TO A THIRD PARTY.

IN LIGHT OF THE CHANGES MADE TO SECTIONS 240(B) AND (C) OF THE PROPOSED REGULATIONS RELATING TO COS[illegible] .OR A[illegible]D IN SUPPORT OF DRILLING, WE HAVE INCLUDED IN OUR SUGGESTED LANGUAGE A DEFINITION OF THE TERMS "COSTS OF DRILLING" AND "DRILLING COSTS" TO INCLUDE COSTS WHICH ARE INCIDENT TO AND NECESSARY FOR DRILLING WELLS AND PREPARING WELLS FOR PRODUCTION.

EFFECTIVE DATE

AOGA RECOMMENDS THAT THE REGULATIONS BE MADE EFFECTIVE FOR TAX RETURNS FILED AFTER THE DATE THE REGULATIONS, WITH AMENDMENTS, ARE ADOPTED. PURSUANT TO OUR UNDERSTANDING OF THE GENERAL RULES OF ADMINISTRATIVE LAW, THE REGULATIONS MAY NOT BE GIVEN RETROACTIVE EFFECT ABSENT A CLEAR STATEMENT IN THE REGULATIONS EVIDENCING THIS INTENT.

May 19, 1980

Senator Clem Tillion
Senate President
Alaska State Legislature
Pouch V
Juneau, Alaska 99811

Re: Oil and Gas Corporate Income Tax

Dear Clem:

According to members of your chamber, there is a plan afoot to amend the State Oil and Gas Corporate Income Tax to provide a deduction for the Federal windfall profits tax. This will cost the Alaskan public some $8 billion by 1990 -- or $20,000 for every man, woman and child.

As near as can be determined through informal channels, proponents of tax relief for the oil industry are planning to spring this on the Legislature at the last moment, without the benefit of public hearings or input, in the form of a Senate amendment to a House bill, sending the issue immediately to the House for concurrence. Although this is a practice both chambers often resort to, it is hardly the manner in which a revenue issue of this magnitude should be handled. If Sohio, ARCO, and other major oil companies want tax relief, they should plead their case the same way as every other Alaskan group.

Sohio is selling this tax deduction disguised as a question of form. In its view, it is necessary to make the changes in the state law to avoid double taxation. But the tax question is not just a technical issue, but a political one also, with many options. If we give them the exemption, we could raise the rate of taxation to make up the difference. Or, we could provide the exemption but raise the severance tax to 15%, where it backs out the Federal windfall profits tax. The industry's concern about taxation policy is a concern about the bottom line.

That line could be drawn higher or lower. The Federal windfall profits tax is aimed at a massive windfall that has been realized by the oil industry. Sohio's 1979 profits are up 164 percent over 1978, and 1980 revenues will reflect the benefits of decontrol. The industry's net after-tax revenues for 1980 should reach $3.6 billion, or enough money to provide $3[illegible],000 for 100,000 families. By 1983, industry profits are expected to top 5 billion dollars annually, or 20% more than Exxon's record $4.2 billion in earnings this year. These are staggering profits. This year's Prudhoe Bay net profit to the industry will equal 2.5% of all U.S. corporate profits earned in 1979, and 7 percent of all corporate dividends paid in the U.S. last year.

AGO 785862

If we respond to this enormous windfall by lowering the oil company taxes, we will certainly be unique. The rest of the world, and indeed, even some states in the U.S., are considering or have already enacted tough new taxes.

Recent actions in Britian and Norway are a case in point. This is particularly interesting when one considers the different political climates of these countries compared to OPEC nations. One industry analyst notes that "[t]he North Sea is still generally viewed as offering about the world's most attractive economic and political climate for oil exploration. . .offering an unbeatable combination - free market pricing, political stability, and proximity to the world's biggest import market." It is doubly interesting to Alaskans because the British government is a large equity owner in Prudhoe Bay through BP's 53 % ownership of Sohio.

New policy directions taken by the Britons and Norwegians include the following:

1. <u>Higher British Taxes</u>.

   "Oil companies fear the [British] government may once again opt to raise its Petroleum Revenue Tax (PRT) on North Sea profits - 70% from 60% in its new budget this week. That would raise the government share of future oil price rises to 87.5% from 83% now and just 70% when the PRT was initiated in 1975.

   (Petroleum Intelligence Weekly, March 24, 1980)

2. <u>Higher Norwegian taxes</u>.

   "North Sea producers's profits per barrel could be slashed by as much as half by the new tax proposals, which are seen jumping Norway's 'take' to about 85% to 87% from 70% - 79% now. Oslo cites soaring world prices as justifying the rise.'

   (PIW, Feb. 25, 1980)

   The increase in Norwegian taxes includes, among other things, Norway's "special" tax on North Sea profits of 35% to 25%. This "special" tax on profits is not deductable against the Norwegian corporate income tax of 50%. This, of course, is analogous to the situation where the State of Alaska's 9.4 percent tax on profits does not allow a deduction for the Federal Windfall Profits Tax.

3. <u>British ownership of field development</u>. When Margaret Thatcher's tory government was elected, she promised to trim the sails of the government owned British National Oil Corporation (BNOC). Subsquently, members of Ms. Thatcher's cabinent have expressed reservations about the government relinquishing its oil holdings. Now industry experts report that oil companies are unhappy about

   "the proposed British seventh-round licensing terms that would make British National Oil Corp. a co-licensee and continue its rights to 51% of all oil output."

   (PIW, March 24, 1980)

4. <u>Norwegianization of field development</u>.

   "Norway's new White Paper on oil policy is generally being interpreted as a blueprint for accelerating 'Norwegianization' of offshore oil resources and operations. While it is simply an advisory document to be debated in parliament, 'Norway for the Norwegians' is seen likely to be a popular political doctrine. . .

   The document is seen favoring greater use, where feasible, of 100% Norwegian equity in licenses reserved for the three principal Norwegian oil firms - state owned Statoil, state-controlled Norsk Hydro and privde Saga Petroleum. . .

   It's believed likely that unassigned acreage around promising North Sea oil and gas discoveries will go in the future to all-Norwegian ownership.

   (PIW, Feb. 2, 1980)

The tax question is an important one, and given both the recent price hikes and the worldwide reaction, it may make sense to take another look at whether the citizens of this state are getting their fair share. This will not be accomplished by pushing for an 8 billion dollar tax break for the industry in the dying moments of the legislature, with no debate or analysis. I urge you to use your influence to prevent this matter from comming before the Senate this year.

Sincerely,

ALASKA PUBLIC INTEREST RESEARCH GROUP

James Love
Director

enclosures

AGO 785864

Profits of three Prudhoe Bay operators

company	third quarter $ Mill 1979	third quarter % Chg v '78	fourth quarter $ Mill 1979	fourth quarter % Chg v '78	full year $ Mill 1979	full year % Chg v '78
Arco	320	+ 45%	343	+ 54%	1,166	+ 45
Exxon	1,145	+ 118	1,365	+ 60	4,295	+ 55
Sohio	366	+ 191	451	+ 174	1,190	+ 164

Comparison of Exxon's Prudhoe Bay and worldwide operations, 1979

Estimated net revenue from Prudhoe Bay operations	$458 million
Estimated tax and royalty payments from Prudhoe Bay operations	553 million
Reported profits from worldwide operations	4,295 million
Alaska net revenue as percentage of worldwide profits	10.7%
Reported taxes paid worldwide	22,870 million
Alaska tax and royalty payments as percentage of worldwide tax payments	2.4%

AGO 785865

REPORTS FROM PETROLEUM INTELLIGENCE WEEKLY

BP's net income from Sohio tripled

Continuing to benefit largely from inventory profits and gains in Alaskan income, British Petroleum's 1979 profits more than tripled to $3.6 billion. Indicated fourth-quarter profits also nearly tripled to $9994 million. Sales and operating revenues for the year net of duties and sales tax rose a gentler 28% to $40.5-billion.

BP's net income from Sohio more than tripled to $1.05-billion as Sohio's share of Alaskan oil rose to 675,000 b/d from 579,000 b/d in 1978. BP has a 53% share in Sohio's net profits on Alaskan production between 600,000 and 1.05-million b/d.

March 17, 1980

AGO 785866

December 24, 1979 Industry analysis of North Slope profits shows rate-of-return is 47% higher than average return earned by U.S. manufacturing industries. (before decontrol)

"North Slope profits are up more than 100% in 1979, with net after-tax margins now in the area of a handsome $6.20 a barrel, according to a Petroleum Intelligence Weekly analysis. Profits on Alaskan crude have been substantial right from the start of North Slope output in 1977. Even though the producers had some initial difficulty in lining up clients, profits in 1977 ranged from $1.70 to $2.70 a barrel. By early 1979, margins climbed to about $2.50 to $3, then rocketed to $4 in the second quarter, and $6 in the third quarter. . .

The present $7-plus per barrel profit on North Slope crude represents an annualized 22% return on the $14.5-billion invested in Alaska exploration, production and the pipeline, PIW calculates. This compares with a U. Inflation rate of 13% and the genral 15% return earned by U.S. manufacturing industries. In early 1979, the return on North Slope was a bare 10%.

If North Slope crude were 100% free to track runaway OPEC prices now, producers could easily raise selling prices as much as $10 a barrel This would boost after-tax profits by a heady $3.50-$4 a barrel, PIW calculates. Revenues of Alaska and the Federal Government would also climb. For every $1 price rise the companies profits would jump some 35 ¢ to 40 ¢ a barrel, Alaska would get 30 ¢ and the Federal Government 25 ¢, with the rest covering other costs.

Starting Jan. 1980, the price and profit outlook will depend on the combined effects of phased crude price decontrol and the final version of the pending new excise tax on the resulting 'windfall profits.'"

(Petroleum Intelligence Weekly, Dec. 24, 1979)

GOING TO THE WELL: 'BIG OIL' FIRMS FIND THAT OUTLETS FOR INVESTMENT OF THEIR LARGE EARNINGS ARE LIMITED

Wall Street Journal
April 9, 1980

Sun Oil Purchases Seagram Co.

Two months ago Jack Neafsey, senior vice president of Sun Co., the nation's 10th largest oil company, was voicing an extraordinary problem: With 1979 profits up by 69%, the company was practically in the position of having too much money to invest at once. The only constraint the company was facing, he said, was "the question of how many opportunities we can take on at one time."

Two days ago, Sun found a place for some of its expansive profits -- it offered $2.3 billion for the bulk of the U.S. oil and gas properties of Seagram Co. The proposed acquisition's price tag was second only to Shell Oil Co.'s $3.65 billion takeover of Belridge Oil Co. last year.

Exxon has problems spending it's money

For many large U.S. oil concerns the embarrassment of riches brought their way by last year's record profits is both an odd and a vexing problem. Even though their capital budgets are at record levels and far exceed their profits, these companies say they have more financial resources than they can profitably spend.

Exxon Corp., the world's largest oil concern, has a $7.5 billion spending program for this year, a 25% increase from last year's inital appropriation. But Exxon would like to spend even more, says Roger Meadrick, the deputy controller. 'We're not financially constrained from doing so,' he says. 'We're what you might call opportunity-limited.'

Money is no object

At Standard Oil Co. of California, Mobil Corp., Phillips Petroleum Co. and Getty Oil Co., capital spending is proceeding as though money were no object - which it isn't. "I've told our operating people that if they've got a sound oil and gas project they can handle, don't worry about the money - I'll find a way to get it,' says Howard Bell, California Standard's vice president of finance.

. . .Spending money at home has public-relations value, of course. At one big oil company, there is the rumor that a 'political' percentage was tacked onto the bids that the firm submitted for a big offshore lease sale a few years back. After the tracts had been appraised, a company source says, 'word was going around that the suggested bids were sent up to the chairman's office, and he grossed them up because he wanted our spending figures to look bigger.'

AGO 785868

Prudhoe Bay tax scenarios, 1980 - 1990

assumes 12% annual inflation in oil prices

year	present state take	Sohio proposal for windfall profits deduction	diff.	McKinnon/ Rogers proposal for 15% severance tax	diff.	50% state income tax	diff.	proposal for 80% state income tax	diff.
80	$ 2,901.5	$ 2,813.5	($ 88.0)	$3,189.2	$ 287.7	$5,557.3	$2,655.8	$7,368.0	$4,466.5
81	4,268.8	3,974.2	(294.5)	4,727.7	458.9	7,442.9	3,174.1	10,349.7	6,080.9
82	5,058.7	4,649.5	([illegible]09.2)	5,646.8	58[illegible].1	8,576.3	3,517.6	12,285.1	7,226.4
83	5,640.7	5,150.6	(490.1)	6,346.3	705.6	9,445.6	3,804.9	13,754.2	8,113.5
84	6,291.9	5,708.6	(583.3)	7,136.9	845.0	10,437.3	4,145.4	15,384.9	9,093.0
85	7,035.9	6,346.0	(689.9)	8,032.1	996.2	11 597.3	4,561.4	17,551.5	10.515.6
86	7,912.8	7,104.0	(808.8)	9,031.9	1,119.1	12,898.8	4,986.0	19,780.8	11,868.0
87	8,887.5	7,941.8	(945.7)	10,162.0	1,274.5	14,391.8	5,504.3	22,528.8	13,641.3
88	9,975.5	8,873.7	(1,101.8)	11,426.7	1,451.2	16,055.9	6,080.4	25,409.7	15,434.2
89	11,172.5	9,890.8	(1,281.7)	12,852.8	1,680.3	18,144.8	6,972.3	28,903.9	17,731.4
90	10.889.2	9,596.2	(1,293.0)	12,577.0	1,687.8	17,767.0	6,877.2	28,296.0	17,406.8
	80,035	72,048.9	(7,986.1)	96,776.2	16,741.2	132,315.0	52,279.4	201,612.5	121,577.6
dollars per/ capita	200,087	180,122	(19,965)	241,941	41,853	330,788	130,699	504,[illegible]31	303,944
dollars per/family of four	800,350	720.489	(79,861)	967,762	167,412	1,323,150	522,794	2,016,125	1,215,776
industry dcf rate of return	26.4 %	26.66 %		26.3 %		24.13%		20.98%	

AGO 785869

DIVISION OF REVENUE FROM PRUDHOE BAY UNDER DIFFERENT TAXATION SCENARIOS

PRICES INFLATED AT 12%

TAX SCENARIO	YEAR	STATE TAKE	%	FEDERAL TAKE	%	INDUSTRY NET	%	INDUSTRY NET AS $ PER CAPITA	INDUSTRY NET AS $ PER FAMILY OF 4
present tax	80	$3,106.7	.34	$2,432.4	.27	$3,627.0	.40	$9,068	$36,270
	81	4,453.0	.33	4,782.0	.35	4,337.7	.32	10,844	43,377
	82	5,266.9	.33	6,057.9	.38	4,705.7	.29	11,764	47,057
	83	5,893.6	.33	6,961.9	.39	5,006.2	.28	12,516	50,062
Sohio proposal for windfall profits tax deduction									
	80	2,813.5	.31	2,561.4	.28	3,7[illegible]1.2	.41	9,478	37,912
	81	3,974.2	.29	5,073.0	.37	4,525.5	.33	11,314	45,255
	82	4,649.5	.29	6,461.7	.40	4,919.2	.31	12,298	49,192
	83	5,150.6	.29	7,463.1	.42	5,248.0	.29	13.120	52,480
McKinnon/Rogers proposal for 15% severance tax									
	80	3,189.2	.35	2,407.6	.26	3,569.2	.39	8,923	35,692
	81	4,727.7	.35	4,699.6	.35	4,145.4	.31	10,364	41,454
	82	5,646.8	.35	5,943.9	.37	4,439.8	.28	11,100	44,398
	83	6,346.3	.36	6,826.1	.38	4,689.3	.26	11,723	46,893
15% severance tax and 50% state income tax with windfall profits tax deduction									
	80	5,557.[illegible]	.61	1,697.2	.19	1,911.6	.21	4,779	19,116
	81	7,442.9	.55	3,885.1	.29	2,244.8	.17	5,612	22,448
	82	8,576.3	.53	5,065.1	.32	2,389.1	.15	5,973	23,891
	83	9,445.6	.53	5,896.3	.33	2.519.8	.14	6,298	25,198
15% severance tax and 80% state income tax with windfall profits tax deduction									
	81	7,368.0	.80	1,1[illegible]4.0	.13	644.0	.07	1 610	6,440
	81	10,349.7	.76	2,402.6	.18	820.4	.06	2,050	8,204
	82	12,285.1	.77	2,846.9	.18	898.5	.06	2,246	8,985
	83	13,754.2	.77	3,130.2	.18	977.2	.05	2,443	9,772

AGO 785870

California considers 10% surtax on oil industry profits.

At the top of the television screen, six pigs snuffle greedily in a trough; at the bottom, hugh profit figures from the oil companies make the sponor's porcine point. 'Sure, big oil companies have a right to reasonable profit,' says the announcer. 'But this year they're eating up more than their share.' A slogan - 'Tax Pig Oil' - flashes onto the screen, and as the voice-over continues, the 'P' fades into a 'B.' 'Let's stick it to Big Oil,' says the announcer. 'They've been sticking it to us for years.'

The Pig ad is a plug for Proposition 11, a California proposal to impose a 10 per cent surtax on oil-company profits. It will appear on the state ballot June 3.

Other states follow suit

Like Proposition 13, the tax slashing measure that inspired simil'ar initiatives in many other states, Prop 11 promises to reverberate far beyond California's borders. Connecticut has already enacted a 2 per cent tax on the gross receipts of big oil companies operating within the state, and at least half a dozen others are considering similar action.

Newsweek, May 19, 1980

Australia increases government "take", keeps 94% of OPEC windfall

Austalia's complex import-parity pricing formula for its 425,000 barrels daily crude oil production is making the government, not the producing companies, the big gainer from the sharp rise in OPEC prices. . .

The government 'take'* on domestic crude has increased as from Jan. 1 to nearly three quarters of the selling price - which PIW estimates at a weighted average $27.55 per barrel - up from two-thirds of an average $21.05 last July. The producers were left a mere 37 ¢ out of the $6.48 average Jan. increase, with the government taking $6.11. . .

* before deducting the state royalty, operating costs, depreciation, and Commonwealth corporate income tax. Thus not to be construed as net profit.

(PIW, March 17, 1980)

AGU 785871