

2150

ST

HB 866- HJR 20

200

Yr	Pre-Tax Cash Flow from Project	Project Depreciation	With State Investment Tax Credit Under Existing State Law							With State Investment Tax Credit under HB 866				
			AK Inc. Tax From Project Before ITC	AK ITC Applied	AK Inc. Tax From Project After ITC	US Inc. Tax From Project Before ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow	AK ITC Applied	AK Inc. Tax From Project After ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow
1	-1,000,000	0	0	0	0	0	0	0	-1,000,000	0	0	0	0	-1,000,000
2	250,000	80,000	15,980	18,000*	-2,020	79,129	100,000	-20,871	272,891	82,520**	-66,540	100,000	9,738	306,802
3	250,000	140,000	10,340	0	10,340	45,844	0	45,844	193,816	17,480	-7,140	0	49,123	208,012
4	250,000	120,000	12,220	0	12,220	54,179	0	54,179	183,601	0	12,220	0	54,179	183,601
5	250,000	100,000	14,100	0	14,100	62,514	0	62,514	173,386	0	14,100	0	62,514	173,386
6	237,500	100,000	12,925	0	12,925	57,305	0	57,305	167,271	0	12,925	0	57,305	167,271
7	225,625	100,000	11,809	0	11,809	52,355	0	52,355	161,461	0	11,809	0	52,355	161,461
8	214,344	90,000	11,688	0	11,688	51,822	0	51,822	150,834	0	11,688	0	51,822	150,834
9	203,627	90,000	10,681	0	10,681	47,355	0	47,355	145,591	0	10,681	0	47,355	145,591
10	193,445	90,000	9,724	0	9,724	43,112	0	43,112	140,609	0	9,724	0	43,112	140,609
11	183,773	90,000	8,815	0	8,815	39,081	0	39,081	135,878	0	8,815	0	39,081	135,878
12	174,584	0	16,411	0	16,411	72,760	0	72,760	85,413	0	16,411	0	72,760	85,413
13	165,855	0	15,590	0	15,590	69,122	0	69,122	81,143	0	15,590	0	69,122	81,143
14	157,562	0	14,811	0	14,811	65,666	0	65,666	77,086	0	14,811	0	65,666	77,086
15	149,684	0	14,070	0	14,070	62,382	0	62,382	73,231	0	14,070	0	62,382	73,231
16	142,200	0	13,367	0	13,367	59,263	0	59,263	69,570	0	13,367	0	59,263	69,570
17	135,090	0	12,698	0	12,698	56,300	0	56,300	66,091	0	12,698	0	56,300	66,091
18	128,336	0	12,064	0	12,064	53,485	0	53,485	62,787	0	12,064	0	53,485	62,787
19	121,919	0	11,460	0	11,460	50,811	0	50,811	59,648	0	11,460	0	50,811	59,648
20	115,823	0	10,887	0	10,887	48,270	0	48,270	56,665	0	10,887	0	48,270	56,665
21	110,032	0	10,343	0	10,343	45,857	0	45,857	53,832	0	10,343	0	45,857	53,832
22	104,530	0	9,826	0	9,826	43,564	0	43,564	51,140	0	9,826	0	43,564	51,140
23	99,304	0	9,335	0	9,335	41,386	0	41,386	48,583	0	9,335	0	41,386	48,583
24	94,338	0	8,868	0	8,868	39,316	0	39,316	46,154	0	8,868	0	39,316	46,154
25	89,621	0	8,424	0	8,424	37,350	0	37,350	43,846	0	8,424	0	37,350	43,846

IRR=15.772%

IRR=16.769%

* Under present law, Alaska's ITC equals 18% of the federal ITC, or 1.8% of the qualified investment. Since the corporation has \$750,000 of other Alaskan taxable income, the \$2020 in ITC not used to shelter income from the project from tax can be used to reduce the tax on this other income. By the same token, the \$100,000 federal ITC can all be used in one year to reduce the tax on the other \$750,000 of taxable income.

** Under HB 866, Alaska's ITC would equal the federal ITC, or \$100,000 in this example. The negative figure reflects the fact that a \$100,000 Alaskan ITC would shelter not only all of the \$170,900 taxable income from the project, but would reduce to zero the \$66,540 tax on the other \$750,000 of taxable Alaskan income, and still leave some \$17,480 of ITC to spare. This \$17,480 is carried over into the next year, where it reduces to zero the \$10,340 tax liability generated by the project and reduces the taxes on the other \$750,000 by \$7,140 (reflected as a negative figure).

PLEASE NOTE: THE FOLLOWING PAGES WERE TREATED
AS A UNIT IN THE ORIGINAL DOCUMENT

- FILE -
Alaska State Legislature

HOME ADDRESS

WHILE IN JUNEAU
POUCH V
JUNEAU, ALASKA 99811
TELEPHONE



SENATOR

John C. Sackett

SENATE FINANCE COMMITTEE

Senate

M E M O R A N D U M

May 20, 1982

TO: Senator Bill Ray
FROM: Senator John C. Sackett
SUBJECT: House Bill 866

A handwritten signature in dark ink, appearing to be "JS", written over the "FROM" line of the memorandum.

I would appreciate it very much if you would schedule House Bill 866 for a hearing before the Senate Transportation Committee. It still has a further referral to the Senate Finance Committee.

Attached is the back-up on the bill. Although it is a house bill, I still have an interest in it. Thank you for your consideration.



Alaska State Legislature

Senate Committee on State Affairs


Vic Fischer, Chairman • Pouch V • Juneau, Alaska 99811 • (907) 465-4954

Official Business

MEMORANDUM

DATE: May 17, 1982

TO: Senator Ed Dankworth, Co-Chairman, Senate Finance Committee
Senator Don Bennett, Co-Chairman, Senate Finance Committee

FROM: Senator Vic Fischer 

RE: HB 866, Investment Tax Credit

The House version of HB 866 provided an investment tax credit equal to 100 percent of the investment credit allowed on federal taxes. Corporations investing in farming, fishing, timber or mining would be eligible for the investment credit. Oil and gas investments would not be eligible for the credit.

The Senate CS for HB 866 makes the following amendments:

1. The investment tax credit is changed to 36 percent of the investment credit allowed on federal taxes. The state currently allows an investment tax credit equal to 18 percent of the investment credit allowed on federal taxes.
2. The investment tax credit only applies to mining activities and the activities must be conducted by corporations which have previously not been active in Alaska or conducted at previously undeveloped sites.
3. The new investment tax credit expires December 31, 1986.

The purpose of the amendments is to channel investment tax credits to initiate new mining investments which would not have been made without the investment tax credit. The committee could not obtain a clear legal judgement as to whether US Borax might qualify and thus obtain a windfall of close to \$80 million.

The following reference materials are enclosed:

CS for HB 866
Transcript of State Affairs hearing of May 5, 1982, on HB 866.
Fiscal note on House passed version of HB 866
Letter of May 15, 1982, to Senator Vic Fischer, from Commissioner Williams, regarding Effects on Economic-Decision Making from Increasing the State Investment Tax Credit as Proposed in HB 866
Memorandum of May 12, 1982, to Senator Fischer, regarding Effect of Investment Credit on Projected State Revenues Generated by US Borax
other pertinent material

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH 5
JUNEAU, ALASKA 99811
PHONE: (907) 465-2300

April 27, 1982

The Honorable Vic Fischer
Chairman
Senate State Affairs Committee
Room 423 - Capitol Building
Juneau, Alaska

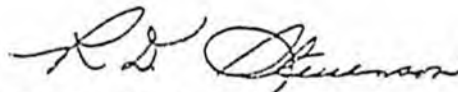
Re: House Bill No. 866 am

Dear Senator Fischer:

House Bill No. 866 am, an Act establishing a special investment tax credit, upon first reading in the Senate on April 26, 1982 was referred to the Senate State Affairs and Finance Committees.

For the consideration of the Senate State Affairs Committee, I am enclosing a copy of a Fiscal Note prepared by Mr. Robert R. Kessel, Director, Audit Division, Department of Revenue concerning the proposed legislation.

Sincerely,



R. D. Stevenson
Special Assistant

cc: The Honorable Don Bennett
The Honorable M. E. Dankworth
Co-Chairmen
Senate Finance Committee

Joseph K. Donohue
Deputy Commissioner
Department of Revenue

Robert R. Kessel, Director
Audit Division
Department of Revenue

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST

Bill/Resolution Number: HB 866 am

Title: An Act establishing a special investment tax credit

Requested by: State Affairs

Date: April 26, 1982

II. FISCAL DETAIL

Agency Affected: Department of Revenue

Program Category Affected: Revenue Collection and Management

BRU, Program, or Subprogram(s) Affected: Audit Division

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
100 PERSONAL SERVICES	-	-	-	-	-	-
200 TRAVEL	-	-	-	-	-	-
300 CONTRACTUAL	-	-	-	-	-	-
400 COMMODITIES	-	-	-	-	-	-
500 EQUIPMENT	-	-	-	-	-	-
600 LAND & STRUCTURES	-	-	-	-	-	-
700 GRANTS, CLAIMS, ETC	-	-	-	-	-	-
800 MISCELLANEOUS	-	-	-	-	-	-
TOTAL	-	-	-	-	-	-

FUNDING (Millions of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
GENERAL FUND	(2.5)	(11.5)	(13.0)	-	-	-
FEDERAL FUNDS	-	-	-	-	-	-
OTHER (Specify Source)	-	-	-	-	-	-

POSITIONS

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
FULL TIME	-	-	-	-	-	-
PART TIME	-	-	-	-	-	-
TEMPORARY	-	-	-	-	-	-

III. ANALYSIS (See Fiscal Note Preparation Instruction, Section III)

It is assumed that the investment tax credit utilized by the four impacted industries, including carryback of the credit, would essentially equate to the income tax payable by these four groups for the latest year. These four groups account for approximately 33 percent of the Department's revenue projections.

Robert R. Kessel

IV. DATE: April 26, 1982

PREPARED BY: Robert R. Kessel

AGENCY: Audit Division

PHONE: 465-2320

Original: Legislative Finance

cc: Budget and Management

Prime Sponsor (First Legislator Named)

STATE OF ALASKA
DEPARTMENT OF REVENUE

M E M O R A N D U M

TO: R. D. Stevenson
Special Assistant

FROM: Robert R. Kessel
Director, Audit Division *RH*

DATE: April 26, 1982

RE: HB 866 am

The bill would substantially expand the Investment Tax Credit for certain corporations. However, the bill falls short of its intended purpose to promote the development of farming, fishing, timber and mining and, in addition, is potentially very expensive.

I am not aware of any study which supports the conclusion that state income tax credits are a strong encouragement for investment in a particular state. Most studies, in fact, reflect that state income taxes have a low importance ranking when investment appraisals are made. In fact, supply of labor, financing, marketability, supply of raw materials, etc., are of the most relevancy.

Experience has shown that when a social or economic problem arises, often the first - and not carefully considered - answer is to use the tax system, whether the proposal comes from government or the private sector. However, tax credits seldom solve the social or economic problem. In fact, tax credits are useful only to those who have income taxes to pay (profitable) and who can therefore make use of the credits. Those who don't pay taxes - those with sufficient or no tax liability - thus receive no assistance from the tax credit program. If a tax credit were to cover these groups - the ones who really need it - it must be refundable; i.e., paid by the state even in the absence of tax liability, and a refundable credit really involves direct spending or subsidy.

It is questionable whether the Federal Investment Tax Credit has provided businesses the incentive to make investments and whether the credit has provided an accelerator effect on the economy as a whole.

Questions that have been asked at the Federal level include:

1. Does the credit flow through to stockholders in the form of dividends rather than used for capital expenditures?
2. Has the credit been used for foreign investment rather than domestic investment thus exporting more jobs overseas?
3. Has the investment tax credit actually increased investment in capital projects?

These very same questions must be asked if Alaska allows the investment tax credit to the extent of HB 866 am.

The extent of the investment tax credit in HB 866 am appears to be grossly misunderstood. The bill would allow the same amount of investment tax credit as is allowed on the Federal return. This is in spite of the tremendously large differentials in tax liabilities at the two levels. For example, if a taxpayer invested \$5,000,000 in qualified investment property with the resulting investment credit of \$500,000 (10%), the Alaska taxable income needed to absorb that amount would be about \$5,400,000. In other words, not a cent of Alaska income tax would be paid if the corporation had a taxable income of \$5,400,000. Conversely, the Federal tax liability on that amount, even with the investment tax credit, would be about \$2,000,000

If a corporation invested \$50,000,000 in qualified property, the Alaska taxable income needed to absorb the investment tax credit would be in excess of \$50,000,000 whereas the Federal tax liability on the \$50,000,000 would be about \$18,000,000.

Since only profitable companies could utilize the investment tax credit, the reduction in Alaska State Income Taxes resulting from HB 866 am would increase Federal taxable income by a like amount. In essence, up to 46% of what is saved at the State level would simply be transferred to the Federal Government in the form of a higher Federal income tax liability.

In addition, Alaska already has an investment tax credit for all industries but limited to 18% of the Federal Tax Credit and a further limitation of \$20,000,000 for qualified property eligible for the credit. The 18% directs itself to the fact that the tax rates are so different; i.e., maximum State rate - 9.4%, maximum Federal rate - 46%.

There are more qualified farmers than there is farmland available. The additional investment tax credit would give the existing farmers additional tax benefits but would do little to expand ownership to a new influx of farmers.

Most timber related companies already have more tax credits and carry-over losses than they can utilize. It is markets that are needed.

For fisheries, all except bottom fishing appears overly crowded. That fact is witnessed by the limited entry system controlling the harvest of fishery resources. Tax credits would not expand the market nor provide higher prices.

Mining, in general, is a highly capital intensive industry. The expanded investment tax credit would serve the purpose of providing almost permanent assurance that no tax would be due because of the fifteen year carry-over provision available for the investment tax credit.

Finally, the expanded credit could be very costly particularly in one instance. If U. S. Borax develops its Ketchikan Molybdenum mine to the extent publicly indicated, the investment tax credit to that corporation could be as high as \$100,000,000 (based on investment cost of \$1 billion). With the fifteen year carry-over provision for the investment tax credit, the investment tax credit of \$100,000,000 could equate to the following revenue loss to Alaska (assuming U. S. Borax had sufficient taxable income to absorb):

Investment Credit applied against tax liability - per current law

\$1,000,000,000	
x 10% Investment Credit amount	
x 18% currently allowed for Alaska corporations	\$ 18,000,000

Investment Credit applied against tax liability per this bill

\$1,000,000,000	
x 10%	<u>100,000,000</u>

Net Loss in Revenue	<u>\$ 82,000,000</u>
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The above assumes that the entire \$1 billion would be eligible for the investment tax credit. The portion actually available could vary from 65-100%.

Borax activity will not impact the immediate future fiscally since production from the Ketchikan mine is not anticipated until the late 1980's.

The bill also creates a carry-back problem. The investment tax credit can be carried back and would affect prior year taxes. Therefore, in essence, this bill provides for the potential of a refund of past years taxes. This potentially creates a constitutional question.

HB 866 am adds a provision not contained in HB 866. It is as follows:

"(K) No Credit shall be allowed under (j) of this section for any investment credit which is allowed as to federal taxes for leased property by reason of Section 168(F)(8) of the Internal Revenue Code (26 U.S.C. 168(F)(8))."

One consequence of the Accelerated Cost Recovery System and revisions of the investment tax credit is that many companies are not able currently to use all their tax deductions and credits. In considering potential investments, these companies are at a competitive disadvantage and can become targets for tax-induced takeovers and merges. The Economic Recovery Tax Act of 1981 (ERTA) establishes what is referred to as a safe-harbor for characterizing transactions as leases rather than as sale. A lease transaction permits the lessee-user of property to transfer tax benefits to a lessor-investor, a sale transaction does not. If a lessee-user transfers the tax benefits back to the lessor, the user receives a significant portion of the tax benefits through reduced rental charges.

The new law provides more ease in transferability and its provisions eliminate many of the arguments which often had occurred between the taxpayer and IRS. However, the substantive law regarding lease transactions has not changed as a result of the Economic Recovery Tax Act (ERTA). Procedural law has changed and provides for the ease in transferability of the tax benefits from lessee to lessor.

Section 2(K) of HB 866 am provides for an unworkable administrative process for the Department of Revenue. The Department does not have the staffing to determine if the pre-ERTA Federal

law provision would have caused a lease arrangement to be considered a sale. The taxpayer, as under pre-ERTA, would obviously class certain transactions as a lease rather than a sale and await our challenge, as they previously did with the Federal Government. Therefore, no decrease in the fiscal note developed for HB 866 is foreseen and, if any, would be impossible to determine.

RRK/gb

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH 5
JUNEAU, ALASKA 99811
PHONE: (907) 465-2300

May 15, 1982

The Honorable Vic Fischer, Chairman
Senate State Affairs Committee
Pouch V
Juneau, AK 99811

Re: Effects on Economic Decision-Making from Increasing the State
Investment Tax Credit as Proposed in House Bill 866

Dear Mr. Chairman:

In my testimony before the Committee I stated that increasing the State's investment tax credit as proposed in HB 866 would have only a minimal effect on the internal rate of return after taxes for new projects in Alaska. I also said that, to the extent there would be an effect on the rate of return, it would be greater for "fat cat" corporations than for small ones. I now have had the opportunity to prepare an example which demonstrates the truth of both assertions.

Suppose we have a new project in Alaska, and to avoid any distortions by making it too large, suppose further that it costs \$1,000,000, takes a year to complete and will employ 25 people. Suppose, too, that after expenses other than income taxes and depreciation, the project yields a net cash flow of \$250,000 a year for its first four years of operation, and then each year thereafter the net cash flow decreases by five percent from the previous year. Finally, let us suppose that the project qualifies for Accelerated Capital Recovery System treatment under the new tax law using a 10-year life.

The analysis I have used takes this project and compares the internal rate of return (IRR) on the investment under Alaska's present investment tax credit with the IRR under the credit proposed in HB 866. This comparison is first made with the project standing alone; that is, the investor has no other income to be sheltered from the tax benefits generated from the project. I call this Case 1. Case 2 doesn't involve too fat a "fat cat" corporation, simply one with \$750,000 a year of taxable Alaskan net income from other sources.

The tables attached to this letter show what the after-tax cash flows are under Case 1 and Case 2, both with the present investment tax credit and with the one proposed by HB 866. As you can see from those tables, the IRR under the non-"fat cat" case (Case 1) is 18.763% under

Hon. Vic Fischer (re HB 866)
May 15, 1982
Page 2

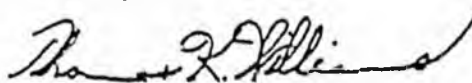
the present law and would rise by only 0.363 of a percentage point to 19.126% under HB 866. In contrast, the improvement in the rate of return for the "fat cat" case (Case 2) is nearly three times as great as for the "skinny" cat -- 0.997 of a percentage point (15.772% to 16.769%).

Note also how small a difference there is in the rate of return between present law and HB 866. The extra economic incentive from raising the State's investment tax credit is truly minimal (and you can see why: look how much higher the federal taxes would be during the early years with HB 866 than they are under present law, in both Cases 1 and 2). Other factors have much more effect on the economics of an investment than the amount of investment tax credit. For example, in Case 1, suppose one's assumptions about market prices, labor costs and other operating expenses had a 10 percent margin of error. If the net pre-tax cash flows were only 10 percent higher than the figures in the table, the increase in the rate of return would be 4.25 times that from the extra tax incentive under HB 866.

Without going on excessively, I would only reiterate my objections that HB 866 does too little economically, at too high a price for the State, to the advantage of wealthy corporations over small ones. It scarcely makes economic sense and certainly makes poor State policy.

I hope this information may prove useful to you and your Committee in considering HB 866.

Sincerely,



Thomas K. Williams
Commissioner of Revenue

Attachments

P.S. I might add parenthetically that the reason for the lower IRRs in the "fat cat" case is that all income from the project is taxed in the maximum tax bracket under both federal and state tax laws, because of the other \$750,000 of taxable income; the project represents incremental income to the corporation. In Case 1 the project stands alone, and so the first \$100,000 and first \$90,000 are taxed below the maximum rates under the federal and Alaska tax laws, respectively.

CASE 7. A NEW ALASKAN BUSINESS ON ITS OWN

Year	Pre-Tax Cash Flow from Project	Project Depreciation	With State Investment Tax Credit Under Existing State Law						With State Investment Tax Credit under HB 866				
			AK Inc. Tax From Project Before ITC	AK ITC Applied	AK Inc. Tax From Project After ITC	US Inc. Tax From Project Before ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow	AK ITC Applied	AK Inc. Tax From Project After ITC	US ITC Applied	US Inc. Tax From Project After ITC
1	-1,000,000	0	0	0	0	0	0	-1,000,000	0	0	0	0	-1,000,000
2	250,000	80,000	12,020	12,020	0	57,950	57,950	250,000	12,020	0	57,950	0	250,000
3	250,000	140,000	6,380	5,980*	400	30,166	30,166	249,600	6,380	0	30,166	0	250,000
4	250,000	120,000	8,260	0	8,260	35,750	11,884	217,874	8,260	0	11,884	27,850	222,150
5	250,000	100,000	10,140	0	10,140	44,086	0	195,774	10,140	0	0	48,750	201,250
6	237,500	100,000	8,965	0	8,965	38,876	0	189,659	8,965	0	0	43,000	194,500
7	225,625	100,000	7,849	0	7,849	33,927	0	183,849	7,849	0	0	37,538	188,088
8	214,344	90,000	7,728	0	7,728	33,393	0	173,222	7,728	0	0	36,948	177,396
9	203,627	90,000	6,721	0	6,721	28,927	0	167,979	6,721	0	0	32,018	171,609
0	193,445	90,000	5,764	0	5,764	24,822	0	162,859	5,764	0	0	27,335	166,110
1	183,773	90,000	4,855	0	4,855	21,317	0	157,601	4,855	0	0	23,259	160,514
2	174,584	0	12,451	0	12,451	54,331	0	107,802	12,451	0	0	60,059	114,525
3	165,855	0	11,630	0	11,630	50,693	0	103,531	8,867**	2,763	0	54,772	108,319
4	157,562	0	10,851	0	10,851	47,237	0	99,474	0	10,851	0	47,237	99,474
5	149,684	0	10,110	0	10,110	43,954	0	95,620	0	10,110	0	43,954	95,620
6	142,200	0	9,407	0	9,407	40,835	0	91,958	0	9,407	0	40,835	91,958
7	135,090	0	8,738	0	8,738	37,872	0	88,480	0	8,738	0	37,872	88,480
8	128,336	0	8,104	0	8,104	35,057	0	85,176	0	8,104	0	35,057	85,176
9	121,919	0	7,500	0	7,500	32,383	0	82,036	0	7,500	0	32,383	82,036
0	115,823	0	6,927	0	6,927	29,842	0	79,054	0	6,927	0	29,842	79,054
21	110,032	0	6,383	0	6,383	27,429	0	76,220	0	6,383	0	27,429	76,220
22	104,530	0	5,866	0	5,866	25,216	0	73,449	0	5,866	0	25,216	73,449
23	99,304	0	5,375	0	5,375	23,322	0	70,608	0	5,375	0	23,322	70,608
24	94,338	0	4,908	0	4,908	21,522	0	67,908	0	4,908	0	21,522	67,908
25	89,621	0	4,466	0	4,466	19,812	0	65,343	0	4,466	0	19,812	65,343

IRR=18.763%

IRR=19.126%

* Under present law, Alaska's ITC equals 18% of the federal ITC, or 1.8% of the qualified investment. As with the federal ITC, any ITC that is not used in a tax year may be carried forward into the next tax year. In this case only \$12,020 of the \$18,000 state ITC was taken in the first year; the balance of \$5,980 is taken in the second.

** Under HB 866, Alaska's ITC would equal the federal ITC, or \$100,000 in this example. This \$8,867 figure represents what remains of the \$100,000 ITC after the twelfth year of the project.

CASE 2. A LARGE ONGOING ALASKAN BUSINESS

Yr	Pre-Tax Cash Flow from Project	Project Depreciation	With State Investment Tax Credit Under Existing State Law						With State Investment Tax Credit under HB 866					
			AK Inc. Tax From Project Before ITC	AK ITC Applied	AK Inc. Tax From Project After ITC	US Inc. Tax From Project Before ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow	AK ITC Applied	AK Inc. Tax From Project After ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow
1	-1,000,000	0	0	0	0	0	0	0	-1,000,000	0	0	0	0	-1,000,000
2	250,000	80,000	15,980	18,000*	-2,020	79,129	100,000	-20,871	272,891	82,520**	-66,540	100,000	9,738	306,802
3	250,000	140,000	10,340	0	10,340	45,844	0	45,844	193,816	17,480	-7,140	0	49,123	208,012
4	250,000	120,000	12,220	0	12,220	54,179	0	54,179	183,601	0	12,220	0	54,179	183,601
5	250,000	100,000	14,100	0	14,100	62,514	0	62,514	173,386	0	14,100	0	62,514	173,386
6	237,500	100,000	12,925	0	12,925	57,305	0	57,305	167,271	0	12,925	0	57,305	167,271
7	225,625	100,000	11,809	0	11,809	52,355	0	52,355	161,461	0	11,809	0	52,355	161,461
8	214,344	90,000	11,688	0	11,688	51,822	0	51,822	150,834	0	11,688	0	51,822	150,834
9	203,627	90,000	10,681	0	10,681	47,355	0	47,355	145,591	0	10,681	0	47,355	145,591
10	193,445	90,000	9,724	0	9,724	43,112	0	43,112	140,609	0	9,724	0	43,112	140,609
11	183,773	90,000	8,815	0	8,815	39,081	0	39,081	135,878	0	8,815	0	39,081	135,878
12	174,584	0	16,411	0	16,411	72,760	0	72,760	85,413	0	16,411	0	72,760	85,413
13	165,855	0	15,590	0	15,590	69,122	0	69,122	81,143	0	15,590	0	69,122	81,143
14	157,562	0	14,811	0	14,811	65,666	0	65,666	77,086	0	14,811	0	65,666	77,086
15	149,684	0	14,070	0	14,070	62,382	0	62,382	73,231	0	14,070	0	62,382	73,231
16	142,200	0	13,367	0	13,367	59,263	0	59,263	69,570	0	13,367	0	59,263	69,570
17	135,090	0	12,698	0	12,698	56,300	0	56,300	66,091	0	12,698	0	56,300	66,091
18	128,336	0	12,064	0	12,064	53,485	0	53,485	62,787	0	12,064	0	53,485	62,787
19	121,919	0	11,460	0	11,460	50,811	0	50,811	59,648	0	11,460	0	50,811	59,648
20	115,823	0	10,887	0	10,887	48,270	0	48,270	56,665	0	10,887	0	48,270	56,665
21	110,032	0	10,343	0	10,343	45,957	0	45,957	53,832	0	10,343	0	45,957	53,832
22	104,530	0	9,826	0	9,826	43,564	0	43,564	51,140	0	9,826	0	43,564	51,140
23	99,304	0	9,335	0	9,335	41,386	0	41,386	48,583	0	9,335	0	41,386	48,583
24	94,338	0	8,868	0	8,868	39,316	0	39,316	46,154	0	8,868	0	39,316	46,154
25	89,621	0	8,424	0	8,424	37,350	0	37,350	43,846	0	8,424	0	37,350	43,846

IRR=15.772%

IRR=16.769%

* Under present law, Alaska's ITC equals 18% of the federal ITC, or 1.8% of the qualified investment. Since the corporation has \$750,000 of other Alaskan taxable income, the \$2020 in ITC not used to shelter income from the project from tax can be used to reduce the tax on this other income. By the same token, the \$100,000 federal ITC can all be used in one year to reduce the tax on the other \$750,000 of taxable income.

** Under HB 866, Alaska's ITC would equal the federal ITC, or \$100,000 in this example. The negative figure reflects the fact that a \$100,000 Alaskan ITC would shelter not only all of the \$170,000 taxable income from the project, but would reduce to zero the \$66,540 tax on the other \$750,000 of taxable Alaskan income, and still leave some \$17,480 of ITC to spare. This \$17,480 is carried over into the next year, where it reduces to zero the \$10,340 tax liability generated by the project and reduces the taxes on the other \$750,000 by \$7,140 (reflected as a negative figure).

MEMORANDUM

DATE: May 12, 1982

TO: Senator Fischer *I.W.*

FROM: Ira Winograd, staff

RE: HB 866 am, (House Passed Version of Investment Tax Credit) Effect of 10% Investment Credit on Projected State Revenues Generated by US Borax

The 10 percent investment credit offered by the House version of HB 866 would exempt Borax from state income taxation for from fourteen to seventeen years. HB 866 would cost the state \$45 million in forgone Borax revenue.

The ten percent investment credit would generate approximately \$45 million in investment credits for Borax to apply against state income tax liability. Borax could also be the beneficiary of an additional \$32. million in excess credits.

Borax estimated that it would be liable for \$46.8 million in state income tax for the first fourteen years of operation. More recent estimates indicate that income tax liability during the first seventeen years of operation may be \$45.7 million under a high investment scenario.

Methodology

Low investment scenario	High investment scenario
	Investment to obtain full production
\$870 million*	\$1,500 million
	Investment eligible for investment credit
548.1	950
	Investment credit entitlement
44.9	77.9
	Directly Useable investment credits
44.9	45.7

* In 1982 real dollars.

Investment to obtain full production. Low figure (870) supplied by Borax to the governors office. High figure (1,500) supplied by Borax to Phil Holdsworth of the Alaska Miners Association.

Investment eligible for investment credit. Borax estimates that 63 percent of investment is eligible for investment credit. (The department of revenue estimates that 80% of investment may be eligible for investment credit.)

Investment credit entitlement equals investment eligible for investment credit multiplied by the proposed 8.2 percent net increase in investment credit. The net increase in investment credit is the difference between the H.B. 866 10% credit and the existing 1.8% credit.

Useable investment credits. Borax verified the following stream of state income tax liability (in real 1982 dollars based on an 870 million investment):

year	Tax Liability	net income	adjusted net income	adjusted tax
1	-.023 million	.2	(25.0)	0
2	-.276	2.9	(22.3)	0
3	-.374	4.0	(21.2)	0
4	-.528	5.6	(19.6)	0
5	-.541	5.8	(19.4)	0
6	2.6	27.7	2.5	.2
7	4.1	43.6	18.4	1.7
8	5.1	54.3	29.1	2.7
9	6.1	64.9	39.7	3.7
10	6.1	64.9	<u>39.7</u>	3.7
11	5.9	62.8		5.9
12	5.9	52.1		5.9
13	4.7	50.0		4.7
14	4.6	48.9		4.6
15	4.5	47.9		4.5
16	4.5	47.9		4.5
17	4.6	48.9		4.6
Total			21.9	<u>45.7</u>

The corresponding income is shown in column two, based on the existing 9.4% corporate income tax.

Column three shows the adjusted net income to account for the extra depreciation during the first ten years due to the additional 630 million investment under the high investment scenario; (870 low investment, plus 630 additional investment, equals 1,500 high investment). The department of revenue estimates that each additional investment dollar will reduce net income by 40¢ over a ten year depreciation schedule.

The fourth column shows adjusted tax liability based on decreased net income during the first ten years under the high investment scenario.

Useable investment credits cannot exceed net tax liability for the first 15 years after the investment. However, not all investment will be made before the first year of operation. After approximately the seventeenth year of operation, investment credits based on initial investments would no longer be eligible for refund. Under the high investment scenario, only \$45.9 would be eligible for credit refund. Excess investment credit would be \$32.2 million.



ALASKA MINERS ASSOCIATION, INC.

509 W. Third Ave., Suite 17, Anchorage, Alaska 99501 (907) 276-0347

May 5, 1982

The Honorable Vic Fisher, Chairman
Senate State Affairs Committee
Alaska State Legislature
Pouch V (MS 3100)
Juneau, Alaska 99811

Dear Senator Fisher:

The Statewide Board of Directors of the Alaska Miners Association unanimously passed the attached resolution urging enactment of HB-866. The Alaska Miners Association represents approximately 1400 miners located throughout Alaska.

The Alaska Miners Association believes that the investment tax credits proposed in HB-866 will broaden Alaska's economic base. The people of Alaska are concerned about our state's dependence upon oil revenues. We feel diversification of our state's economy is very important for the long term economic health of Alaska.

Many members of the legislature may be hesitant to consider a tax credit bill in the face of declining oil revenues. However, HB-866 is an incoming-producing bill. It will send a strong signal to investors that Alaska is seriously attempting to attract mineral development and increase exploration and mining activity. The economic benefits accruing to the state will far outweigh the revenues lost by the tax credit.

The initial reduction in revenues by mineral investment would be small, less than ten million dollars annually. The tax credits will make Alaskan mineral investments more competitive on a world wide basis and lead to the establishment of a long term healthy mining industry.

We are asking for your help to obtain passage of this bill and make an investment in Alaska's long term economic future.

Sincerely yours,

David A. Heatwole
President

DAH/dlw



ALASKA MINERS ASSOCIATION, INC.

509 W. Third Ave., Suite 17, Anchorage, Alaska 99501 (907) 276-0347

RESOLUTION - HOUSE BILL-866

Whereas the Alaska Miner's Association desires to foster the development of Alaska's mineral resources and,

Whereas the people of Alaska desire to broaden the economic basis of our state and,

Whereas the Investment Tax Credits proposed in HB-866 would provide financial incentives for the development of minerals in Alaska.

The Board of Directors hereby resolves to urge the Speaker of the Alaska State House and the President of the Alaska State Senate, for expeditious passage of HB-866.

Approved

Fairbanks, Alaska

March 30, 1982

David A. Heatwole - President

Sandra M. Thomas - Secretary

SENATOR FISHER AND MEMBERS OF THE COMMITTEE

My name is Lance Anderson and I am Vice President of Finance for Cook Inlet Region, Inc.

Cook Inlet Region, Inc. supports passage of H.B. 866 because we believe:

First, that the bill will encourage additional investments into the State of Alaska's non oil and gas basic resource industries. By encouraging investment in those presently marginal industries through a temporary tax decrease the State is encouraging the private sector to accelerate the diversification of the State's economy and employment base.

Second, we believe passage of this bill sends a clear policy signal that the State is interested in participating and encouraging these industries by rewarding successful capital investment in the State.

During the past several months I have had many opportunities to discuss this bill with many different people. If I may at this time, I would like to answer some of the most common questions asked of me.

WHO QUALIFIES FOR THE TAX CREDIT?

All corporations paying Alaska corporate income taxes to the State could utilize the special tax credit to the extent they invest in qualified investment tax property in the specified targeted industries.

WHAT IS "QUALIFIED INVESTMENT TAX PROPERTY?"

Qualified investment tax property is primarily tangible personal property, i.e., trucks, manufacturing equipment, etc. It does not include roads, buildings, mine sites, feasibility studies, overhead, etc. In a development project the amount of qualifying property will only be a part of the total investment in the project.

HOW IS THE INVESTMENT TAX CREDIT COMPUTED?

First the amount of the actual investment in qualifying property by a corporation is determined. Then the property is grouped by useful lives and the following percentages are multiplied times the property basis:

0 to 3 Years	-0-
3 to 5 Years	-1/3-
5 to 7 Years	-2/3-
Excess of 7 Years	All-

The result is then multiplied by 10% to determine the tax credit.

For example, if a \$10,000 truck having a 6 year useful life was purchased and used in a mining project, \$6,667 of the basis would qualify and the amount of the credit would be \$667. The \$667 could then be used to reduce the corporate income tax due on the company's profits.

WHAT IMPACT WOULD THIS BILL HAVE ON PROJECTIONS OF STATE REVENUES?

The bill should have a very minimal impact on current projections of State revenues. At present, only minimal amounts are being invested in the farming, fishing, timber and mining industries by tax paying corporations. If the

Montana
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passage of this bill succeeds in its intended purpose of increasing the investment in these resources, the fiscal impact on State revenues of the bill should be positive rather than negative. Additionally, investments in these industries could substantially expand local governments' sales and property tax bases.

THEN WHY DOES THE DEPARTMENT OF REVENUE PROJECT A NEGATIVE FISCAL NOTE?

It is difficult to understand the basis of the Department of Revenue's fiscal note. For F.Y. '82, the non oil and gas corporate income tax will only generate approximately 25 to 30 million dollars. For example, for the Department's F.Y. '83 fiscal note to be correct, all of the tax paying corporations in Alaska including Penneys, Safeway, Wien, etc., would have to invest \$115,000,000 in qualified property in the four specified industries to generate the projected \$11.5 million revenue loss. This is not a realistic assumption.

WON'T THE STATE LOSE \$82,000,000 ALONE ON THE U.S. BORAX DEVELOPMENT?

Certainly not. This erroneous calculation was made in the Department of Revenue's fiscal note by assuming all of U.S. Borax's proposed one billion dollar investment would fully qualify for the tax credit. Obviously the substantial portion of U.S. Borax's investment will be for non-qualifying property such as roads, buildings, housing, and the mine development itself. Only a limited amount will be expended on the actual mining equipment which would qualify for the special investment tax credit.

ISN'T THIS BILL JUST ANOTHER SUBSIDY TO A SPECIAL INTEREST?

The investment tax credit is not a subsidy but rather a temporary tax reduction directly tied to profitable investment. The impact of the bill is beyond any special interest because of the broad impact it hopefully will have on industries that are Statewide.

WHY IS CIRI SO INTERESTED IN THE PASSAGE OF THIS BILL?

CIRI's interest in passage of this bill is directly related to the company's experiences in attempting to develop its natural resource base including Beluga coal, Seldovia chrome and other hardrock possibilities. When ANCSA passed in 1971 there was great optimism about releasing the "great wealth" held by the Native lands to the Regional Corporations, the stockholders and indirectly to the State economy. To date, to the best of my knowledge, there is not one major subsurface estate development underway on Native lands. The primary reasons for this are:

1. the delay in transfer of the lands.
2. the long lead times necessary to locate and develop mineral properties.
3. the costly infrastructure required and the decline in metal prices.
4. the lack of adequate capital by the Native Corporations for the tremendous investments required, and therefore the need to locate and negotiate major joint venture partners with the expertise and capital necessary.

This bill assists in overcoming some of the problems with attracting capital and convincing joint venture partners of the positive State policy towards development.

WON'T AN INVESTMENT DECISION BE MADE IRREGARDLESS OF A TAX CREDIT?

This is an academic argument that has been debated for twenty years since John F. Kennedy introduced the first investment tax credit in 1961. Since that

time the investment tax credit has been expanded and used on a Federal tax basis to encourage investment in

- (1) Historical buildings rehabilitation
- (2) Business energy saving devices
- (3) Research facilities
- (4) Single purpose agriculture structures
- (5) Pollution control facilities

Currently discussion is underway to extend the investment tax credit to rehabilitation of the central business core of many of America's larger cities. I think based on the continued expansion of the tax credit I would have to conclude that the conventional wisdom is that the investment tax credit is an effective tool to encourage additional investment in targeted areas.

I thank you for this opportunity to testify and will be pleased to answer any questions you may have.

SENATE STATE AFFAIRS COMMITTEE

Testimony of Dave Heatwole

for

HOUSE BILL 866

MAY 6, 1982

My name is Dave Heatwole and I am here to represent Alaska's mining industry. I am President of the Alaska Miner's Association, representing some 1,400 miners from large and small companies, and I have spent my entire career in the mining industry.

I believe all of you can agree with me that most Alaskans are very concerned about broadening our state's economic base. Why are we so dependent upon oil revenues? What are we going to do when the oil runs out?, are questions frequently asked by Alaskan public forums. What I would like to do today is give you some idea what the future hard rock mining industry could do for Alaska's economy and tell you why House Bill 866 is important to stimulate mining activity in our state.

Historically mining has always been important to Alaska--The discovery of gold at the turn of the century led to Alaska's first great economic boom. Hard rock mining became active in the early 1900's with the development of the Kennecott and Alaska-Juneau mines. Mining was the mainstay of Alaska's economy until men and material restrictions of the second world war forced the closure of Alaska mines. After the war, mining never really got started again, lower 48 and foreign producers attracted investment capital and with the exception of a few gold mines, and major mining activity never really got started again in Alaska.

In the late 1960's - early 70's, a few major mining companies returned to Alaska to begin mineral exploration programs. These companies returned to Alaska to begin mineral exploration programs, because foreign expropriation and pending domestic mineral shortages-made domestic mineral investment much more attractive. Alaska offered the United State's last great unexplored frontier. This recent mineral exploration activity has produced a few major world class discoveries:

- o The Ambler Deposits of Southeast Brooks Range.
- o The Red Dog Deposits in Delong Mts., North of Kotzebue.
- o The Brady Glacier Cu-Ni Deposit.
- o The Quartz Hill Deposit and;

In Juneau's back yard the Green's Creek Deposit.

The Gross Metal value-of these deposits, based on published figures--is on the order of \$50 billion, close to the pre- OPEC value of Prudhoe Bay.

The development of these deposits could create a substantial addition to Alaska's economy--mining, unlike oil, is a very labor intensive business, a majority of the new wealth created would stay in the state in the form of wages and goods purchased. John Whitney, a noted mineral economist, in 1979 predicted that the development of the deposits of NW Alaska, Red Dog and Ambler would create over 1,000 new jobs in Alaska and produce annual gross sales on the order of \$570 million (1979 dollars). Given the right conditions by the year 2,000, there could be 10 or more developments of this scale in Alaska.

I hope I have convinced you that mining has the potential to significantly impact Alaska's future economy. The development of major mining, depends on two factors:

1. Availability of infrastructure.
2. A stable investment climate.

I am not going to discuss infrastructure today, suffice to say it is of equal importance to investment climate.

Alaskan mineral deposits are going to have to compete on a world-wide basis. Copper produced in Alaska is going to be sold at the same price as that produced in Western U.S., South America, or South Africa. Therefore, to be competitive, costs of production must be comparable. Fortunately, nature has given Alaska some high grade deposits, which will help keep them competitive, but Alaskan costs are high.

The investment tax credits proposed in House Bill 866 will help keep the cost of Alaskan mineral development competitive. It will allow investors to recoup their risk capital quicker, making the Alaskan investment more attractive. But more importantly, enactment of House Bill 866 will send a strong signal to outside investors that the State of Alaska is serious about developing its mineral industry by providing incentives for investment.

As I have stated in my letter, House Bill 866 should be considered an income producing bill. The immediate cost of enactment is very small, but potential impact on the Alaska's future economy is quite substantial. For a diversified economy in Alaska, I urge you to pass this bill.

MEMORANDUM

DATE: May 4, 1982

TO: Senator Vischer

FROM: Ira Winograd, staff *I.W.*

RE: HB 866, Investment Credits - Effect on Borax, and Benefits Already
Conferred to Renewable Resource Industries

BORAX

Upon full operation, Borax estimates that state corporate income tax liability will be \$5 million per year, and \$40 to \$60 for the life of the original equipment. Under HB 866, the Department of Revenue estimates that Borax will have \$86 million additional state investment credits. Thus, Borax would not pay any income tax. (Borax would still be liable for license fees.) The Department of Revenue estimates that the Borax mine will cause an increase in state budgetary expenditures of \$12.5 million per year. (All figures are in 1982 dollars.)

TIMBER

Among tax breaks already given to the timber industry are the following:

corporate income tax revenues. The FY 1981 general [non-petroleum]
corporate income tax yield was \$34,800,000. $.03 \times 34.8 = 1.04$)

Fisheries revenues (\$29.2 million) equaled 1.3 percent of total state
revenues (\$2,282.6 million) in 1981, and state expenditures on fisheries
were 2.2 percent of the state budget.

1. The effect of section 631 of IRS code is that timber companies are only taxed on 60% of their income. (The difference between fair market value and the cost of their own timber is treated as a capital gain. Capital gain maximum tax liability is 28% instead of the maximum 46% tax rate applied to corporate income in non-timber industries. [.6 = .28/.46] The rationale for section 631 is that it encourages reforestation.)

2. Seedlings are typically supplied at a discount through government agencies.

AGRICULTURE

The state has appropriated \$114,624,800 since 1979 to develop agriculture. According to the legislative finance division, expenditures are as follows:

Delta I	13,883,000
Pt. McKenzie	5,025,000
Nenana/Totchaket	500,000
DNR	495,700
U of Ak.	25,749,400
Rural Ag.	2,147,000
ARLF	20,719,200
Capital Proj.	41,137,400
Operating Bud.	<u>4,967,300</u>
Total	\$114,624,800

The industry has generated little, if any, corporate tax revenues to offset these expenditures.

Excerpts from, "Financing Agricultural Projects in Alaska", House Research Agency

State programs for financing agriculture include land contracts offered by the Department of Natural Resources, clearing loans through the Agricultural Action Council, and loans for development and operations of both project and non-project commercial agricultural ventures through the Agricultural Revolving Loan Fund.

The ARLF holds about 50 percent of the \$47 million of farm credit outstanding in Alaska. Land contracts and clearing loans bring the state share to 80 percent of total farm credit in Alaska.

The state's dominant position in the farm credit market is due primarily to the interest rate differential between state programs and other sources of credit. The current interest rate through state programs is six percent versus the 12 percent or higher available through other major lenders.

If state support continues at current levels, loan demand for operation and development of project acreage is expected to peak at \$91 million (1981 dollars) outstanding in 1989. Capital project infrastructure improvements are expected to cost an additional \$23 million, with operating losses totaling nearly \$5 million per year for several years.

Other projected state expenditures for roads, bridges, surveying, administration, etc. is anticipated to be \$49 million (1981 dollars) in land-related appropriations through 1990.

FISHERIES

Excerpts from, "The Alaska Fishing Industry", House Research Agency

State appropriations for programs related to commercial fishing totaled about 120 million in FY 1982. The appropriations were distributed as follows:

fisheries financing programs	56.3 million
management and regulation	30.5 million
fisheries development & marketing	24.1 million
capital improvements	<u>8.8 million</u>
total	\$119,700,000

Fisheries expenditures were 2.2 percent of the state budget in 1978, 79, 80 and 81.

State revenue from non-corporate fish taxes and fees levied on the fishing industry totalled \$28.2 million in FY 1981.

I estimate that the fisheries contributed an additional \$1,044,000 million in corporate income tax payments in F.Y. 1981. (In 1979 the Dept. of Rev. calculated that the fisheries contributed 3% of general

Here are a few tips on how to read those new annual reports intelligently.

Numbers Game

Reading between the lines

By Aaron Bernstein

WITH ANNUAL REPORTS arriving in the mail almost daily now, a short primer on what to look for this year may be in order.

A joyous LIFO

You've probably always thought of LIFO (last in, first out) inventory accounting as a conservative technique that tends to depress earnings. That's generally true. But, since LIFO matches current sales against latest costs, earnings can be dramatically buoyed when inventories are cut and the latest costs get older and older, lower and lower.

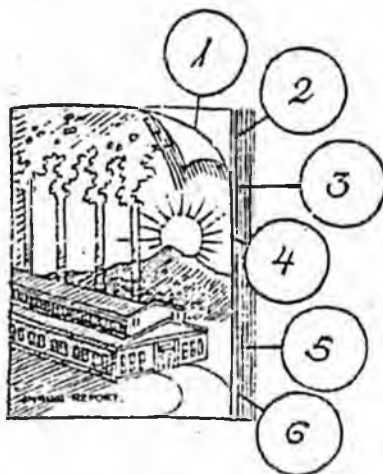
"A full year of high interest rates and slow sales has led to strong pressure to cut inventories," says Seidman & Seidman's Harvey Moskowitz. "This is something I think readers should look for because it inflates earnings."

Take Texaco. High interest rates and an oil glut caused Texaco to cut inventories by 16%. The LIFO cushion that was built into those barrels over the years amounted to \$454 million, and transformed what would have been a drop in net income into a modest gain. Texaco's annual report revealed that.

Spicing up income

Last year a number of firms received a much-needed shot in the arm from the Economic Recovery Tax Act's provision for selling tax benefits. These sales are one-time deals and shouldn't be confused with higher earnings resulting from better sales or margins.

Moore McCormack Resources, a \$766 million natural resources conglomerate, for instance, netted a nice \$5.5 million from sales of investment



credits and depreciation deductions. That brought net income up to \$51.3 million in 1981 from \$47 million in 1980. Without those sales, income for 1981 is down slightly from the previous year.

It sounds better in translation

For years now, companies have been complaining about the adverse effect of accounting for foreign currency translations. Now that the FASB has finally taken steps to make translations painless, you can bet that companies aren't going to complain in their presidents' letters that earnings have been improved as a result.

Although the new rule, FASB Statement 52, won't be mandatory until Dec. 15, 1982, a number of firms elected to adopt it last year. In fact, some even picked up the new accounting method retroactively, which the FASB permits.

Xerox chose to take advantage of the new rule this way and altered its results back four years. Net income as reported in their new annual is \$7.08 in 1981, up from \$6.69 in 1980 and \$6.12 in 1979.

Without the new rule, Xerox' 1981 net income drops 31 cents, to \$6.77, as compared with increases to \$7.24

in 1980 and \$6.60 the year before. A somewhat different picture.

Watch the actuaries

With interest rates seemingly glued to the heavens, a number of firms have changed their assumptions about how much money their pension plans will earn for many years to come. By raising your interest rate assumptions, you can put vastly fewer dollars into the pension plan in a given year. Presto: higher earnings.

General Motors, for instance, explains in a note that it changed its assumed rate of return on its pension fund from 6% to 7% last year. That added 69 cents a share to GM's bottom line—which amounts to over half of its \$1.07 net earnings in 1981.

Selling out

It would appear that last year was a bad one for \$1.2 billion (sales) AMF. Net income dropped almost one-third, from \$2.58 a share in 1980 to \$1.84. But this poor showing is due mostly to sale of unprofitable operations, and doesn't really reflect AMF's true status as a going concern. If you look just at the remaining businesses in each year, profits rose by 23%, from \$2.39 a share in 1980 to \$2.95 last year.

Says Moskowitz, "The recession last year forced many companies to look hard at operations that weren't carrying their own weight." As a result, it's important to determine to what extent the figures you are examining are for ongoing operations, and to what extent they include one-time writeoffs for discontinued operations.

Inequitable?

The use of equity accounting—which allows a company to show, as earnings, a percentage of the earnings of other companies in which it has a minority interest of about 20% or more—is misleading in any year. After all, the parent company never really sees any nondividend cash from those equity investments. So, when you're trying to see how much money a company really has to spend, subtract those dollars.

At Teledyne, the \$3.2 billion conglomerate, net income per share last year was \$19.96. Of this, \$3.49, or about \$72 million, came from equity accounting. That means that about 17% of Teledyne's earnings isn't Teledyne's to spend. The company actually received a mere \$18 million in dividends from the investments. ■

STATE OF ALASKA

JAY S. HAMMOND, GOVERNOR

DEPARTMENT OF REVENUE

STATE OFFICE BUILDING

POUCH SA - JUNEAU 99811

May 20, 1982

The Honorable Bill Ray, Chairman
Senate Transportation Committee
Pouch V
Juneau, AK 99811

Re: HB 866 and SCS HB 866 (SA) - Providing for an increase in the investment tax credit against the State corporate income tax

Dear Mr. Chairman:

The idea behind this legislation is ill-conceived and represents poor state policy. It is poor state policy because rich corporations stand to get far more benefit from it than poor ones. For example, I did a comparison for Senator Fischer's committee on the effect of the original version of HB 866 on the rate of return for a project standing on its own, versus that same project if it is owned by a affluent company (not even oil-company sized) having \$750,000 a year of taxable Alaska income from other business activities. The improvement in the rate of return would be nearly three times greater for the big business than it would be for the little guy just starting out. For the large oil companies, the disproportion would be somewhat greater still.

The Bill is ill-conceived because the effect on investment rates of return as the result of increasing this investment tax credit (ITC) is too small to have any economic meaning, despite claims to the contrary by its supporters. A project will go forward or not go forward, because of other factors than the ITC. Even in the case of the rich corporation that I prepared for Senator Fischer, the improvement in the internal rate of return on the investment was less than one percentage point. The effect of assuming only a 10 percent higher operating margin over the life of the project was four and a quarter times greater. And, that was when the Bill still provided that the new state ITC would be 100% of the federal ITC. Under the State Affairs CS, the state ITC would be only 36% of the federal ITC, which would make the change in the rate of return vanishingly small.

There are other reasons not to pass this Bill or some variation of it. First, mining already enjoys a three-year "holiday" from paying the mining license tax, from the time the mine starts operating. Second, the amount of qualified investment on which the ITC is computed was

Senator Ray (re HB 866)
May 20, 1982
Page 2

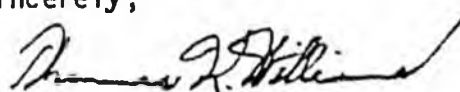
increased last year 40-fold, from \$500,000 to \$20,000,000; increasing the percentage of that investment which may be deducted dollar for dollar against the income tax is too much of a good thing. Third, corporations last year were given a significant tax break, particularly the smaller ones, by the decrease in state income tax rates on the first \$90,000 of taxable income (for example, the first \$10,000 of taxable income is taxed now at only one percent, as opposed to 5.4 percent before last year's rate change). Fourth, by whittling away at the non-petroleum tax base of the State, we not only make the State finances more vulnerable to the vagaries of the world oil market, but we also tend to furnish factual support for the type of tax lawsuits which you may recall Dick Donaldson of SOHIO was threatening you and the Legislature with last year.

All in all, this Bill is nothing more than a give-away of State revenues with nothing for the State to show in return that it wouldn't have gotten anyway. Moreover, to the extent it conveys benefits, they are more advantageous to the rich corporations than the poor.

I am enclosing a copy of my letter to Senator Fischer, and I would welcome the opportunity to speak to you or your Committee further on this Bill if you so desire.

Thank you for your consideration.

Sincerely,



Thomas K. Williams
Commissioner of Revenue

Enclosure

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH 5
JUNEAU, ALASKA 99811
PHONE: (907) 465-2300

May 15, 1982

The Honorable Vic Fischer, Chairman
Senate State Affairs Committee
Pouch 5
Juneau, AK 99811

Re: Effects on Economic Decision-Making from Increasing the State
Investment Tax Credit as Proposed in House Bill 866

Dear Mr. Chairman:

In my testimony before the Committee I stated that increasing the State's investment tax credit as proposed in HB 866 would have only a minimal effect on the internal rate of return after taxes for new projects in Alaska. I also said that, to the extent there would be an effect on the rate of return, it would be greater for "fat cat" corporations than for small ones. I now have had the opportunity to prepare an example which demonstrates the truth of both assertions.

Suppose we have a new project in Alaska, and to avoid any distortions by making it too large, suppose further that it costs \$1,000,000, takes a year to complete and will employ 25 people. Suppose, too, that after expenses other than income taxes and depreciation, the project yields a net cash flow of \$250,000 a year for its first four years of operation, and then each year thereafter the net cash flow decreases by five percent from the previous year. Finally, let us suppose that the project qualifies for Accelerated Capital Recovery System treatment under the new tax law using a 10-year life.

The analysis I have used takes this project and compares the internal rate of return (IRR) on the investment under Alaska's present investment tax credit with the IRR under the credit proposed in HB 866. This comparison is first made with the project standing alone; that is, the investor has no other income to be sheltered from the tax benefits generated from the project. I call this Case 1. Case 2 doesn't involve too fat a "fat cat" corporation, simply one with \$750,000 a year of taxable Alaskan net income from other sources.

The tables attached to this letter show what the after-tax cash flows are under Case 1 and Case 2, both with the present investment tax credit and with the one proposed by HB 866. As you can see from those tables, the IRR under the non-"fat cat" case (Case 1) is 18.763% under

Hon. Vic Fischer (re HB 866)
May 15, 1982
Page 2

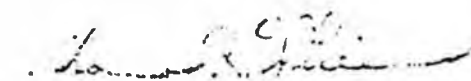
the present law and would rise by only 0.363 of a percentage point to 19.126% under HB 866. In contrast, the improvement in the rate of return for the "fat cat" case (Case 2) is nearly three times as great as for the "skinny" cat -- 0.997 of a percentage point (15.772% to 16.769%).

Note also how small a difference there is in the rate of return between present law and HB 866. The extra economic incentive from raising the State's investment tax credit is truly minimal (and you can see why: look how much higher the federal taxes would be during the early years with HB 866 than they are under present law, in both Cases 1 and 2). Other factors have much more effect on the economics of an investment than the amount of investment tax credit. For example, in Case 1, suppose one's assumptions about market prices, labor costs and other operating expenses had a 10 percent margin of error. If the net pre-tax cash flows were only 10 percent higher than the figures in the table, the increase in the rate of return would be 4.25 times that from the extra tax incentive under HB 866.

Without going on excessively, I would only reiterate my objections that HB 866 does too little economically, at too high a price for the State, to the advantage of wealthy corporations over small ones. It scarcely makes economic sense and certainly makes poor State policy.

I hope this information may prove useful to you and your Committee in considering HB 866.

Sincerely,



Thomas K. Williams
Commissioner of Revenue

Attachments

P.S. I might add parenthetically that the reason for the lower IRRs in the "fat cat" case is that all income from the project is taxed in the maximum tax bracket under both federal and state tax laws, because of the other \$750,000 of taxable income; the project represents incremental income to the corporation. In Case 1 the project stands alone, and so the first \$100,000 and first \$90,000 are taxed below the maximum rates under the federal and Alaska tax laws, respectively.

CASE 1. A NEW ALASKAN BUSINESS ON ITS OWN

Yr	Pre-Tax Cash Flow from Project	Project Depreciation	With State Investment Tax Credit Under Existing State Law						With State Investment Tax Credit under HB 86				
			AK Inc. Tax From Project Before ITC	AK ITC Applied	AK Inc. Tax From Project After ITC	US Inc. Tax From Project Before ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow	AK ITC Applied	AK Inc. Tax From Project After ITC	US ITC Applied	US Inc. Tax From Project After ITC
1	-1,000,000	0	0	0	0	0	0	-1,000,000	0	0	0	0	-1,000,000
2	250,000	80,000	12,020	12,020	0	57,950	57,950	250,000	12,020	0	57,950	0	250,000
3	250,000	140,000	6,380	5,980*	400	30,166	30,166	249,600	6,380	0	30,166	0	250,000
4	250,000	120,000	8,260	0	8,260	35,750	11,884	217,874	8,260	0	11,884	27,850	222,000
5	250,000	100,000	10,140	0	10,140	44,086	0	195,774	10,140	0	0	48,750	201,000
6	237,500	100,000	8,965	0	8,965	38,876	0	189,659	8,965	0	0	43,000	194,000
7	225,625	100,000	7,849	0	7,849	33,927	0	183,849	7,849	0	0	37,538	188,000
8	214,344	90,000	7,728	0	7,728	33,393	0	173,222	7,728	0	0	36,948	177,000
9	203,627	90,000	6,721	0	6,721	28,927	0	167,979	6,721	0	0	32,018	171,000
10	193,445	90,000	5,764	0	5,764	24,822	0	162,859	5,764	0	0	27,335	166,000
11	183,773	90,000	4,855	0	4,855	21,317	0	157,601	4,855	0	0	23,259	160,000
12	174,584	0	12,451	0	12,451	54,331	0	107,802	12,451	0	0	60,059	114,000
13	165,855	0	11,630	0	11,630	50,693	0	103,531	8,867**	2,763	0	54,772	108,000
14	157,562	0	10,851	0	10,851	47,237	0	99,474	0	10,851	0	47,237	99,000
15	149,684	0	10,110	0	10,110	43,954	0	95,620	0	10,110	0	43,954	95,000
16	142,200	0	9,407	0	9,407	40,835	0	91,958	0	9,407	0	40,835	91,000
17	135,090	0	8,738	0	8,738	37,872	0	88,480	0	8,738	0	37,872	88,000
18	128,336	0	8,104	0	8,104	35,057	0	85,176	0	8,104	0	35,057	85,000
19	121,919	0	7,500	0	7,500	32,383	0	82,036	0	7,500	0	32,383	82,000
20	115,823	0	6,927	0	6,927	29,842	0	79,054	0	6,927	0	29,842	79,000
21	110,032	0	6,383	0	6,383	27,429	0	76,220	0	6,383	0	27,429	76,000
22	104,530	0	5,866	0	5,866	25,216	0	73,449	0	5,866	0	25,216	73,000
23	99,304	0	5,375	0	5,375	23,322	0	70,608	0	5,375	0	23,322	70,000
24	94,338	0	4,908	0	4,908	21,522	0	67,908	0	4,908	0	21,522	67,000
25	89,621	0	4,466	0	4,466	19,812	0	65,343	0	4,466	0	19,812	65,000

IRR=18.763%

IRR=19

* Under present law, Alaska's ITC equals 18% of the federal ITC, or 1.8% of the qualified investment. As with the federal ITC, any ITC that is not used in a tax year may be carried forward into the next tax year. In this case only \$12,020 of the \$18,000 state ITC was taken in the first year; the balance of \$5,980 is taken in the second.

** Under HB 866, Alaska's ITC would equal the federal ITC, or \$100,000 in this example. This \$8,867 figure represents what remains of the \$100,000 ITC after the twelfth year of the project.

Yr	Pre-Tax Cash Flow from Project	Project Depreciation	With State Investment Tax Credit Under Existing State Law							With State Investment Tax Credit under III				
			AK Inc. Tax From Project Before ITC	AK ITC Applied	AK Inc. Tax From Project After ITC	US Inc. Tax From Project Before ITC	US ITC Applied	US Inc. Tax From Project After ITC	Net After-Tax Cash Flow	AK ITC Applied	AK Inc. Tax From Project After ITC	US ITC Applied	US Inc. Tax From Project After ITC	Aft Cas
1	-1,000,000	0	0	0	0	0	0	0	-1,000,000	0	0	0	0	-1,000,000
2	250,000	80,000	15,980	18,000*	-2,020	79,129	100,000	-20,871	272,891	82,520**	-66,540	100,000	9,738	316,281
3	250,000	140,000	10,340	0	10,340	45,844	0	45,844	193,816	17,480	-7,140	0	49,123	206,676
4	250,000	120,000	12,220	0	12,220	54,179	0	54,179	183,601	0	12,220	0	54,179	195,380
5	250,000	100,000	14,100	0	14,100	62,514	0	62,514	173,386	0	14,100	0	62,514	187,486
6	237,500	100,000	12,925	0	12,925	57,305	0	57,305	167,271	0	12,925	0	57,305	170,176
7	225,625	100,000	11,809	0	11,809	52,355	0	52,355	161,461	0	11,809	0	52,355	163,270
8	214,344	90,000	11,688	0	11,688	51,822	0	51,822	150,834	0	11,688	0	51,822	152,456
9	203,627	90,000	10,681	0	10,681	47,355	0	47,355	145,591	0	10,681	0	47,355	145,946
10	193,445	90,000	9,724	0	9,724	43,112	0	43,112	140,609	0	9,724	0	43,112	140,321
11	183,773	90,000	8,815	0	8,815	39,081	0	39,081	135,878	0	8,815	0	39,081	134,893
12	174,584	0	16,411	0	16,411	72,760	0	72,760	85,413	0	16,411	0	72,760	102,173
13	165,855	0	15,590	0	15,590	69,122	0	69,122	81,143	0	15,590	0	69,122	96,733
14	157,562	0	14,811	0	14,811	65,666	0	65,666	77,086	0	14,811	0	65,666	91,897
15	149,684	0	14,070	0	14,070	62,382	0	62,382	73,231	0	14,070	0	62,382	87,901
16	142,200	0	13,367	0	13,367	59,263	0	59,263	69,570	0	13,367	0	59,263	84,533
17	135,090	0	12,698	0	12,698	56,300	0	56,300	66,091	0	12,698	0	56,300	81,391
18	128,336	0	12,064	0	12,064	53,485	0	53,485	62,787	0	12,064	0	53,485	78,472
19	121,919	0	11,460	0	11,460	50,811	0	50,811	59,648	0	11,460	0	50,811	75,859
20	115,823	0	10,887	0	10,887	48,270	0	48,270	56,665	0	10,887	0	48,270	73,485
21	110,032	0	10,343	0	10,343	45,857	0	45,857	53,832	0	10,343	0	45,857	71,179
22	104,530	0	9,826	0	9,826	43,564	0	43,564	51,140	0	9,826	0	43,564	68,974
23	99,304	0	9,335	0	9,335	41,386	0	41,386	48,583	0	9,335	0	41,386	66,869
24	94,338	0	8,868	0	8,868	39,316	0	39,316	46,154	0	8,868	0	39,316	64,868
25	89,621	0	8,424	0	8,424	37,350	0	37,350	43,846	0	8,424	0	37,350	62,974

IRR=15.772%

IRR=

* Under present law, Alaska's ITC equals 18% of the federal ITC, or 1.8% of the qualified investment. Since the corporation has \$750,000 of other Alaskan taxable income, the \$2020 in ITC not used to shelter income from the project from tax can be used to reduce the tax on this other income. By the same token, the \$100,000 federal ITC can all be used in one year to reduce the tax on the other \$750,000 of taxable income.

** Under HB 866, Alaska's ITC would equal the federal ITC, or \$100,000 in this example. The negative figure reflects the fact that a \$100,000 Alaskan ITC would shelter not only all of the \$170,000 taxable income from the project, but would reduce to zero the \$66,540 tax on the other \$750,000 of taxable Alaskan income, and still leave some \$17,480 of ITC to spare. This \$17,480 is carried over into the next year, where it reduces to zero the \$10,340 tax liability generated by the project and reduces the taxes on the other \$750,000 by \$7,140 (reflected as a negative figure).

- FILE -

STATE OF ALASKA

DEPARTMENT OF REVENUE

OFFICE OF THE COMMISSIONER

JAY S. HAMMOND, GOVERNOR

POUCH S
JUNEAU, ALASKA 99811
PHONE: (907) 465-2300

May 24, 1982

The Honorable Bill Ray
Chairman
Senate Transportation Committee
Room 103 - Capitol Building
Juneau, Alaska

Re: Senate CS for House Bill No. 866 (State Affairs)

Dear Senator Ray:

Senate CS for House Bill No. 866 (State Affairs), an Act establishing a special tax credit, was given an additional referral on May 17, 1982 to the Senate Transportation Committee.

For the consideration of the Senate Transportation Committee, I am enclosing a copy of a Fiscal Note prepared by Mr. Robert R. Kessel, Director, Audit Division, Department of Revenue concerning the proposed legislation.

Sincerely,



R. D. Stevenson
Special Assistant

Enclosure

cc: Joseph K. Donohue
Deputy Commissioner
Department of Revenue

Robert R. Kessel, Director
Audit Division
Department of Revenue

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST

Bill/Resolution Number: SCSHB 866 (SA)

Title: Special investment tax credit

Requested by: Senate Transportation Committee Date: May 24, 1982

II. FISCAL DETAIL

Agency Affected: Department of Revenue

Program Category Affected: General Government

BRU, Program, or Subprogram(s) Affected: Audit Division

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
100 PERSONAL SERVICES	-	-	-	-	-	-
200 TRAVEL	-	-	-	-	-	-
300 CONTRACTUAL	-	-	-	-	-	-
400 COMMODITIES	-	-	-	-	-	-
500 EQUIPMENT	-	-	-	-	-	-
600 LAND & STRUCTURES	-	-	-	-	-	-
700 GRANTS, CLAIMS, ETC	-	-	-	-	-	-
800 MISCELLANECUS	-	-	-	-	-	-
TOTAL	0	0	0	0	0	0

FUNDING (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	-	-	-	-	-	-
OTHER (Specify Source)	-	-	-	-	-	-

POSITIONS

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

III. ANALYSIS (See Fiscal Note Preparation Instruction, Section III)

Although there would not be additional administrative expense incurred as a result of enactment of the proposed legislation, this CS would double the State investment tax credit (ITC) to 36% of the federal ITC (vs. 100% of the federal ITC under its original version). The extra large ITC is limited to mining only, instead of extending to farm and timber ventures also as it did before. It appears the limitation of \$20,000,000 on qualifying investment under AS 43.20.036(b) would NOT apply to mining investments under this Bill -- in other words, the sky's the limit in terms of how much investment could give rise to this enlarged ITC. This CS provides for a repeal of its new ITC provisions on December 31, 1986.

IV. DATE: May 24, 1982

PREPARED BY: Robert R. Kessel

AGENCY: Audit Division

PHONE: 465-2320

Original: Legislative Finance

cc: Budget and Management

Prime Sponsor (First Legislator Named)

33-001 (Rev. 12/81)

STATE OF ALASKA

DEPARTMENT OF REVENUE

JAY S. HAMMOND, GOVERNOR

STATE OFFICE BUILDING

POUCH SA - JUNEAU 99811

May 20, 1982

The Honorable Bill Ray, Chairman
Senate Transportation Committee
Pouch Y
Juneau, AK 99811

Re: HB 866 and SOS HB 866 (SA) - Providing for an increase in the investment tax credit against the State corporate income tax

Dear Mr. Chairman:

The idea behind this legislation is ill-conceived and represents poor state policy. It is poor state policy because rich corporations stand to get far more benefit from it than poor ones. For example, I did a comparison for Senator Fischer's committee on the effect of the original version of HB 866 on the rate of return for a project standing on its own, versus that same project if it is owned by a affluent company (not even oil-company sized) having \$750,000 a year of taxable Alaska income from other business activities. The improvement in the rate of return would be nearly three times greater for the big business than it would be for the little guy just starting out. For the large oil companies, the disproportion would be somewhat greater still.

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There are other reasons not to pass this Bill or some variation of it. First, mining already enjoys a three-year "holiday" from paying the mining license tax, from the time the mine starts operating. Second, the amount of qualified investment on which the ITC is computed was

Senator Ray (re HB 866)
May 20, 1982
Page 2

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All in all, this Bill is nothing more than a give-away of State revenues with nothing for the State to show in return that it wouldn't have gotten anyway. Moreover, to the extent it conveys benefits, they are more advantageous to the rich corporations than the poor.

I am enclosing a copy of my letter to Senator Fischer, and I would welcome the opportunity to speak to you or your Committee further on this Bill if you so desire.

Thank you for your consideration.

Sincerely,



Thomas K. Williams
Commissioner of Revenue

Enclosure

- FILE -

THE LEGISLATURE OF THE STATE OF ALASKA
TWELFTH LEGISLATURE

FISCAL NOTE

I. REQUEST

Bill/Resolution Number: SCSHB 866 (SA)

Title: Special investment tax credit

Requested by: Senate Transportation Committee Date: May 24, 1982

II. FISCAL DETAIL

Agency Affected: Department of Revenue

Program Category Affected: General Government

BRU, Program, or Subprogram(s) Affected: Audit Division

(Note: If more than one budget component is affected, separate line-item amounts and funding for each component in the analysis section.)

EXPENDITURES (Thousands of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
100 PERSONAL SERVICES	-	-	-	-	-	-
200 TRAVEL	-	-	-	-	-	-
300 CONTRACTUAL	-	-	-	-	-	-
400 COMMODITIES	-	-	-	-	-	-
500 EQUIPMENT	-	-	-	-	-	-
600 LAND & STRUCTURES	-	-	-	-	-	-
700 GRANTS, CLAIMS, ETC	-	-	-	-	-	-
800 MISCELLANEOUS	-	-	-	-	-	-
TOTAL	0	0	0	0	0	0

FUNDING (Thousands of Dollars)

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	-	-	-	-	-	-
OTHER (Specify Source)	-	-	-	-	-	-

POSITIONS

	FY 82	FY 83	FY 84	FY 85	FY 86	FY 87
FULL TIME	-	-	-	-	-	-
PART TIME	-	-	-	-	-	-
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III. ANALYSIS (See Fiscal Note Preparation Instruction, Section III)

Although there would not be additional administrative expense incurred as a result of enactment of the proposed legislation, this CS would double the State investment tax credit (ITC) to 36% of the federal ITC (vs. 100% of the federal ITC under its original version). The extra large ITC is limited to mining only, instead of extending to farm and timber ventures also as it did before. It appears the limitation of \$20,000,000 on qualifying investment under AS 43.20.036(b) would NOT apply to mining investments under this Bill -- in other words, the sky's the limit in terms of how much investment could give rise to this enlarged ITC. This CS provides for a repeal of its new ITC provisions on December 31, 1986.

IV. DATE: May 24, 1982

PREPARED BY: Robert R. Kessel

AGENCY: Audit Division

PHONE: 465-2320

Original: Legislative Finance

cc: Budget and Management

Prime Sponsor (First Legislator Named)

STATE OF ALASKA

DEPARTMENT OF REVENUE

STATE OFFICE BUILDING

POUCH SA - JUNEAU 99811

JAY S. HAMMOND, GOVERNOR

May 20, 1982

The Honorable Bill Ray, Chairman
Senate Transportation Committee
Pouch M
Juneau, AK 99811

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Dear Mr. Chairman:

The idea behind this legislation is ill-conceived and represents poor state policy. It is poor state policy because rich corporations stand to get far more benefit from it than poor ones. For example, I did a comparison for Senator Fischer's committee on the effect of the original version of HB 866 on the rate of return for a project standing on its own, versus that same project if it is owned by a affluent company (not even oil-company sized) having \$750,000 a year of taxable Alaska income from other business activities. The improvement in the rate of return would be nearly three times greater for the big business than it would be for the little guy just starting out. For the large oil companies, the disproportion would be somewhat greater still.

The Bill is ill-conceived because the effect on investment rates of return as the result of increasing this investment tax credit (ITC) is too small to have any economic meaning, despite claims to the contrary by its supporters. A project will go forward or not go forward, because of other factors than the ITC. Even in the case of the rich corporation that I prepared for Senator Fischer, the improvement in the internal rate of return on the investment was less than one percentage point. The effect of assuming only a 10 percent higher operating margin over the life of the project was four and a quarter times greater. And, that was when the Bill still provided that the new state ITC would be 100% of the federal ITC. Under the State Affairs CS, the state ITC would be only 36% of the federal ITC, which would make the change in the rate of return vanishingly small.

There are other reasons not to pass this Bill or some variation of it. First, mining already enjoys a three-year "holiday" from paying the mining license tax, from the time the mine starts operating. Second, the amount of qualified investment on which the ITC is computed was

Senator Ray (re HB 866)
May 20, 1982
Page 2

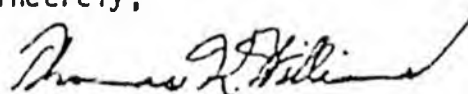
increased last year 40-fold, from \$500,000 to \$20,000,000; increasing the percentage of that investment which may be deducted dollar for dollar against the income tax is too much of a good thing. Third, corporations last year were given a significant tax break, particularly the smaller ones, by the decrease in state income tax rates on the first \$90,000 of taxable income (for example, the first \$10,000 of taxable income is taxed now at only one percent, as opposed to 5.4 percent before last year's rate change). Fourth, by whittling away at the non-petroleum tax base of the State, we not only make the State finances more vulnerable to the vagaries of the world oil market, but we also tend to furnish factual support for the type of tax lawsuits which you may recall Dick Donaldson of SOHIO was threatening you and the Legislature with last year.

All in all, this Bill is nothing more than a give-away of State revenues with nothing for the State to show in return that it wouldn't have gotten anyway. Moreover, to the extent it conveys benefits, they are more advantageous to the rich corporations than the poor.

I am enclosing a copy of my letter to Senator Fischer, and I would welcome the opportunity to speak to you or your Committee further on this Bill if you so desire.

Thank you for your consideration.

Sincerely,



Thomas K. Williams
Commissioner of Revenue

Enclosure

HJR

20

THE ALASKA RAILROAD ACT,
signed into law March 12, 1914,
(38 Stat. 305) states:

"The President of the United States is empowered, authorized, and directed to designate and cause to be located in the Territory of Alaska not to exceed in the aggregate one thousand miles, to be so located as to connect one or more of the open Pacific Ocean harbors on the southern coast of Alaska with the navigable waters in the interior of Alaska, and with a coal field or fields so as best to aid in the development of the agricultural and mineral or other resources of Alaska, and the settlement of the public lands therein...."

RAILROADS, TELEGRAPH, AND TELEPHONES

§ 1. Railroad; location, construction, and operation.—The President of the United States is empowered, authorized, and directed to adopt and use a name by which to designate the railroad or railroads and properties to be located, owned, acquired, or operated under the authority of sections 301 to 305 of this title; to employ such officers, agents, or agencies,

in his discretion, as may be necessary to enable him to carry out the purposes of sections 301 to 305; to authorize and require such officers, agents, or agencies to perform any or all of the duties imposed upon him by the terms of sections 301 to 305; to detail and require any officer or officers in the Engineer Corps in the Army or Navy to perform service under sections 301 to 305; to fix the compensation of all officers, agents, or employees appointed or designated by him; to designate and cause to be located a route or routes for a line or lines of railroad in the Territory of Alaska not to exceed in the aggregate one thousand miles, to be so located as to connect one or more of the open Pacific Ocean harbors on the southern coast of Alaska with the navigable waters in the interior of Alaska, and with a coal field or fields so as best to aid in the development of the agricultural and mineral or other resources of Alaska, and the settlement of the public lands thereof, and so as to provide transportation of coal for the Army and Navy, transportation of troops, arms, munitions of war, the mails, and for other governmental and public uses and for the transportation of passengers and property; to construct and build a railroad or railroads along such route or routes as he may so designate and locate, with the necessary branch lines, feeders, sidings, switches, and spurs; to purchase or otherwise acquire all real and personal property necessary to carry out the purposes of sections 301 to 305; to exercise the power of eminent domain in acquiring property for such use, which use is declared to be a public use, by condemnation in the courts of Alaska in accordance with the laws now or hereafter in force there; to acquire rights of way, terminal grounds, and all other rights; to purchase or otherwise acquire all necessary equipment for the construction and operation of such railroad or railroads; to build or otherwise acquire docks, wharves, terminal facilities, and all structures needed for the equipment and operation of such railroad or railroads; to fix, change, or modify rates for the transportation of passengers and property, which rates shall be equal and uniform, but no free transportation or passes shall be permitted except that the provisions of the interstate commerce laws relating to the transportation of employees and their families shall be in force as to the lines constructed under sections 301 to 305; to receive compensation for the transportation of passengers and property, and to perform generally all the usual duties of a common carrier by railroad; to make and establish rules and regulations for the control and operation of said railroad or railroads; in his discretion, to lease the said railroad or railroads, or any portion thereof, including telegraph and telephone lines, after completion under such terms as he may deem proper, but no lease shall be for a longer period than twenty years, or in the event of failure to lease, to operate the same until the further action of Congress. If said railroad or railroads, including telegraph and telephone lines, are leased under the authority given under sections 301 to 305, then and in that event they shall be operated under the jurisdiction and control of the provisions of the interstate commerce laws; to purchase, condemn, or otherwise acquire upon such terms as he may deem proper any other line or lines of railroad in Alaska which may be necessary to complete the construction of the line or lines of railroad designated or located by him. The price to be paid in case of purchase shall in no case exceed the actual physical value of the railroad; to make contracts or agreements with any railroad or steamship company or vessel owner for joint transportation of passengers or property over the road or roads herein provided for, and such railroad or steamship line or by such vessel, and to make such other contracts as may be necessary to carry out any of the purposes of sections 301 to 305; to utilize in carrying on the work herein provided for any and all machinery, equipment, instruments, material, and other property of any sort whatsoever used or acquired in connection

with the construction of the Panama Canal, so far and as rapidly as the same is no longer needed at Panama, and the successors to the Isthmian Canal Commission are authorized to deliver said property to such officers or persons as the President may designate, and to take credit therefor at such percentage of its original cost as the President may approve, but this amount shall not be charged against the fund provided for in said sections. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

302. *Telegraph and telephone lines.*—The authority granted under section 301 of this title shall include the power to construct, maintain, and operate telegraph and telephone lines so far as they may be necessary or convenient in the construction and operation of the railroad or railroads as herein authorized and they shall perform generally all the usual duties of telegraph and telephone lines for hire. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

303. *Townsites.*—The President is authorized to withdraw, locate, and dispose of, under such rules and regulations as he may prescribe, such area or areas of the public domain along the line or lines of such proposed railroad or railroads for townsite purposes as he may from time to time designate. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

304. *Terminals, stations and rights of way.*—Terminal and station grounds and rights of way through the lands of the United States in the Territory of Alaska are granted for the construction of railroads, telegraph and telephone lines authorized by sections 301 to 303 of this title, and the President may, in such manner as he deems advisable, make reservation of such lands as are or may be useful for furnishing materials for construction and for stations, terminals, docks, and for such other purposes in connection with the construction and operation of such railroad lines as he may deem necessary and desirable. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

305. *Patents to contain reserve for right of way.*—In all patents for lands taken up, entered, or located in Alaska after March 12, 1914, there shall be expressed that there is reserved to the United States a right of way for the construction of railroads, telegraph and telephone lines to the extent of one hundred feet on either side of the center line of any such road and twenty-five feet on either side of the center line of any such telegraph or telephone lines. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

306. *Disposition of proceeds of lease or sale of public lands.*—All moneys derived from the lease, sale, or disposal of any of the public lands, including townsites, in Alaska, or the coal or mineral therein contained, or the timber thereon, and the earnings of said railroad or railroads, together with the earnings of the telegraph and telephone lines constructed under authority of sections 301 to 303 of this title, above maintenance charges and operating expenses, shall be paid into the Treasury of the United States as other miscellaneous receipts are paid, and a separate account thereof shall be kept and annually reported to Congress. (Mar. 12, 1914, c. 37, § 3, 38 Stat. 307.)

307. *Authority of President.*—It is the intent and purpose of Congress through the provisions of sections 301 to 303 of this title to authorize and empower the President of the United States, and he is fully authorized and empowered, through such officers, agents, or agencies as he may appoint or employ, to do all necessary acts and things in addition to those specially authorized in such sections to enable him to accomplish the purposes and objects of such sections. (Mar. 12, 1914, c. 37, § 1, 38 Stat. 305.)

308. *Officers, agents, etc., to make annual report to President; transmission to Congress.*—The officers, agents, or agencies placed in charge of the work by the President shall make to the President annually, and at such other periods as may be required by the President or by either House of Congress, full and complete reports of all their acts and doings and of

all moneys received and expended in the construction of said work and in the operation of said work or works and in the performance of their duties in connection therewith. The annual reports provided for in this section shall be by the President transmitted to Congress. (Mar. 12, 1914, c. 37, § 4, 38 Stat. 307.)

ALASKA OVERVIEW: LEGISLATIVE HISTORY

The Alaska State Legislature enacted House Joint Resolution 27 in 1975, directing Governor Jay Hammond to convene an international conference to discuss possible railroad connection between Alaska and Canada. However, only through constant pressure by legislative leaders on the Governor's office did it finally occur. On April 8, 1976 (one year later), a meeting was held in municipal offices in Juneau, attended by members of state, federal and Canadian governmental agencies, and representatives of industry and rail companies from Alaska, Canada and the Western United States.

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It was learned that Alaska was far behind Canada in transportation planning, particularly for rail, and that an official commitment to perform such planning was essential. That commitment came in the form of a special legislative appropriation. To show good faith to both the Canadian and the U.S. Federal governments, resolutions were enacted that declared Alaska's support for the project. The Alaska State Legislature appropriated the sum of \$50,000, to perform a review of the project's potentials. Further, it was agreed that there was great potential in the State, and that it appeared to be a most viable project. The major hurdle would be the assurance that continued efforts would be made to pursue the idea, and that a formal commitment be made by the State of Alaska. The majority of those in attendance were clearly in favor of further work on this project.

In 1977, the Alaska State Legislature appropriated \$865 000 for the purpose of reconnaissance photography and studies, field surveys, mapping, engineering work and cost comparisons to delineate a utility corridor and railroad right-of-way for extension of the Alaska Railroad. Governor Jay Hammond line-item vetoed all but \$150,000 of the money appropriated. The Department of Transportation was only able to perform minimal route reconnaissance in 1977.

At the opening of the next legislative session in January 1978, the members restored the full dollar amount of the original appropriation by overriding the veto. By this time, however, the most important factor controlling success of this project was time, since a great amount of work needed to be completed before June 30, 1979, at which time the funding was scheduled to expire.

In 1978, the Governor again line-item vetoed \$265,000 out of this same appropriation, and the Alaska State Legislature immediately appropriated these same dollars to the Legislative Council, in order to complete the work as planned. Thus, the authority of the Governor to control these dollars was taken away. The assurance that the necessary work would be completed was accomplished.

In 1979, the Governor once more attempted to line-item veto the \$265,000 from the budget, but this time was forced to replace the ~~money~~ because contracts were already committed on these dollars, and substantial legal liabilities would have been incurred by himself and his office. The Alaska State House and Senate issued a joint statement in 1979 giving full support to the rail extension project.

CHAP. 34.—An Act To repeal an Act regulating the construction of bridges across the Muskingum River in Ohio.

March 9, 1914.
[H. R. 11571.]

[Public, No. 65.]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Act of Congress entitled "An Act regulating the construction of bridges over the Muskingum River in Ohio," approved April second, eighteen hundred and eighty-eight, be, and the same is hereby, repealed.

Muskingum River, Ohio.
Restrictions on bridges across, removed.
Vol. 25, p. 74, repealed.

Approved, March 9, 1914.

CHAP. 35.—An Act To authorize the construction, maintenance, and operation of a bridge across the Tombigbee River near Old Cotton Gin Port, in Monroe County, Mississippi.

March 9, 1914.
[H. R. 11565.]

[Public, No. 67.]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the board of supervisors of Monroe County, Mississippi, is hereby authorized to construct, maintain, and operate a bridge and approaches thereto across the Tombigbee River, at a point suitable to the interests of navigation, near Old Cotton Gin Port, in Monroe County, Mississippi, in accordance with the provisions of an Act entitled "An Act to regulate the construction of bridges over navigable waters," approved March twenty-third, nineteen hundred and six.

Tombigbee River, Monroe County, Miss., may bridge, at Old Cotton Gin Port.
Construction.
Vol. 34, p. 64.

SEC. 2. That the right to alter, amend, or repeal this Act is hereby expressly reserved.

Amendment.

Approved, March 9, 1914.

CHAP. 36.—An Act To extend the time for constructing a bridge across the Mississippi River at the town site of Sartell, Minnesota.

March 11, 1914.
[H. R. 11545.]

[Public, No. 68.]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the time for commencing and completing the bridge authorized by the Act of Congress approved August twenty-fourth, nineteen hundred and twelve, to be built across the Mississippi River, at the town site of Sartell, Stearns County, Minnesota, is hereby extended to one year and three years, respectively, from date of approval hereof.

Mississippi River.
Time extended for bridging, by Sartell, Minn.
Vol. 37, p. 194, amended.

SEC. 2. That the right to alter, amend, or repeal this Act is hereby expressly reserved.

Amendment.

Approved, March 11, 1914.

CHAP. 37.—An Act To authorize the President of the United States to locate, construct, and operate railroads in the Territory of Alaska, and for other purposes.

March 12, 1914.
[S. 45.]

[Public, No. 69.]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the President of the United States is hereby empowered, authorized, and directed to adopt and use a name by which to designate the railroad or railroads and properties to be located, owned, acquired, or operated under the authority of this Act; to employ such officers, agents, or agencies, in his discretion, as may be necessary to enable him to carry out the purposes of this Act; to authorize and require such officers, agents, or agencies to perform any or all of the duties imposed upon him by the terms of this Act; to detail and require any officer or officers in the Engineer Corps in the Army or Navy to perform service under this Act; to fix the compensation of all officers, agents, or employees appointed or designated by him; to designate and cause to be located a route or routes for a line or lines of railroad in the Territory of Alaska not to exceed in the aggregate one thousand

Alaska.
President authorized to operate, etc., railroads in.

Location and purpose.

miles, to be so located as to connect one or more of the open Pacific Ocean harbors on the southern coast of Alaska with the navigable waters in the interior of Alaska, and with a coal field or fields so as best to aid in the development of the agricultural and mineral or other resources of Alaska, and the settlement of the public lands therein, and so as to provide transportation of coal for the Army and Navy, transportation of troops, arms, munitions of war, the mails, and for other governmental and public uses, and for the transportation of passengers and property; to construct and build a railroad or railroads along such route or routes as he may so designate and locate, with the necessary branch lines, feeders, sidings, switches, and spurs; to purchase or otherwise acquire all real and personal property necessary to carry out the purposes of this Act; to exercise the power of eminent domain in acquiring property for such use, which use is hereby declared to be a public use, by condemnation in the courts of Alaska in accordance with the laws now or hereafter in force there; to acquire rights of way, terminal grounds, and all other rights; to purchase or otherwise acquire all necessary equipment for the construction and operation of such railroad or railroads; to build or otherwise acquire docks, wharves, terminal facilities, and all structures needed for the equipment and operation of such railroad or railroads; to fix, change, or modify rates for the transportation of passengers and property, which rates shall be equal and uniform, but no free transportation or passes shall be permitted except that the provisions of the interstate commerce laws relating to the transportation of employees and their families shall be in force as to the lines constructed under this Act; to receive compensation for the transportation of passengers and property, and to perform generally all the usual duties of a common carrier by railroad; to make and establish rules and regulations for the control and operation of said railroad or railroads; in his discretion, to lease the said railroad or railroads, or any portion thereof, including telegraph and telephone lines, after completion under such terms as he may deem proper, but no lease shall be for a longer period than twenty years, or in the event of failure to lease, to operate the same until the further action of Congress: *Provided*, That if said railroad or railroads including telegraph and telephone lines, are leased under the authority herein given, then and in that event they shall be operated under the jurisdiction and control of the provisions of the interstate commerce laws; to purchase, condemn, or otherwise acquire upon such terms as he may deem proper any other line or lines of railroad in Alaska which may be necessary to complete the construction of the line or lines of railroad designated or located by him: *Provided*, That the price to be paid in case of purchase shall in no case exceed the actual physical value of the railroad; to make contracts or agreements with any railroad or steamship company or vessel owner for joint transportation of passengers or property over the road or roads herein provided for, and such railroad or steamship line or by such vessel, and to make such other contracts as may be necessary to carry out any of the purposes of this Act; to utilize in carrying on the work herein provided for any and all machinery, equipment, instruments, material, and other property of any sort whatsoever used or acquired in connection with the construction of the Panama Canal, so far and as rapidly as the same is no longer needed at Panama, and the Isthmian Canal Commission is hereby authorized to deliver said property to such officers or persons as the President may designate, and to take credit therefor at such percentage of its original cost as the President may approve, but this amount shall not be charged against the fund provided for in this Act. X

Construction, etc.

Rights of way, terminals, etc.

Transportation rates, etc.

Common carrier duties.

Lease after completion.

Provision. Subject to interstate commerce laws if leased.

Purchase of existing lines.

Price. Joint agreements with other carriers.

Use of Panama Canal machinery, etc., for construction.

A PRELIMINARY STUDY

ALASKA-CANADA TRANSCONTINENTAL RAIL CONNECTION TO CONTIGUOUS UNITED STATES

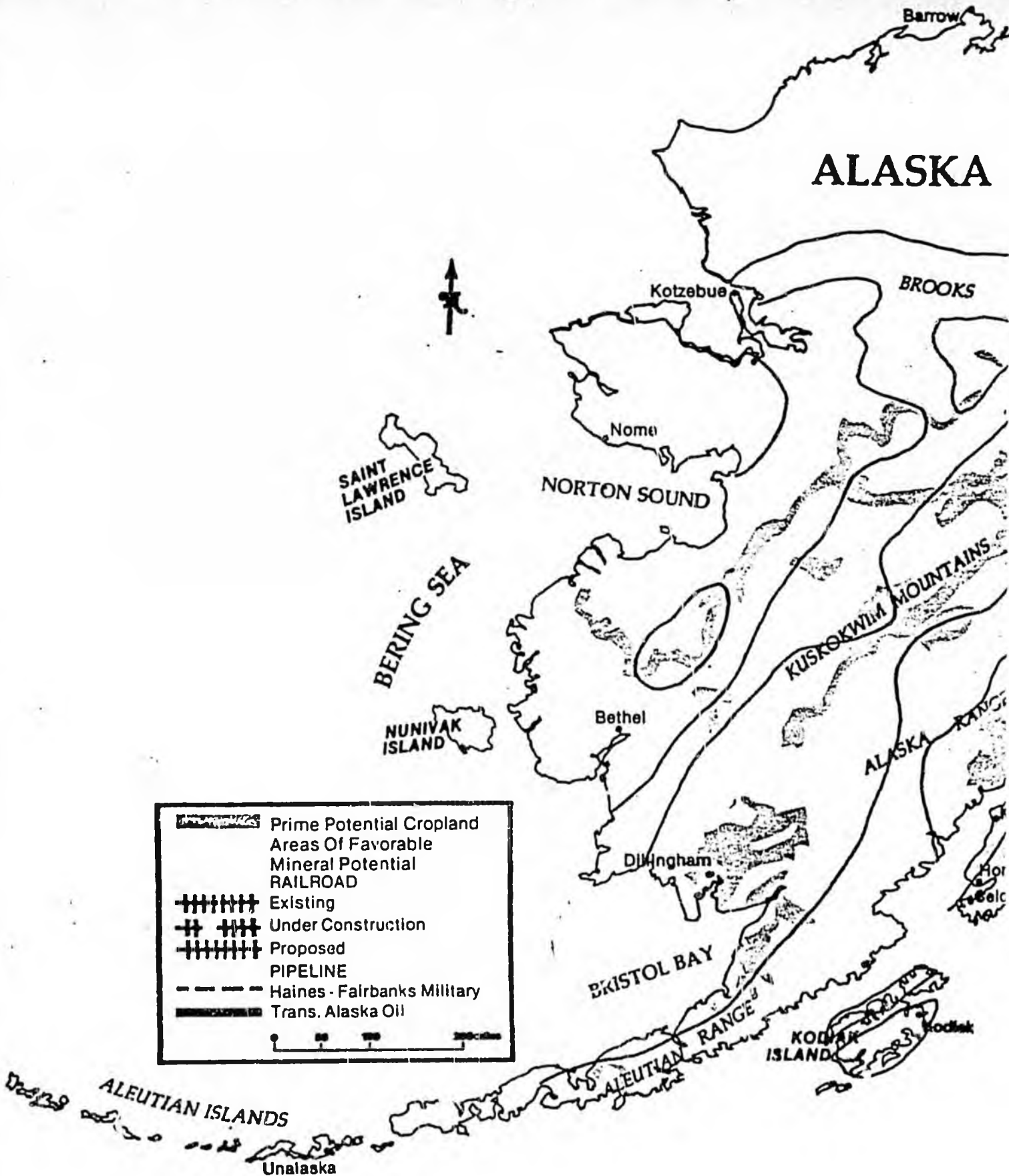


STATE OF ALASKA
DEPARTMENT OF
COMMERCE
&
ECONOMIC DEVELOPMENT

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ALASKA



	Prime Potential Cropland
	Areas Of Favorable Mineral Potential
RAILROAD	
	Existing
	Under Construction
	Proposed
PIPELINE	
	Haines - Fairbanks Military
	Trans. Alaska Oil



Barrow

BEAUFORT SEA

ALASKA

BROOKS RANGE

CANADA
UNITED STATES
YUKON
ALASKA

CANADA

MOUNTAINS

Fairbanks

Big Delta

Dawson

ALASKA RANGE

Glennallen

Ross River

Palmer

Valdez

Carmacks

Cordova

Whitehorse

Homer

Gerdard

Watson Lake

GULF OF ALASKA

Yakutat

Skagway

Paines

COAST MOUNTAINS

Dease Lake

Leavenworth

Petersburg

Wrangell

Prince Rupert

I. THE ROUTE

The British Columbia Railroad is scheduled to complete a 400 mile northern extension of their track in 1978, from near Prince George to Dease Lake - about 120 air miles east-northeast of Juneau and 100 miles southwest of Watson Lake located on the Yukon border. A potential route to Alaska through the Yukon would be first, an extension from Dease Lake to Watson Lake, then following first the Laird and then the Pelly Rivers to a point below Ross River where it turns East on the Magundy and Little Salmon River drainages to the community of Carmacks on the Yukon, then down the Yukon and a short distance up the White River until it reaches the West Fork of the Ladue River from which it crosses the Alaska border east of Tetlin Junction. It is assumed that the railroad will generally parallel the Alaska Highway from Tetlin into Fairbanks. This route is considered to be "relatively easy" terrain for rail construction, down river valleys and with no major mountain passes to be crossed. This route describes 297 miles of track in Alaska, 568 miles in the Yukon, and about 100 miles remaining to be constructed in B.C. after the Dease Lake extension is completed. If current proposals before the White Pass and Yukon and Alaska Railroads are brought to completion some 250 miles along the route would be placed under construction. The Alaska and part of the Yukon sections were first identified by the Army Corps of Engineers during the construction of the Alaska Highway. The Bureau of Land Management, in their November 1974 report entitled "Multimodal Transportation and Utility Corridor System in Alaska," describes the rail route as Option #27. The land area for the entire route in Alaska may be selected through the eminent domain authority of the Alaska Railroad.

II. THE TYPE OF RAILROAD

The following cost estimates are for a general purpose standard gauge railroad with a good bed structure. The type of track bed should be of such a quality as to be readily upgradeable to unit train capability (unit trains are point-to-point, single bulk commodity, uniform car load trains that are usually not altered between origin and destination. Unit trains haul heavy tonnage and are particularly hard on track and equipment). Currently however, it is the State's policy to promote the processing of raw ores and crude oil within Alaska's boundaries. Most immediate demand for unit trains in Alaska will probably be placed for coal shipments along the existing track of the Alaska Railroad.

III. THE COST

Any estimate of costs at this point are ballpark figures. Cost also has several facets. One is dollar construction costs which, as of this date, are estimated to average \$1.2 million per mile by the railroads closest to the project. Total cost relates also to numbers of miles remaining to be constructed at the time the decision is made to make the through connection.

Officials of the White Pass and Alaska Railroads have agreed that the incremental increase in maintenance and operational structure supporting their railroads now, would be relatively less for the new mileage than for a less isolated railroad in the "lower 48" operating more miles of track and having contract shop facilities available to it nearby.

Another facet is that some costs such as social, environmental, etc., cannot be measured by dollars. They need to be evaluated, weighed, and placed in their proper perspective. It is clear that costs relate to time, and the longer construction is delayed, the higher the cost.

Who will pay? New rail construction clearly generates its costs at the front end. The larger the number of groups sharing the costs, the lower the cost will be to each.

One who asserts the expense will be too high by the time the railroad is built should remember revenue and demand also rises. In short, all the people who will benefit from the railroad, will in some way pay for the railroad.

IV. THE ECONOMIC, SOCIAL, AND POLITICAL CONSIDERATIONS

This area is beyond the scope of this study. However, it is reasonable to assume that the benefits in the form of new jobs and businesses, lower costs for consumer and durable goods, increased revenue for government et al, might far exceed the cost for a through rail connection. The governments and people of Alaska, Canada and the Northern states of the "lower 48" would be receiving most of these benefits. Only a well funded, comprehensive study of the total impact resulting from a rail connection could measure the total effect, and therefore, the viability of the proposal and the route.

V. ENVIRONMENTAL CONSIDERATIONS

The measurement of this impact is not within the funding of this study, but most certainly should be weighed with the other factors in a cost-benefit analysis. Initial reaction is described in the "Other Opinions" section later in this report.

VI. THE REVENUE

Those benefiting from the Railroad include the public, the operator of the railroad, the users of the railroad, and the local, state, provincial and federal governments. When the first tons of cargo move across a portion of the new track the operator will draw some salary and costs out of the rates charged to the shipper for hauling. A substantial volume will have to move, however, before what is collected in rates will pay for the original construction costs of the railroad-though this may happen (see the section on "Full Potential").

VII. THE RATE

In order for a transcontinental railroad to be effective, it must be competitive with existing modes of transportation. Competitiveness for the railroad also suggests the ability to provide tighter schedules and less handling of goods. A shipment could be placed on a rail car in the Midwest and not touched again until it reaches Fairbanks or Anchorage. Additional benefits include less chance for damage, delay, misrouting, and fewer transshipments.

Someone else has been receiving revenue before that first ton of cargo moved, however, perhaps millions of dollars. This revenue is in the form of income, property and business taxes paid to all levels of government during construction. This revenue will decline as the railroad nears completion unless the operator can put the railroad into operation. When operation begins, three revenues or benefits will flow - the revenue termed "public good and convenience," the rate revenue - particularly when it is reinvested, and the governmental tax revenue on all the primary and secondary economic activities.

The total of 1) public good, 2) charges and 3) taxes, versus the original construction and operational costs is what needs to be measured when asking whether the railroad will pay for itself and should be the subject of future study. It is clear the governments will initially have to participate in the construction because the railroad operator himself has not as yet had access to any revenue.

When a potential shipper is asked how much he might ship on a through rail route to the Midwest, his logical reply is: "How much will you charge me?" The answer is, there is presently no way of telling. This department has prevailed upon the railroads to construct a purely hypothetical rate under which they might be able to operate at today's costs. The Alaska Railroad prepared the first draft and the British Columbia and White Pass and Yukon Railroads are still in the process of evaluating this rate structure. It is understood that railroads only in very special circumstances could compete with an all water shipment. However, the question is could the railroads compete today once transshipments to interior points in Alaska and the mid-continent regions are required. When one approaches total tonnages in the modest range of three to four million tons a year, the hypothetical rates answer this question in the affirmative. This is however, only one measure of revenue generated by a railroad (see section on "Revenue"). Cost recovery in this tonnage range can be significant however as seen in the accompanying table.

The Alaska Railroad's estimates do not include profit margins, however, the profit increment is estimated to be 15 percent or less (profitability can also be achieved through operating procedures).

It is common practice that these rates vary among commodities, and that the estimated rate represents an average rate. Understandably these rates are negotiable to individual shippers based on volume and distance. Since a rate structure is already in effect to Prince George, negotiations would produce transcontinental through rates and other through rates to Northern Canada and Alaska destinations, which are usually lower.

Estimated Rate Structure - Prince George to Fairbanks
Capital and Operating Recovery

<u>Tonnage</u>	<u>Canadian Segment</u>	<u>Alaska Segment</u>	<u>Rate/ton</u>	<u>Rate/cwt</u>
1,000,000	\$112.26	\$61.36	\$173.62	\$8.68
2,000,000	64.91	38.62	103.53	5.18
3,000,000	49.93	31.25	81.08	4.05
4,000,000	42.95	27.77	70.72	3.54
5,000,000	39.53	25.89	65.42	3.27
6,000,000	38.00	24.86	62.86	3.14

Operating Expense Recovery Only

<u>Tonnage</u>	<u>Canadian Segment</u>	<u>Alaska Segment</u>	<u>Rate/ton</u>	<u>Rate/cwt</u>
1,000,000	\$37.33	\$23.18	\$60.51	\$3.03
2,000,000	27.45	19.53	46.98	2.35
3,000,000	24.85	18.53	43.38	2.17
4,000,000	24.22	18.23	42.45	2.12
5,000,000	24.54	18.25	42.79	2.14
6,000,000	25.51	18.50	44.01	2.20

VIII. THE VOLUME

There are two types of volume that are of interest in this study; current and future volume. The most readily accessible current volume statistics were those compiled by the Alaska Railroad. Future volume had to be identified through research and contacts with various potential shippers.

In estimating future volume, it was necessary to make three basic assumptions:

1. That traffic originating from inland points east of the Rocky Mountains would probably move along an all land rail route to Alaska, given competitive service.
2. That the present Alaska traffic, excluding pipeline traffic will continue to grow on the average of 7 percent a year.
3. That 1985 would be the earliest normal completion date for the construction of a through rail route between Alaska and the Midwest.

Only a general idea of what commodities are moving and the point of origin and destination appeared necessary for purposes of this study. The large Alaska highway tonnage carried is mostly pipeline oriented to date and it is assumed that most of the commodities carried by air will continue to move in that manner. Consequently, waterborne tonnage into Alaska was the only tonnage gathered in detail for this report.

CURRENT VOLUME

1975 Tonnage

Data gathered from the Alaska Railroad, reveals that 24 percent of their freight originated east of the Rocky Mountains in 1975. That is probably conservative since billing figures were used and Seattle offices are often billed for freight destined for Alaska, regardless of origin.

The Alaska Railroad handled 9,516 car loads of interline traffic in 1975 of which 2,284 car loads or 91,360 tons could be identified by billings as originating east of the Rocky Mountains.

An additional 51,600 tons arrived at Seward by water. Applying the 24 percent factor developed from the Railroad statistics, an estimated 12,384 tons of cargo received at Seward had origins east of the Rockies. The Port of Anchorage received 2,222,169 tons in 1975. Of this total 1,368,192 tons were petroleum products. Of the remaining 853,977 tons, mostly from Sea-Land, it might be assumed that 24 percent, or an estimated 204,954 tons, originated east of the Rockies. Combining the tonnage volume from the Railroad, Seward, and Anchorage, approximately 308,698 tons had origins east of the Rockies. This volume, projected at a 7 percent annual increase, reaches 607,255 tons in 1985, for a good base tonnage.

1976 Tonnage

These figures are incomplete and are displayed as a matter of interest.

The general cargo continues a modest increase over 1975. Column A is interline freight received and Column B is freight tendered to the Railroad by Sea-Land and TOTE for movement to Fairbanks.

Alaska Railroad

Tons of Freight	A	B	Total
FY 1976	395,670	110,609	506,279
July - November 1976	122,705	51,586	174,291

The Port of Anchorage in 1976 processed the tonnages displayed in the following table. The total general cargo handled was 1,072,149 tons. Some of this cargo is transshipped by the Alaska Railroad to Fairbanks and is included in the Railroad's statistics.

Port of Anchorage
Waterborne Commerce by Commodity, 1976
(in tons)

Commodity	Local		Domestic		Foreign	
	Inbound	Outbound	Inbound	Outbound	Inbound	Outbound
Freight, N.O.S.	2.0	7.0	4,927.3	11.6	1,199.2	
Cement, Drilling Mud, etc.			40,329.1		31.4	
Iron or Steel Articles		52.0	120.1		7,248.7	
Lumber			266.4			
Plastic Material Insulation			1,273.0			
Petroleum, Bulk			1,300,521.6	7,623.7	386,854.2	
Petroleum, N.O.S.		1,395.0				
Scrap, Iron or Steel						
Vans, Flats, Containers			884,211.5	94,398.7		
Vehicles			22,779.7	11,192.9	2,703.9	
Totals	2.0	1,454.0	2,254,428.7	113,226.9	398,037.4	

The White Pass and Yukon Railroad is projecting 100,000 tons outbound from the Yukon Territory ultimately destined to interior Canadian points in 1981. Yukon tonnage is chiefly mineral concentrates and may or may not grow at 7 percent annually to 1985. However, these figures are biased downward since tonnages in the opposite direction have not been considered. Therefore, it would seem very conservative to estimate that a million tons would flow across the route by 1985, given competitive service and no new development.

A million tons means about a train a day to the Alaska Railroad. If you exclude fuel related tonnages, like petroleum and coal, the Alaska Railroad presently hauls less than one million tons of general cargo a year. This is also true of the White Pass and Yukon Railroad. The new route would probably increase the tonnage of both railroads and it certainly would offer a good base for the through route.

FUTURE VOLUME

In attempting to identify the future volume of such a rail route, potential shippers were contacted (see the following letter). The letter was sent to 131 firms in the United and Canada. To date, a 39 percent response has been received, which is a good response. This is not to be considered a poll. It is simply an admittedly incomplete sampling of opinions. The reader can gather the tenor of the comments from these potential customers of a rail route. The letter did not ask for nor guarantee confidentiality, however, it was decided to publish the excerpts separate from the authors in order that any presumed confidences would not be violated. Those eight individuals identified with their statements have been done so with their permission.

These letters suggest the railroad itself may trigger the development of some of the mines mentioned. Certainly the respondents seem to overwhelmingly agree that a through railroad would be a plus factor for the economy and a boon to mineral development. It is interesting to note that some companies have stated that they have not even bothered to explore in areas lacking transportation. Of additional importance is the fact that most of the respondents hold high executive positions within their company structure. Read each comment entirely to judge for yourself the support for this route. Some significant potential is suggested.