

Navigating CSHB 488 (RES) (With the Differences from HB 488 Highlighted)

Before the House Finance
Committee

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Robert E. Mintz, Department of Law
Dan E. Dickinson, C.P.A.

HB 488, Section 35 CSHB 488, Section 38

New production tax provisions apply to oil
and gas produced on or after:

July 1, 2006 (HB 488)

April 1, 2006 (CSHB 488)

HB 488, Section 5

AS 43.55.011(a)

There is levied upon the producer . . . a tax for all **oil and gas** produced **each month** . . . The tax is equal to **20 percent** of the **net value** . . . under AS 43.55.160.

CSHB 488, Section 5

AS 43.55.011(a)

There is levied upon the producer . . . a tax for all **oil and gas** produced **each month** . . . [except for] a lessor's royalty interest. . . .

The tax is equal to **20 percent** of the **production tax value** . . . under AS 43.55.160.

CSHB 488, Section 6

AS 43.55.011(e)

There is levied upon the producer . . . a tax for all oil and gas produced each month . . . the ownership or right to which constitutes a lessor's royalty interest The tax is equal to five percent of the gross value at the point of production

CSHB 488, Section 6

AS 43.55.011(f) – (k)

[Above specified price thresholds] There is levied upon the producer

... a tax for all oil ... equal to **.30 percent of the gross value** at the point of production ... multiplied by the **oil price index**

... a tax for all gas ... equal to **two percent of the gross value** at the point of production ... multiplied by the **gas price index**

So . . .

The **original bill** has a **single** production tax: 20 % of net value.

The **CS** has **four** production tax components:

- (1) 20% of net value (now called “production tax value”) *except* for lessor royalty share
- (2) 5% of gross value for lessor royalty share
- (3) A progressive-rate oil tax on gross value, including lessor royalty share
- (4) A progressive-rate gas tax on gross value, including lessor royalty share

HB 488, Section 21

AS 43.55.160(a)

net value . . . is the total of the **gross value at the point of production** of . . . oil and gas . . . from **all leases or properties** in the state, less . . . **lease expenditures** . . . as **adjusted** . . . and . . . 1/72 of . . . **transitional investment expenditures**.

CSHB 488, Section 28

AS 43.55.160(a)

production tax value . . . is the total of the **gross value at the point of production** of . . . oil and gas . . . from **all leases or properties** in the state,
less [**progressivity taxes on gross value**] . . . and . . . less . . . **lease expenditures** . . . as **adjusted**

HB 488, Section 31 CSHB 488, Section 34

AS 43.55.900(7)

“gross value at the point of production”
means

for **oil**, the value . . . at the . . . meter . . . in .
. . . **pipeline quality**

for **gas** . . . the value . . . where . . . metered
[**after any separation or gas processing**]

HB 488, Section 19 CSHB 488, Section 26

AS 43.55.150(a)

... gross value at the point of production is calculated using the reasonable **costs of transportation** ...

HB 488, Section 20 CSHB 488, Section 28

AS 43.55.150(d)

... the department **may allow** ... gross value
[to be calculated based upon] ... a **royalty
settlement agreement** ... [or]
a formula ... that uses ... [**DNR or U.S.
Dep't of Interior**] royalty ... valuation [or]
another **formula** ... **that reasonably
estimates** a value

HB 488, Section 21

AS 43.55.160(c)

... lease expenditures ... are the **total** costs **upstream** of the point of production ... on or after **July 1, 2006** ... that are the **direct, ordinary, and necessary** costs of **exploring for, developing, or producing** oil or gas deposits located ... in the state.

CSHB 488, Section 28

AS 43.55.160(c)

... lease expenditures ... are the **total** costs **upstream** of the point of production ... on or after **January 1, 2006** ... that are the **direct, ordinary, and necessary** costs of **exploring for, developing, or producing** oil or gas deposits located ... in the state.

Section 21/28

AS 43.55.160(c) (continued)

In determining . . . [**direct, ordinary, and necessary**] costs . . . the department shall give substantial weight . . . to typical **industry practices and standards** . . . as to [billable] costs . . . under **unit operating agreements** . . . and [**DNR net profits share lease regulations**].

CSHB 488, Section 28

AS 43.55.160(j)(2)

CS adds a definition of “**ordinary and necessary**” to make clear that **Internal Revenue Code** meaning is adopted.

CSHB 488, Section 28

AS 43.55.160(c) (continued)

lease expenditures . . . do **not** include . . .
catastrophic oil discharge . . . expenses . . .
or damages

HB 488, Section 21

CSHB 488, Section 28

AS 43.55.160(d) provides specific examples of, and exclusions from, “direct costs”

CSHB 488 has several improvements recommended by the Administration: e.g.,

- (d)(1)(A) and (d)(2)(A), clarifying treatment of capitalized expenditures
- (d)(2)(L), ensuring that conservation surcharges are not deductible

HB 488, Section 21

CSHB 488, Section 28

AS 43.55.160(e)

[Lease expenditures must be **adjusted** by **subtracting payments** the producer **receives** for (1) another's use of a production facility; (2) reimbursement, e.g. field costs paid by state, that offset lease expenditures; and (3) sale of assets acquired through lease expenditures or of non-taxable oil or gas used in lease operations.]

CSHB 488, Section 28

AS 43.55.160(a), (b)(2), and (e)

At the Administration's recommendation, the CS addresses potential timing mismatches between lease expenditures and adjustments, ensuring that the tax effect of an adjustment will be recognized even if a producer or explorer has no production, or has low lease expenditures, when an adjustment payment is received.

HB 488, Section 21

AS 43.55.160(g)

... transitional investment expenditures are ...
capital expenditures [incurred **7/2001 through 6/2006**] ... less ... [proceeds from] the **sale ... of assets** ... acquired ... as a result of [those] capital expenditures

[This provision is **not in the CS**; instead CS defines “lease expenditures” to include expenditures **back to January 1, 2006**]

HB 488, Section 21

AS 43.55.160(i)

... a producer that is **qualified** ... may reduce the net value by **deducting an allowance** ... [T]he total of the allowances ... during the calendar year does **not exceed \$73,000,000**. An unused allowance ... may **not be carried forward**

[This provision is **not in the CS**; instead CS provides for **additional credit** of up to **\$12 million per year**]

HB 488, Section 7

CSHB 488, Section 8

AS 43.55.020(a)

... the tax levied under AS 43.55.011, **net of any credits** applied under this chapter, is due

... The tax levied under **AS 43.55.011(a)** . . . **net of any credits** applied under this chapter, is due

HB 488, Section 12 CSHB 488, Section 14

AS 43.55.024(a)

... a producer ... that incurs a **qualified capital expenditure** ... may ... elect ... to take a **tax credit** in the amount of **20 percent** of that expenditure.

Section 12/14 (cont.)

AS 43.55.024(i)(1), (j)

[AS 43.55.024(h)(2) in original bill]

“qualified capital expenditure” -

- [is a **lease expenditure** for G&G exploration, intangible drilling costs, and other expenditures **capitalized** under IRC]
- [does **not** include purchase of a previously acquired or used asset]

CSHB 488, Section 14

AS 43.55.024(i)(2)

“qualified capital expenditure” does **not** include

an expenditure incurred . . . **for . . . an extended period of disuse, dismantlement, removal . . . or abandonment . . . or for the restoration of a lease, field, [etc.]**

Section 12/14 (cont.)

AS 43.55.024(b)

A producer may elect to take a **tax credit** . . . of **20 percent** of a carried-forward **annual loss** [which is the amount of a previous year's **lease expenditures** that were **not deductible** because they would have reduced the net value of the oil and gas below zero].

Section 12/14 (cont.)

AS 43.55.024(d) – (e), (g)

[AS 43.55.024(d) – (f) in original bill]

A producer entitled to a tax credit may apply to the Dep't of Revenue for a **transferable tax credit certificate**. Once issued, a certificate may be used for its face value, but a transferee may not apply a certificate to reduce its tax liability by more than **20 percent** during a calendar year.

CSHB 488, Section 14 (cont.)

AS 43.55.024(f)

[D]epartment [of Revenue] . . . shall issue a **cash refund** . . . for a [transferable tax credit] certificate* if . . .

- [producer's total refunds in calendar year do not exceed \$10 million]
- [producer invests or buys an oil and gas lease for at least the amount of the refund]
- [producer owes no delinquent taxes]

CSHB 488, Section 28

AS 43.55.170 – **Additional nontransferable credit**

Up to **\$12 million** in a calendar year may be taken as a **tax credit** for qualified capital expenditures – even if a credit is taken under AS 43.55.024 or 43.55.025 for the same expenditure

-- unused credit **may not be carried forward or transferred**

-- the provision **expires April 1, 2016**

CSHB 488, Section 28

AS 43.55.170(b) – producer's **qualification** for the additional nontransferable credit

This is an anti-splitting provision to prevent abuse of the \$12 million *per producer* credit.

It is essentially the same anti-splitting provision that is in sec. 21 of the original bill, for the \$73 million *per producer* allowance.

HB 488, Sections 22-29

CSHB 488, Sections 29-32

Original bill allowed a **credit** to be taken for conservation surcharge payments; CS does **not**.

CS **reduces** sec. 201 surcharge from \$.02 to \$.01 per barrel and **increases** sec. 300 surcharge from \$.03 to \$.04 per barrel.

CSHB 488, Sections 15-19

Extends existing exploration credits under AS 43.55.025 through 2016 and conforms sec. 025 to new production tax provisions by specifying that the credits may be taken only against tax under AS 43.55.011(a) – i.e., against the 20 percent tax on production tax value, *not* against lessor royalty tax or additional progressive taxes on gross value

HB 488, Section 7

Ninety percent of production tax, net of credits, is due **each month**.

The remainder is due **March 31** of the next calendar year.

CSHB 488, Sections 8, 13

100 percent of total production tax (total of all four components), net of credits, is due **each month**.

Payment of less than 90 percent of total tax due triggers an automatic **five percent penalty** on the deficiency.

HB 488, Section 9

CSHB 488, Section 10

[P]roducer may deduct [from royalty] the amount of the tax paid on taxable royalty oil and gas . . .

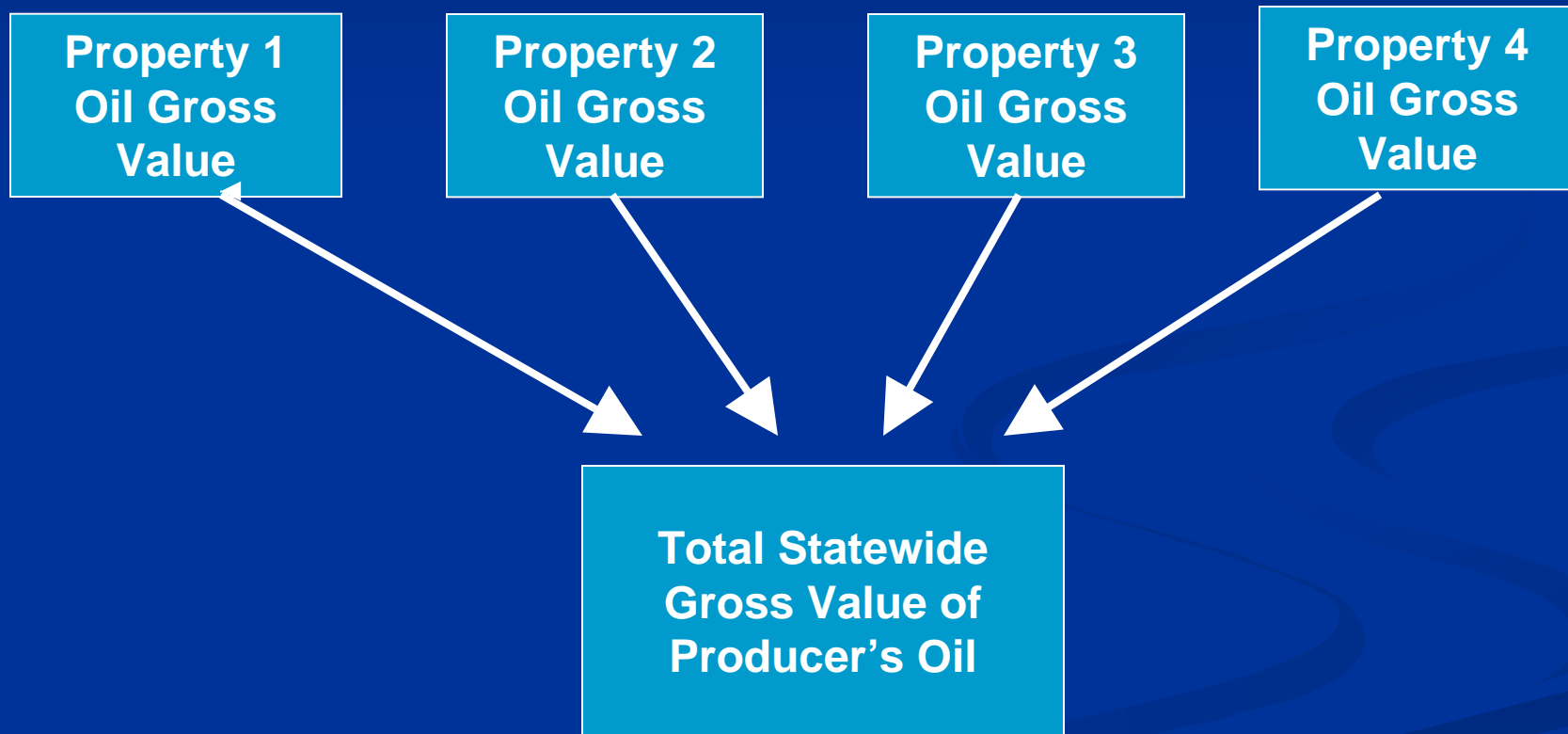
- Original bill provides a default formula for allocating the 20% tax on net value to royalty share.
- CS provides a slightly different formula for allocating the 20% tax on net value (“production tax value”) to *non-lessor* royalty share.

STEPS IN TAX CALCULATION

Under CSHB 488 (RES)

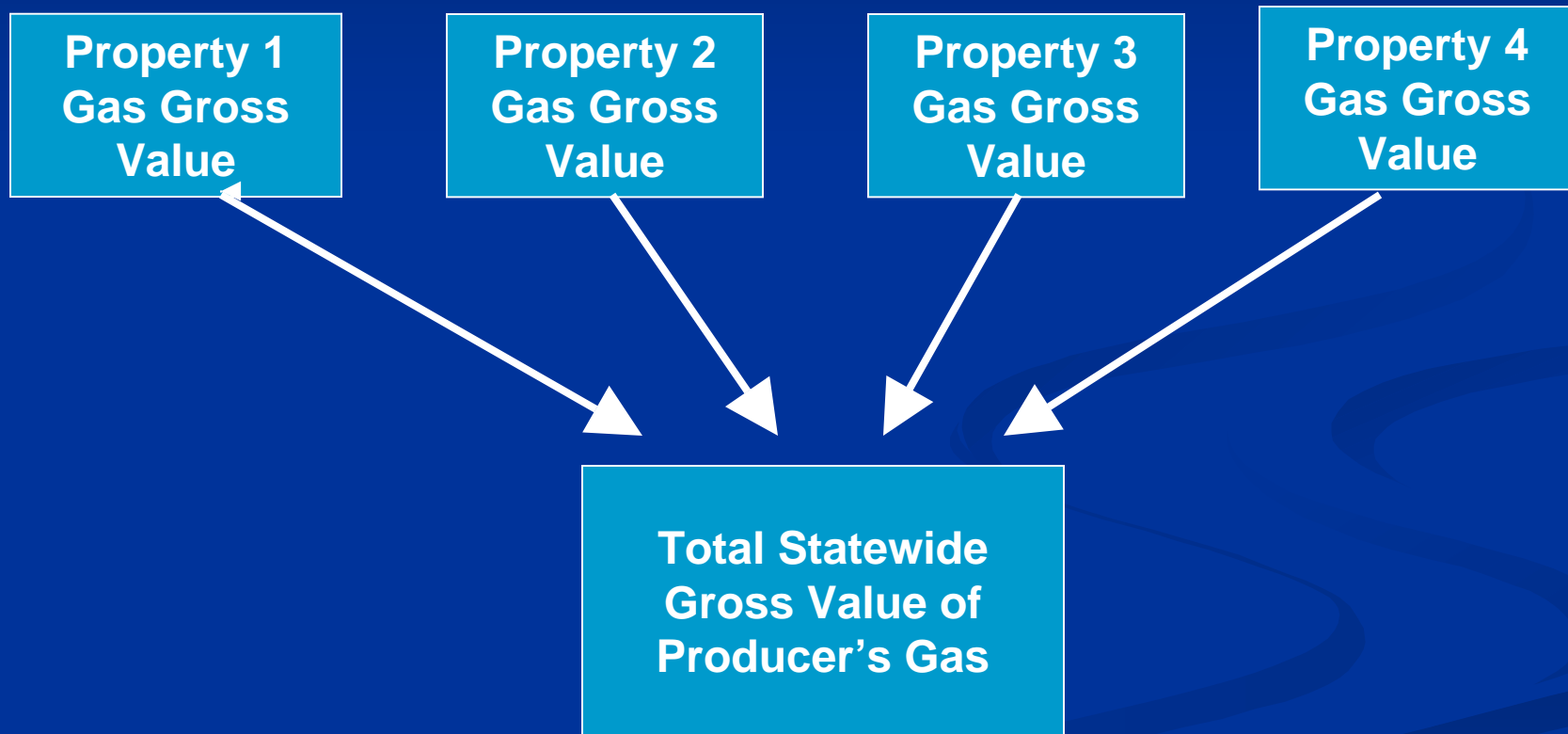
GROSS VALUE OF OIL

AS 43.55.150, AS 43.55.900



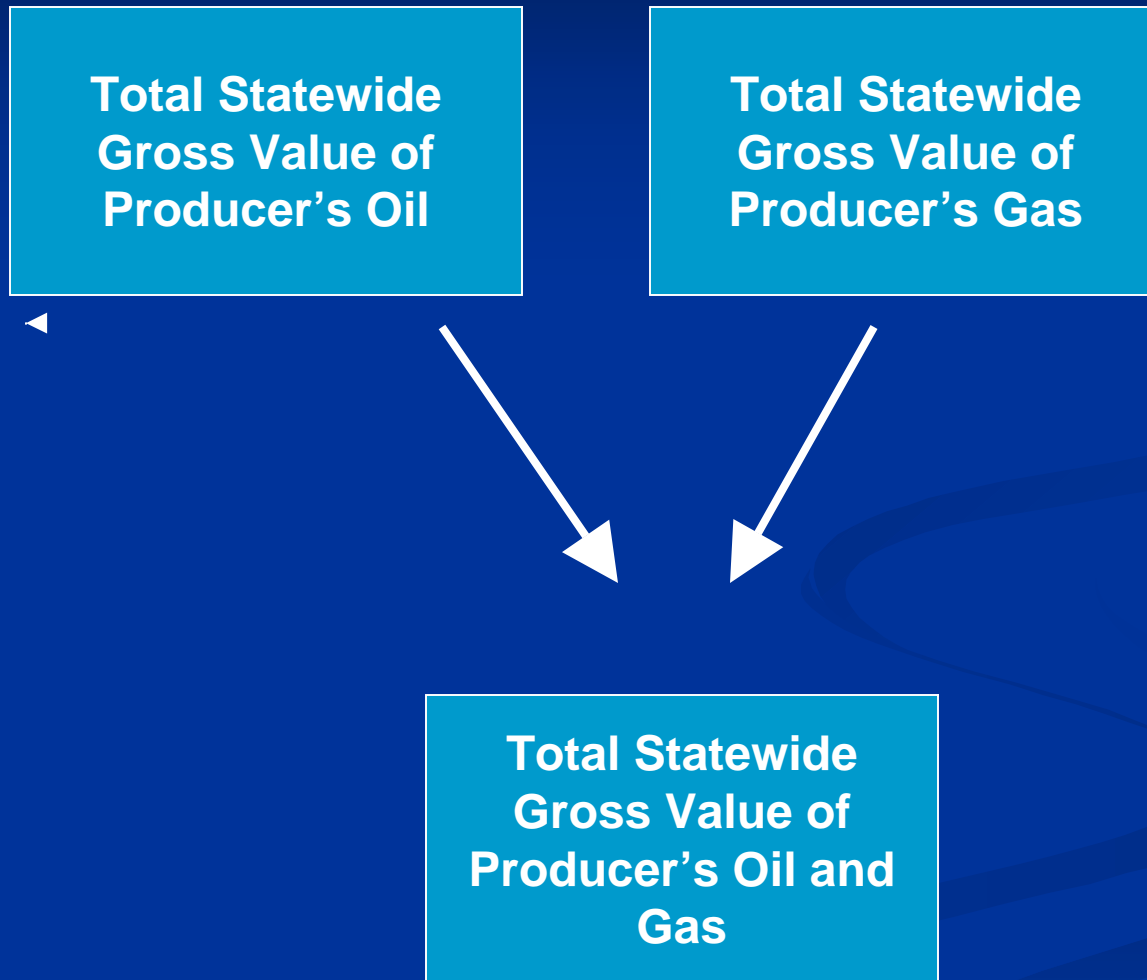
GROSS VALUE OF GAS

AS 43.55.150, AS 43.55.900



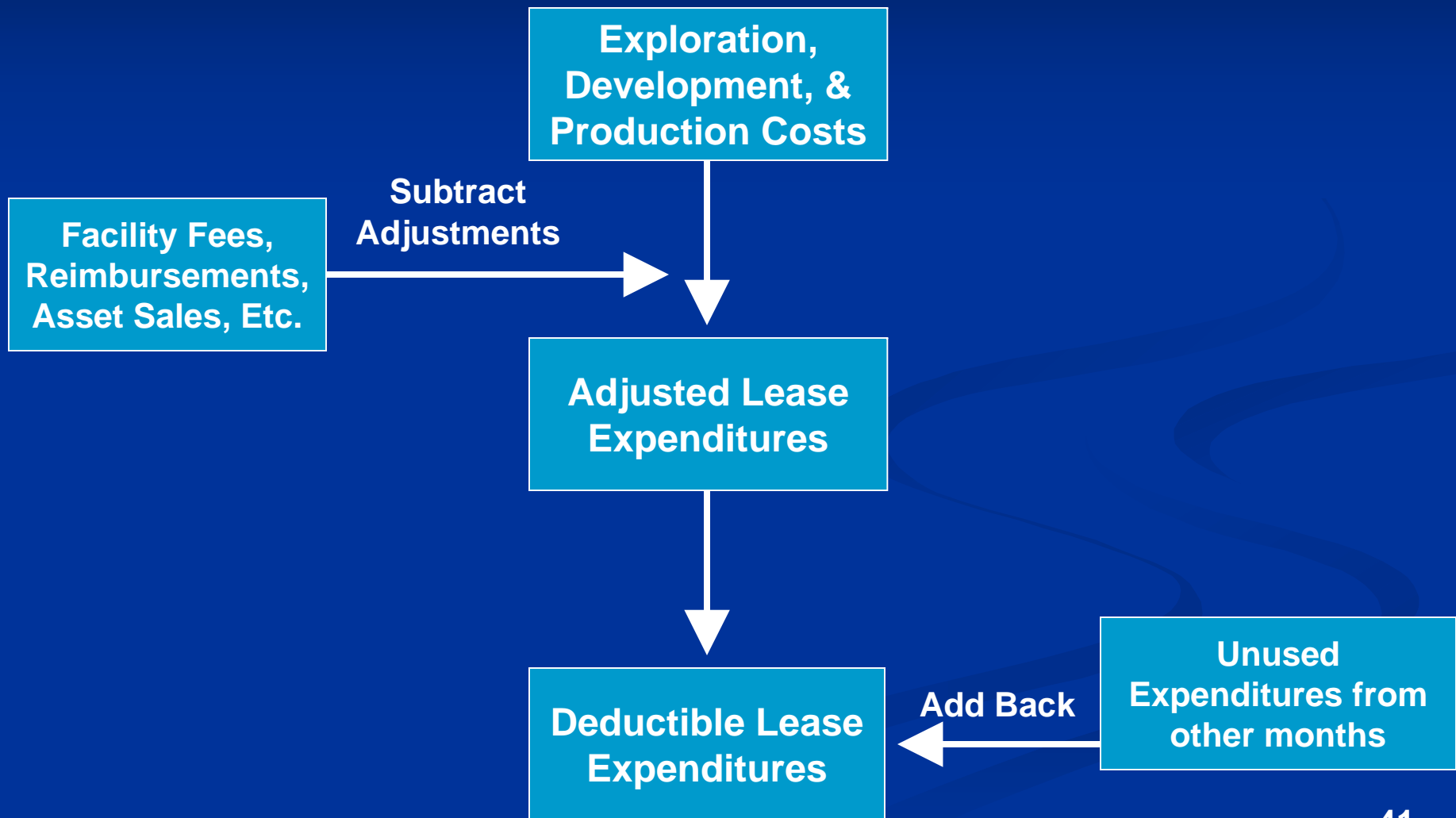
GROSS VALUE OF OIL AND GAS

AS 43.55.150, AS 43.55.900



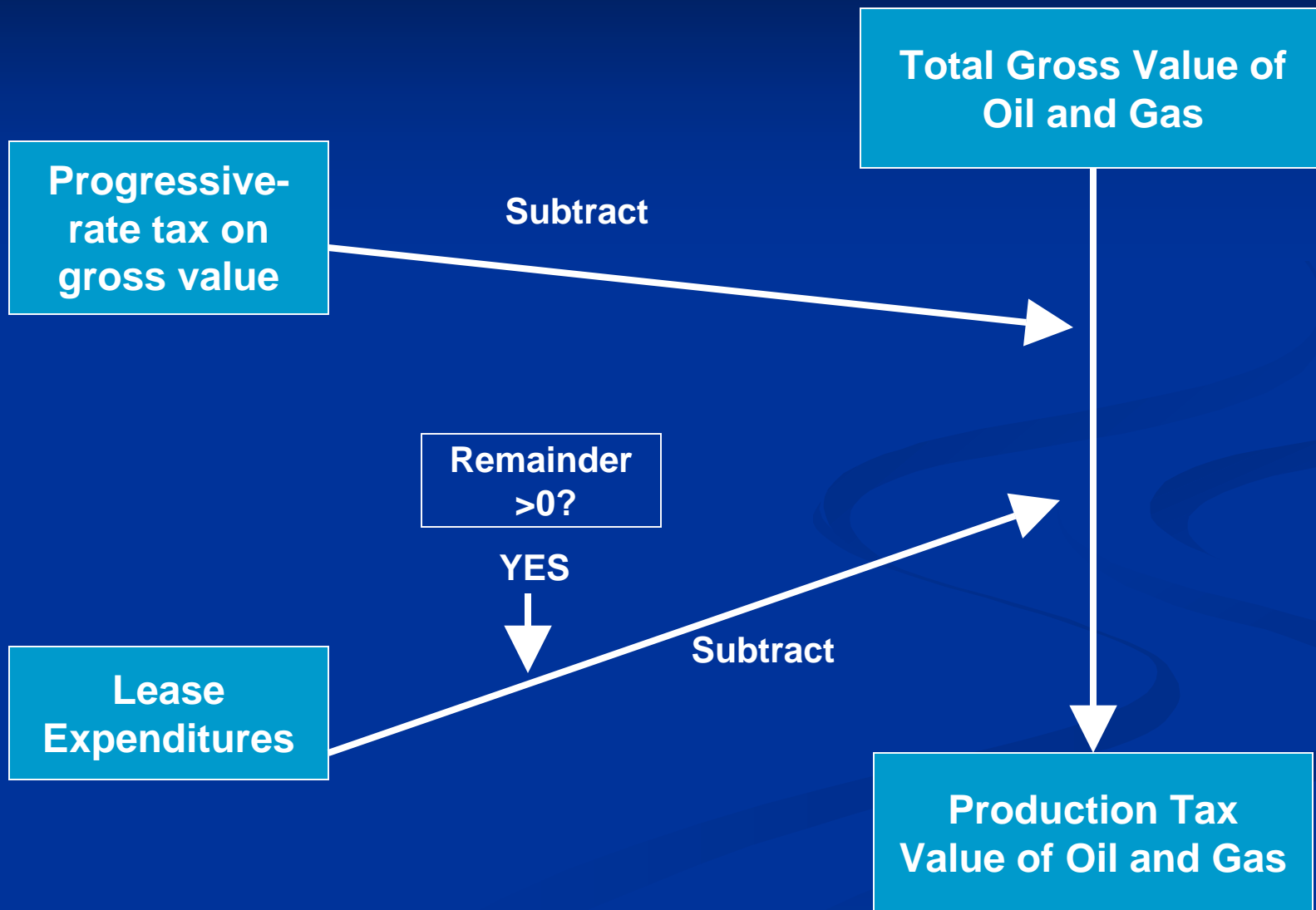
LEASE EXPENDITURES

AS 43.55.160(b) – (f)



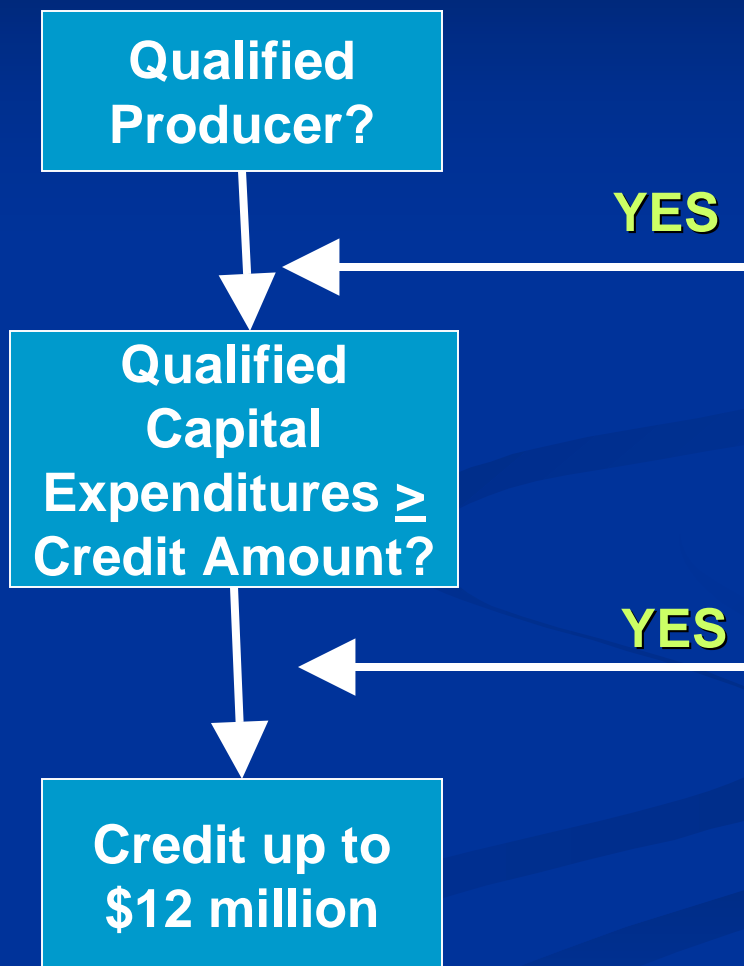
PRODUCTION TAX VALUE

AS 43.55.160 (a)



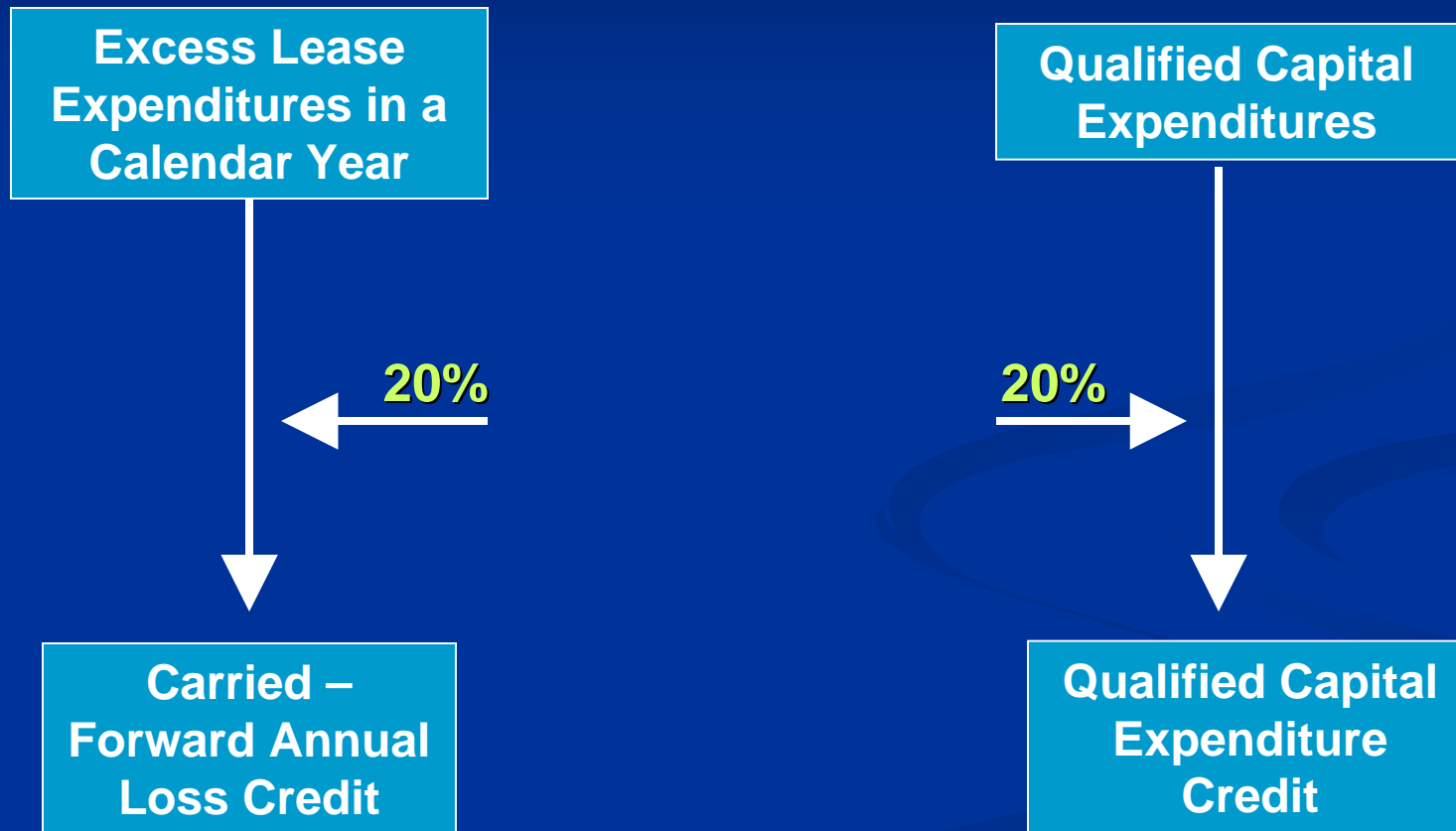
NONTRANSFERABLE CREDIT

43.55.170

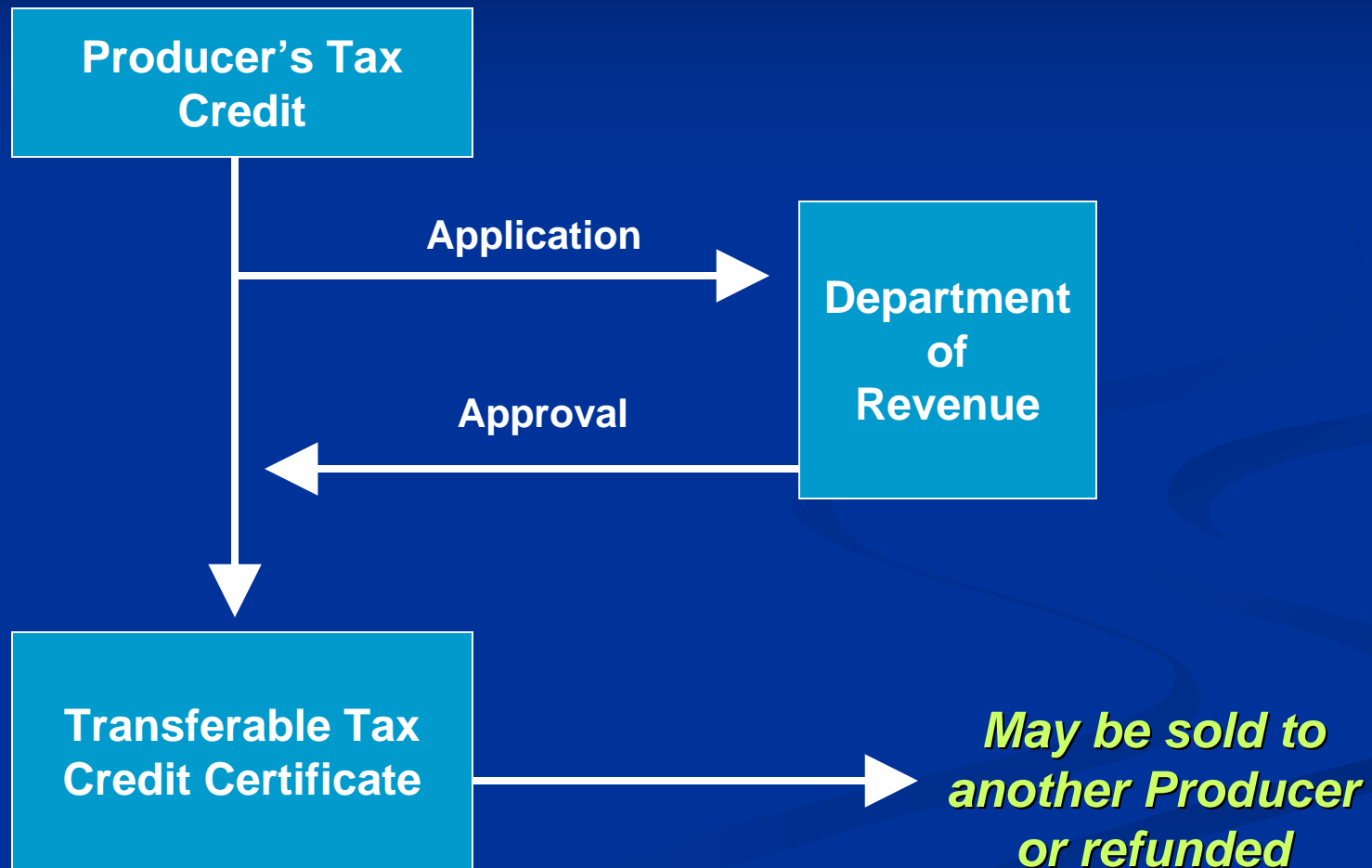


SEC. 024 TAX CREDITS

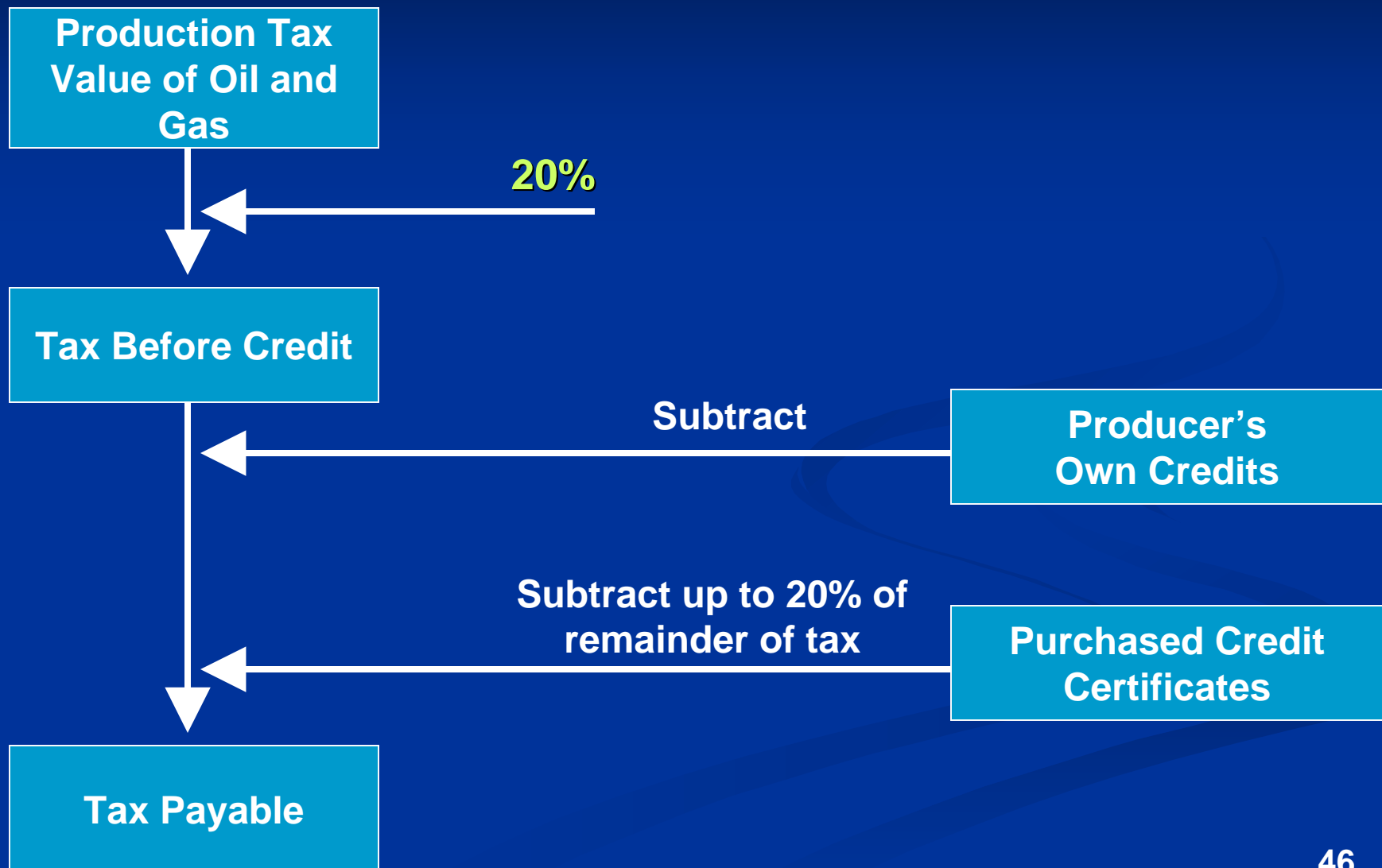
AS 43.55.024 (a) and (b)



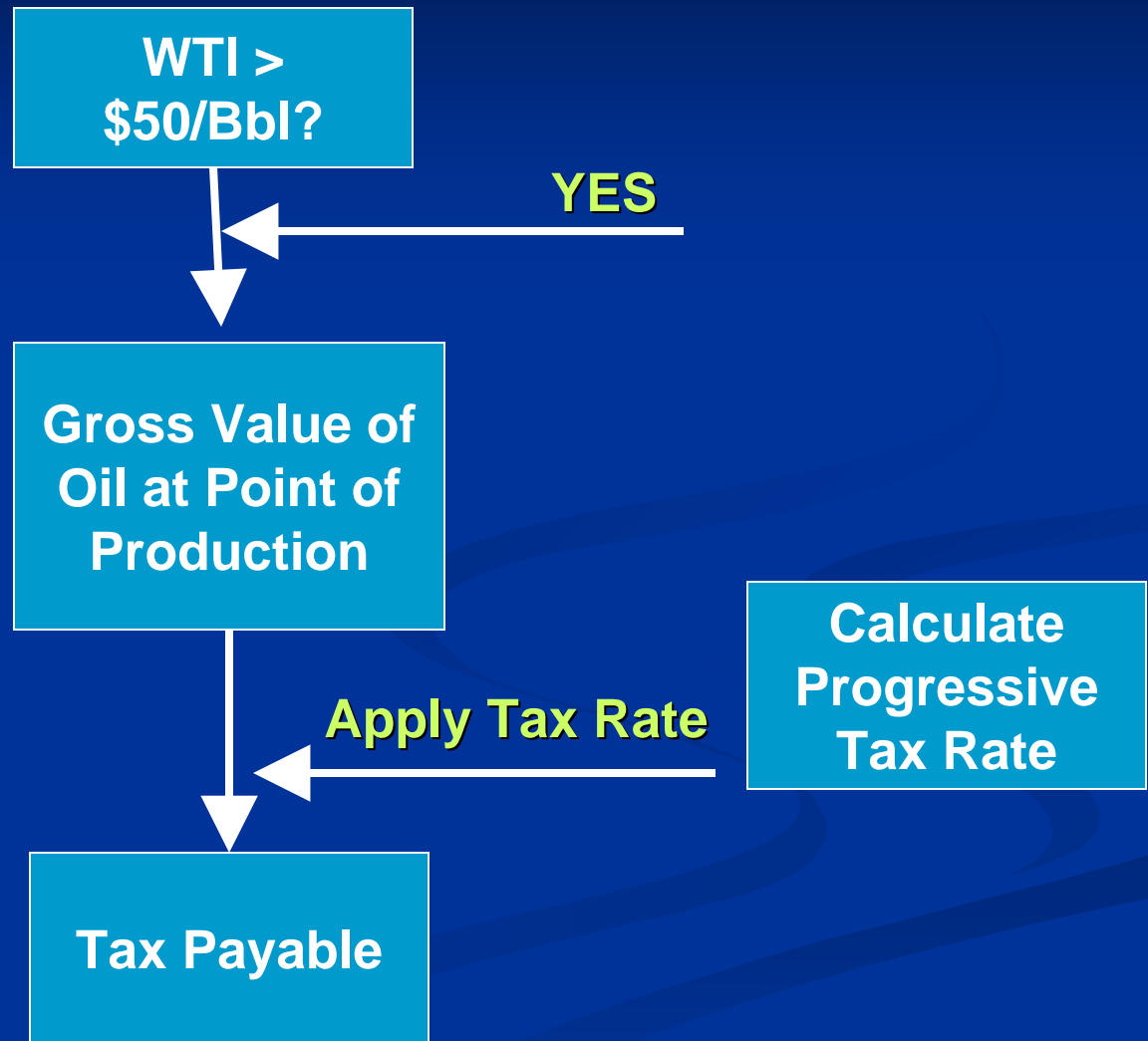
TRANSFERABLE TAX CREDIT CERTIFICATES - AS 43.55.024 (d)-(g)



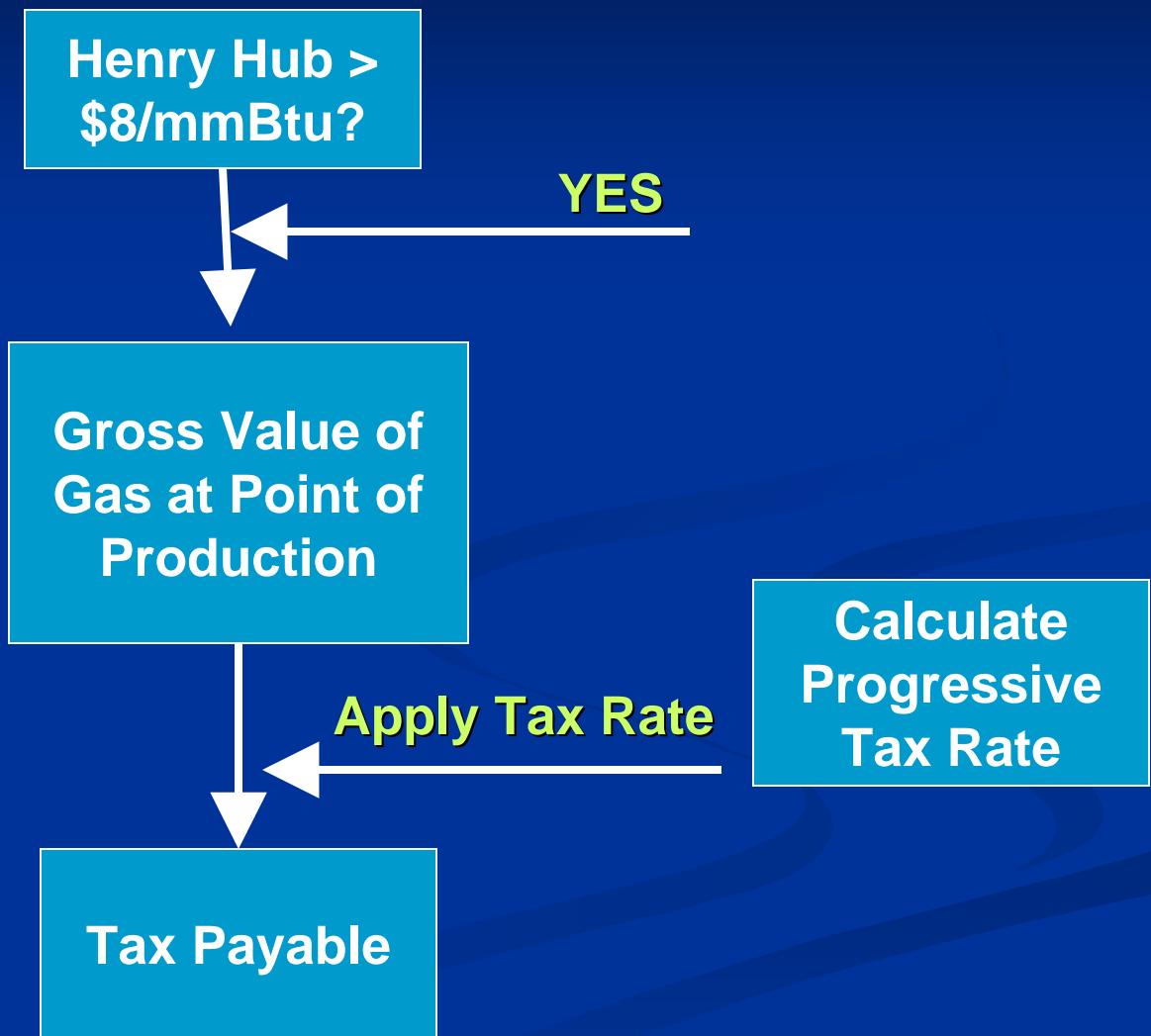
TAX CALCULATION: AS 43.55.011(a), 43.55.024, 43.55.025, 43.55.170



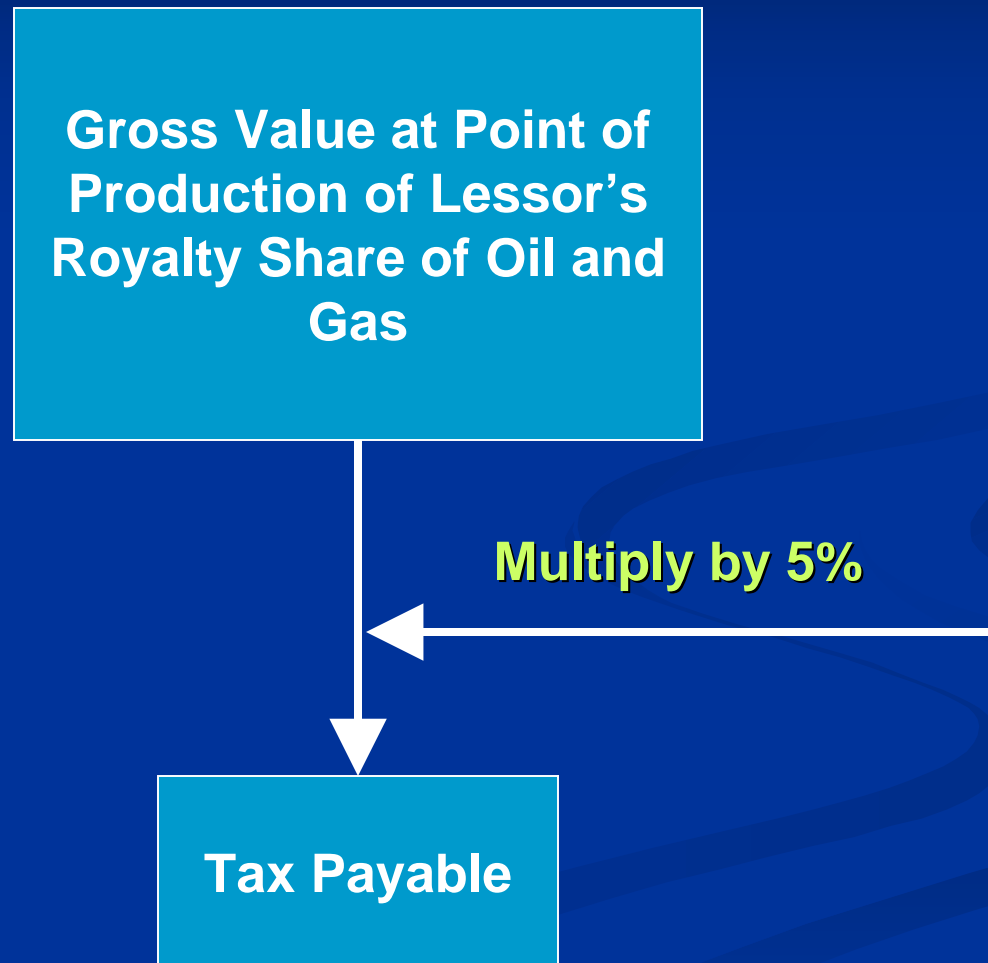
TAX CALCULATION: AS 43.55.011(f) – (h)



TAX CALCULATION: AS 43.55.011(i) –(k)



TAX CALCULATION: AS 43.55.011(e)



TAX PAYMENT

AS 43.55.020(a), (g), and (h)

