Fiscal Note

State of Alaska
2017 Legislative Session

Bill Version: HB 111
Fiscal Note Number:
() Publish Date:

Identifier: HB111CS(RES)-DOR-TAX-03-16-17
Title: OIL & GAS PRODUCTION TAX;PAYMENTS;CREDITS
Sponsor: RESOURCES
Requester: House Finance Committee

Department: Department of Revenue
Appropriation: Taxation and Treasury
Allocation: Tax Division
OMB Component Number: 2476

Expenditures/Revenues

Note: Amounts do not include inflation unless otherwise noted below. (Thousands of Dollars)

	FY2018 Appropriation Requested	Included in Governor's FY2018 Request	Out-Year Cost Estimates				
OPERATING EXPENDITURES	**FY 2018**	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**	**FY 2022**	**FY 2023**
Personal Services							
Travel							
Services							
Commodities							
Capital Outlay							
Grants & Benefits							
Miscellaneous							
Total Operating	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Fund Source (Operating Only)

None							
Total	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Positions

Full-time							
Part-time							
Temporary							

Change in Revenues

1250 UGF Rev (UGF)	45,000.0		75,000.0	60,000.0	60,000.0	65,000.0	65,000.0
Total	**45,000.0**	**0.0**	**75,000.0**	**60,000.0**	**60,000.0**	**65,000.0**	**65,000.0**

Estimated SUPPLEMENTAL (FY2017) cost: 0.0 *(separate supplemental appropriation required)*
(discuss reasons and fund source(s) in analysis section)

Estimated CAPITAL (FY2018) cost: 1,200.0 *(separate capital appropriation required)*
(discuss reasons and fund source(s) in analysis section)

ASSOCIATED REGULATIONS

Does the bill direct, or will the bill result in, regulation changes adopted by your agency? yes
If yes, by what date are the regulations to be adopted, amended or repealed? 01/01/18

Why this fiscal note differs from previous version:

Revised to reflect House Resources committee substitute.

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Approved By: Jerry Burnett, Deputy Commissioner
Agency: Department of Revenue

Phone: (907)465-8221
Date: 03/14/2017 10:00 PM
Date: 03/16/17

STATE OF ALASKA
2017 LEGISLATIVE SESSION

BILL NO. CSHB111(RES)

Analysis

Bill Background
This bill would make multiple changes to Alaska's oil and gas production tax and tax credit statutes. Various credits have been added to statute since 2003, with state repurchase beginning in 2007. Through the end of FY 2016, about $8 billion in tax credits have been received by companies. This includes both credits used against tax liability and credits repurchased by the state; it also includes activity on both the North Slope and other areas of the state.

Legislation passed in 2016 which focused on scaling back credits available in Cook Inlet. Those changes, combined with the sunset of most exploration credits that also occurred in 2016, reduces the state's estimates of future credit demand. Nevertheless, the volume of tax credit certificates eligible for state purchase continues to grow. If annual appropriations continue according to the statutory formula, the current forecast indicates $1.6 billion in purchasable credits outstanding in 2026. Additionally, there have been several large discoveries recently announced on the North Slope; if any of these were sanctioned and built it could result in additional billions in credit liability that under current law could be payable far in advance of any additional tax or royalty revenue from the development.

Under this bill, the state would cease offering transferrable or cashable tax credit certificates for work done on the North Slope. Instead, companies would be expected to carry forward their losses until such time as they owe a tax liability to the state, at which time they could be used to offset the company's oil and gas production taxes. Additionally, the state’s contribution towards many projects will be reduced. Additional provisions of the bill will increase the oil and gas production tax under certain circumstances.

Summary of Revenue Impact
The bill's fiscal impacts can be divided into two categories: increases to revenue (taxes), and reductions in the demand for tax credit repurchases (appropriations). The cover page table only includes the revenue items as it is impossible to predict future appropriations. Savings due to reductions in demand for future appropriations to purchase tax credits are noted in the summary table on page 4. The table shows the impact at forecasted oil prices. Additionally, the bar charts on the bottom of page 4 also examine the average total impact at a wide range of possible oil prices.

The initial revenue impact from this bill would be concentrated in changes to the minimum production tax. This is an alternative tax calculation to the standard "35% net tax less per-barrel credits." Taxpayers pay the higher of two calculations, the net tax as described above or 4% of the gross value at the point of production. Currently, the crossover point is at about $74 per barrel- at oil prices below that point the minimum tax tends to be used, and at higher prices the net tax is used. HB111 increases the minimum tax from 4% (at oil prices above $25) to 5% (at oil prices above $50). This would result in a tax increase at prices below the crossover, in the amount of $45-$75 million per year.

Additionally, HB111 prevents certain credits from being used to reduce tax payments below the minimum tax, a concept colloquially known as "hardening the floor." This will have a smaller revenue impact that disappears in future years as the price of oil increases. A further change changes the price thresholds for the per-taxable-barrel credit, reducing this credit by $2 at most prices. Because of the interaction of this tax feature with the minimum tax, the proposed change would only have a fiscal impact at oil prices above about $75 per barrel. This is seen in some of the later years in the fiscal note analysis.

Analysis

Also, a small indeterminate amount of additional revenue would come from the elimination of the "zero interest rate" provision after three years of production tax delinquency.

Implementation Cost

The changes anticipated in this bill will require somewhat substantial reprogramming of the Tax Revenue Management System and Revenue Online tax portal. Based on the required changes after the passage of HB247 in 2016, we currently assume a one-time cost of about $1,200,000 to accomplish this. We do not anticipate any additional costs to administer the tax program. There will also be a need for substantial amendments to existing regulations to fully implement the changes.

Detail of Specific Provisions

1) Eliminates the 35% Carried Forward Annual Loss Credit (also known as "NOL") rate for the North Slope, effective 1/1/18. This change would reduce the future liability from this credit. Instead of the credit, taxpayers will be able to carry forward 50% of their DNR pre-approved lease expenditures to be used against future taxes. An "uplift", or interest, is added to the carried forward balance.

2) Hardens the floor, so no credits can be used to reduce payments below the minimum tax. At extremely low prices, where major producers could have operating losses, this could result in up to $200 million in added revenue.

3) Increases the minimum tax rate from 4% (at oil prices above $25) to 5% (at oil prices above $50).

4) NOLs will be no longer eligible for cash beginning in 2018. This change would not impact the credit certificates, estimated at about $900 million, that will be in company hands at the end of 2017 given no further action.

5) The amount of cash that each company can receive per year for repurchased credits is reduced to $35 million. This is currently $70 million with a "haircut" provision that makes it effectively $61 million. The haircut is repealed. Eligibility for state cash for credits is also limited to companies producing 15,000 barrels per day or less.

6) Sliding scale per-barrel credit changed so that the $8 credit is for GVPP below $60, with credits generally $2 less than current statute. Credit drops from $3 to zero at Gross Value at the Point of Production at or above $110 per barrel.

7) The Gross Value at the Point of Production for a given property can not go below zero. This would only impact a very high tariff (likely remote) field at very low prices, so those fields could not have negative wellhead value that could offset other tax liability.

8) Eliminates the zero interest rate for delinquent taxes that currently take effect after three years of delinquency.

9) Limits the use of per-taxable-barrel credits to the month in which they were earned. This prevents the so-called "migrating credits" issue where per-barrel credits earned but unused in a month with oil prices under the minimum tax can be used to reduce taxes from a higher oil price month. This only has a revenue impact in a year with highly volatile oil prices.

10) A new "dry hole" credit is added for 15% of qualifying exploration expenditures.

FISCAL NOTE ANALYSIS

STATE OF ALASKA
2017 LEGISLATIVE SESSION

BILL NO. CSHB111(RES)

Analysis

(Revised 1/11/17 OMB/LFD)

Provisions in CSHB 111 (RES)\N and their Estimated Fiscal Impact based on Fall 2016 Forecast ($millions) - Fall 2016 FC PRICE

Revised 3-13-17 by Dept. of Revenue

Description of Provision	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
1. Effective 1/1/18, Operating loss credit eliminated for North Slope and replaced with carry-forward lease expenditures provision. A company may carry forward 50% of DNR-approved North Slope lease expenditures not deducted against tax. Carry-forward earns interest for up to 7 years.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
2. No credits can reduce tax below the minimum tax effective 1/1/18.	$20	$15	$0	$0	$0	$0	$0	-$10	-$25	-$5
3. Minimum tax increased to 5% of GVPP at prices of $50 and above, and GVR reduces basis for minimum tax, effective 1/1/18.	$20	$65	$60	$60	$65	$65	$65	$60	$50	$50
4. No cash repurchase available for net operating loss credits based on expenses incurred after 1/1/18 (for purposes of this fiscal note, assumes all outstanding credits are funded in FY 2018).	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
5. State purchase of credits limited to $35 million per company per year, and only companies with less than 15,000 BTU-equivalent barrels of production, effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
6. Sliding scale per-taxable-barrel credits changed to $8 when GVPP per barrel is less than $60, with brackets ranging to zero when GVPP per barrel is $110 and above, effective 1/1/18.	$0	$0	$0	$0	$0	$0	$10	$65	$70	$65
7. Gross value at point of production (GVPP) cannot go below zero effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
8. Interest on delinquent taxes continues to accrue after 3 years, retroactive to 1/1/17.	Indeterminate - likely positive for state.									
9. No true-up of excess per-taxable-barrel credits effective 1/1/18.	No impact under forecast - could benefit state if prices are volatile.									
10. New "dry hole" credit of 15% of qualifying expenditures, effective 1/1/18.	Indeterminate									
Additional impact of implementing above provisions together vs standalone.	$5	-$5	$0	$0	$0	$0	$0	-$30	$25	$5
Total Revenue Impact	**$45**	**$75**	**$60**	**$60**	**$65**	**$65**	**$75**	**$85**	**$120**	**$115**
A. Budget impact of operating loss and carry-forward lease expenditures changes effective 1/1/18.	$0	$45	$105	$115	$125	$135	$135	$140	$140	$140
B. Budget impact of no credits can reduce tax below the minimum tax effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
C. Budget impact of minimum tax changes effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
D. Budget impact of no cash repurchase for net NOL credits earned after 1/1/18.	$0	$45	$110	$120	$130	$140	$140	$145	$145	$145
E. Budget impact of new limits to credit repurchase eligibility, effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
F. Budget impact of adjustments to sliding scale per-taxable-barrel credits, effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
G. Budget impact of GVPP cannot go below zero effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
H. Budget impact of interest accrual changes, retroactive to 1/1/17.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
I. Budget impact of no true-up of excess per-taxable-barrel credits effective 1/1/18.	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
J. Budget impact of new "dry hole" credit effective 1/1/18.	Indeterminate									
Additional impact of implementing above provisions together vs standalone	$0	-$25	-$85	-$115	-$130	-$140	-$135	-$140	-$140	-$140
Total Budget Impact	**$0**	**$65**	**$130**	**$120**	**$125**	**$135**	**$140**	**$145**	**$145**	**$145**
Total Fiscal Impact - (does not include potential changes in investment)	**$45**	**$140**	**$190**	**$180**	**$190**	**$200**	**$215**	**$230**	**$265**	**$260**
Tax impact of carry-forward lease expenditure balances - current law	$14	$0	$0	$0	$0	$0	$0	$0	$0	$0
Tax impact of carry-forward lease expenditure balances - proposed	$75	$140	$195	$245	$285	$355	$430	$480	$565	$660
Change in year-end balance due to proposal	**$61**	**$140**	**$195**	**$245**	**$285**	**$355**	**$430**	**$480**	**$565**	**$660**

NOTE: The fiscal impact of this proposal is an estimate based on the Fall 2016 revenue forecast. **Estimates shown here are draft / preliminary based on our interpretation of possible changes, and do not include any changes in company behavior as a result of this proposal. We reserve the right to make modifications to estimates for any forthcoming fiscal notes.**