8

Credits

Introduction

Tax credits are an element of tax law that provides incentives for certain activities via a direct reduction in a taxpayer's tax liability. Alaska's tax code provides for a wide range of credits. This chapter provides an overview of the various credits, how they are earned, their limitations, and their revenue impact. Other types of tax expenditures, such as exemptions and exclusions are not included in this chapter, but are detailed in DOR's Alaska Indirect Expenditure Report, a new publication in 2014.

Many tax credits can be applied only in the tax year in which the credit is earned, but some can be carried forward into future years. In some cases, credits are recognized by a tax program when they are applied to an annual or quarterly tax return. These tax credits can be difficult to forecast, as many credits are contingent upon discretionary spending or investments on the part of taxpayers. There are several credit programs that are exceptions, however, and have an approval process prior to the issuance of the credit. One such program is the film production tax credit, which has an extensive approval process prior to issuing credits. Other programs include tax credits applicable to the oil and gas production tax, which are an integral part of the overall fiscal regime, and are built into revenue forecasts.

Recent Developments

In 2014, the 28th Alaska Legislature passed House Bill 306, an act requiring DOR to submit a biennial report to the Legislature detailing indirect expenditures of all agencies in the State under AS 21.06.110. Indirect expenditures include tax credits or other credits, exemptions, discounts, deductions, and differential allowances. HB 306 also imposed or modified sunset dates on certain credits: The Winn Brindle Scholarship tax credit and Salmon Utilization tax credit in 2016, the Film Production Tax credit and the Education credit in 2018, and the Salmon Product and Herring Development credit and Community Development Quota credit in 2020.

Also in 2014, a new credit for qualified infrastructure expenditures for in-state oil refineries was established by House Bill 287 under AS 43.20.053. The former Salmon Product Development Credit, AS 43.75.035, was amended to include herring products, and is now the Salmon and Herring Product Development Credit. House Bill 278 expanded the Education Credit qualifications to include contributions to public or private nonprofit elementary or secondary schools, qualified apprenticeship programs, and regional vocational training schools.

For the North Slope, Senate Bill 21, passed in 2013, amended AS 43.55.023 to allow producers or explorers with qualified capital expenditures to apply 100% of those credits in a calendar year, where previously, only 50% could be applied each calendar year. This change accelerated the use of those credits during calendar year 2013, and as a result, both FY 2013 and FY 2014 show higher than average use of capital expenditure credits.

Oil and Gas Tax Credit Fund

The Oil and Gas Tax Credit Fund, established under AS 43.55.028, was created for the State to purchase certain oil and gas tax credit certificates. Money in this fund is appropriated annually by the Legislature for state purchase of certain transferrable oil and gas tax credit certificates. Credits available for state purchase include the transferrable production tax credits under AS 43.55.023 and AS 43.55.025. Non-transferrable credits are not available for state purchase, and state purchase is only available for companies with fewer than 50,000 British Thermal Units (BTU) equivalent barrels per day of production. This fund allows companies undertaking exploration and development activity to monetize

Table 8-1: FY 2012-2014 Tax credits claimed

	Total Credits Claimed in ($ millions)		
	History		
	FY 2012	**FY 2013**	**FY 2014**(1)
Credits Applicable to the Oil and Gas Production Tax			
Alternative Credit for Exploration, Cook Inlet Jack-Up Rig Credit, and Frontier Basin Credit	$57	$11	$59
Carried-Forward Annual Loss Credit	Totals included in Qualified Capital Expenditure Credit		
Cook Inlet Jack-Up Rig Credit	Totals included in Alternative Credit for Exploration		
Exploration Incentive Credit	$0	$0	$0
Frontier Basin Credit	Totals included in Alternative Credit for Exploration		
Per-Taxable-Barrel Credit	Credit program began on January 1, 2014		$492
Qualified Capital Expenditure Credit, Well Lease Expenditure Credit, and Carried-Forward Annual Loss Credit	$606	$854	$861
Small Producer / New Area Development Credit	$53	$53	$54
Transitional Investment Expenditure Credit	Cannot be reported due to taxpayer confidentiality		
Credits Applicable to the Corporate Income Tax			
Film Production Credit	$3	$6	$21
Gas Exploration and Development Credit	Cannot be reported due to taxpayer confidentiality		
Gas Storage Facility Credit	$0	$0	$15
In-State Gas Refinery Credit	Credit program began on January 1, 2014		
Internal Revenue Code Credits Adopted by Reference	Not tracked		
LNG Storage Facility Credit	Credit program began in 2012	$0	$0
Oil and Gas Industry Service Expenditures Credit	Credit program began on January 1, 2014		
Veteran Employment Tax Credit	Credit program began in FY 2013	$0	$0
Credits Applicable to Multiple Tax Programs			
Education Tax Credit	$4	$7	$3
Minerals Exploration Incentive Credit	$6	$6	$0
Credits Applicable to Fisheries Taxes			
Winn Brindle Scholarship Contributions Credit	<$1	<$1	<$1
Salmon and Herring Product Development Credit	<$1	$2	(<$1)(2)
Community Development Quota Credit	<$1	<$1	<$1
Other Taxes Credit	Not tracked		
Total All Reportable Tax Credits	**$732**	**$940**	**$1,506**

(1)FY 2014 credit totals are estimated pending annual tax filings.

(2)Salmon & Herring Product Development Credits accounted for in FY 2014 were negative as a result of adjustments to prior year credits.

Table 8-2: History of production tax credits 2008-2014

Fiscal Year	2007	2008	2009	2010	2011	2012	2013	2014[1]
				($ millions)				
Statewide Credits								
Credits Used against Tax Liability	**557**	378	333	412	386	363	549	888
Credits Purchased by the State[2]	**55**	54	193	250	450	353	369	593
Total Statewide Production Tax Credits	**612**	**432**	**526**	**662**	**836**	**716**	**918**	**1,481**

the full value of their tax credits when they do not have an offsetting tax liability. Additionally, certain Corporate Income Tax credits under AS 43.20 are also eligible for state purchase from the Oil and gas tax credit fund, including the Gas Storage Facility Credit, the In-State Refinery Tax Credit, and the LNG Storage Facility Credit.

DOR expectations for credits purchased by the state are partly dependent on oil forecasts. At lower oil prices, more producers incur a net operating loss, which increases the amounts of carried-forward annual loss credits eligible for state purchase. At higher oil prices, the same producers may have a smaller net operating loss, or a positive tax liability before credits. As a result, credits for potential state purchase will increase as oil prices decrease. This feature of the tax system is one of the primary reasons that the forecast for credits purchased by the state in FY 2015 and FY 2016 increased over the prior forecast. Oil price expectations for FY 2015 and FY 2016 have been reduced, and we are now forecasting credits purchased by the state of $625 million in FY 2015 and $700 million in FY 2016, as shown in Table 8-3.

Credits Applicable to the Oil and Gas Production Tax

Alternative Credit for Exploration

The Alternative Credit for Exploration is a transferable credit for expenditures for certain oil and gas exploration activities. Outside of Cook inlet, the credit is 40% for seismic costs outside an existing unit, 30% for drilling costs greater than 25 miles from an existing unit, 30% for pre-approved new targets greater than 3 miles from an existing well, and 40% for pre-approved new targets greater than 3 miles from a well and greater than 25 miles from an existing unit. The 3-mile limit does not apply for wells in "Frontier Basins," as described under the Frontier Basin Credit below. For Cook Inlet, the credit is 40% for seismic costs outside an existing unit, 30% for drilling costs greater than 10 miles from an existing unit, 30% for pre-approved new targets, and 40% for drilling costs that are greater than 10 miles from an existing unit and pre-approved new targets. The credit expires on July 1, 2016 for the North Slope and Cook Inlet; for areas other than the North Slope and Cook Inlet, the credit expires January 1, 2022.

Carried-Forward Annual Loss Credit

This credit is a transferable credit for a carried-forward annual loss, defined as a producer or explorer's adjusted lease expenditures that are not deductible in calculating production tax values for the calendar year. For areas outside the North Slope, the credit is 25% of the carried-forward annual loss. Beginning January 1, 2014, the credit for carried-forward annual losses incurred on the North Slope increased to 45% of the loss, and certificates for these credits may be taken in a single year. On January 1, 2016, the credits for losses incurred on the North Slope decreases to 35% of the loss.

Cook Inlet Jack-Up Rig Credit

This credit is for exploration expenses for the first three wells drilled by the first jack-up rig brought in to Cook Inlet. It is only for expenses incurred in drilling wells that test pre-tertiary; all three wells must be drilled by unaffiliated parties using the same rig. The credit is 100% of costs for the first well up to $25 million, 90% of costs for the second well up to $22.5 million, and 80% of costs for the third well up to $20 million. If the exploration well is brought into production, the operator repays 50% of the credit over ten

[1] FY 2014 credit totals are estimated pending annual tax filings.

[2] Credits Purchased by the State consists primarily of production tax credits purchased, but also includes corporate income corporate income tax credits available for state purchase from the Oil and Gas Tax Credit Fund. These include the gas storage facility credit, LNG storage facility credit, and refinery credits.

Table 8-3: Fall 2014 10-year forecast for production tax credits

	($ millions)									
Fiscal Year	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Statewide Credits										
Credits Used against Tax Liability	750	510	1,180	990	810	710	650	490	460	400
Credits Purchased by the State	625	700	400	250	250	250	250	250	250	250
Total Statewide Production Tax Credits	**1,375**	**1,210**	**1,580**	**1,240**	**1,060**	**960**	**900**	**740**	**710**	**650**

years following production start-up.

Exploration Incentive Credit

The exploration incentive credit is a non-transferrable credit for the cost of drilling or seismic work performed under a limited time period established by the Commissioner of the Department of Natural Resources. Credit may be granted for up to 50% of the cost of drilling or seismic work, not to exceed 50% of the tax liability to which it is being applied. This credit may also be applied against the State royalty.

Frontier Basin Credit

The Frontier Basin Credit is for expenses for the first four persons to drill exploration wells and the first four persons to conduct seismic projects within an area designated in AS 43.55.025(p), also called the "Frontier Basins." The credit is for the lesser of 80% of qualified exploration drilling expenses or $25 million; or for seismic projects, credit is for lesser of 75% of qualified seismic exploration expenditures or $7.5 million. It includes expenditures incurred for work performed after June 1, 2012 and before July 1, 2016.

Per-Taxable-Barrel Credit

Beginning January 1, 2014, there is a per-taxable-barrel credit for oil production on the North Slope. This credit cannot be transferred, carried forward, or used to reduce the producer's tax liability to less than zero.

In areas that qualify for a gross value reduction (GVR), the credit is $5 per taxable barrel. Those areas are defined in AS 43.55.160(f) and (g).

For areas that do not qualify for a GVR, the credit ranges from $0 to $8 per taxable barrel based on price. The sliding scale credit is a dollar-per-taxable-barrel credit ranging from zero dollars per barrel at per-barrel gross value at point of production (GVPP) values greater than $150 to $8 per barrel at per-barrel GVPP values less than $80. The credit for non-GVR eligible oil may not reduce the producer's tax liability to less than the minimum tax established under AS 43.55.011(f).

The vast majority of oil produced on the North Slope in not GVR-eligible. Therefore, the structure of the per-taxable-barrel credit is such that as the price of oil increases, the dollar value of the credit decreases. Likewise, when the price of oil decreases, the dollar value of the credit increases.

Qualified Capital Expenditure and Well Lease Expenditure Credit

This credit is a transferable tax credit for qualified oil and gas capital expenditures in the State and outside the North Slope. It can be taken in lieu of exploration incentive credits under AS 43.55.025 and gas exploration credits under AS 43.20.043. The credit is 20% of eligible capital expenditures, or 40% for qualified well lease expenditures. As of January 1, 2014, the qualified capital expenditure credit is no longer available for North Slope capital expenditures.

Small Producer / New Area Development Credit

The Small Producer Credit is a non-transferable credit for oil and gas produced by small producers, defined as having average taxable oil and gas production of less than 100,000 BTU equivalent barrels per day. The credit is available until the later of 2016 or nine years after the first commercial production of oil and gas on the properties for which the credit applies. The small producer credit is capped at $12 million annually for producers with less than 50,000 BTU equivalent barrels per day. The credit then phases out, reaching to zero for producers with 100,000 or more BTU equivalent barrels per day. The credit may only be used against a tax liability, providing the producer has a positive tax liability before the application of credits.

The New Area Development Credit is a credit of up to $6 million per company annually, for oil or gas produced from leases outside Cook Inlet and south of 68 degrees North latitude, providing the producer has a positive tax liability on that production before the application of credits. The credit is available until the later of 2016 or nine years after the first commercial production of oil and gas on the properties for which the credit applies.

Transitional Investment Expenditure Credit

The transitional investment expenditure credit is a non-transferable credit for qualified oil and gas capital expenditures incurred between March 31, 2001 and April 1, 2006. It is only available to companies that did not have production in commercial quantities prior to January 1, 2008. The credit is 20% of qualified oil and gas capital expenditures incurred between March 31, 2001 and April 1, 2006, not to exceed 10% of the capital expenditures incurred between March 31, 2006 and January 1, 2008. The credit was only available until December 31, 2013.

Credits Applicable to Corporate Income Tax

Gas Exploration and Development Credit

The Gas Exploration and Development Credit is a non-transferable credit for qualified expenditures for the exploration and development of non-North Slope natural gas reserves. The credit is 25% of qualified expenditures for investment after January 1, 2010; investments in existing units qualify. The credit is capped at 75% of tax liability as calculated before applying other credits.

Gas Storage Facility Credit

The Gas Storage Facility Credit is a non-transferable credit for the costs incurred to establish a natural gas storage facility. The credit is $1.50 per thousand cubic feet of "working gas" storage capacity as determined by the Alaska Oil and Gas Conservation Commission. It does not apply to gas storage related to a gas sales pipeline on the North Slope. To qualify, the facility must operate as a public utility regulated by the Regulatory Commission of Alaska with open access for third parties. It is effective for facilities placed into service between January 1, 2011 and December 31, 2015. The maximum credit is the lesser of $15 million or 25% of costs incurred to establish the facility.

In-State Refinery Tax Credit

The In-State Refinery Tax Credit is a credit for qualified infrastructure expenditures for in-state oil refineries. The credit may not exceed the lesser of 40% of total qualifying expenditures or $10 million per tax year per refinery. The credit can be applied against corporate income tax liability and carried forward for up to five years, or purchase by the state via the Oil and Gas Tax Credit Fund. The authorizing statute will sunset on December 31, 2019.

Internal Revenue Code Credits Adopted By Reference

Under Alaska's blanket adoption of the federal Internal Revenue Code, taxpayers can claim all federal incentive credits. Federal credits that refund other federal taxes are not allowed. Multistate taxpayers apportion their total federal incentive credits. In most cases, the credit is limited to 18% of the amount of the credit determined for federal income tax purposes which is attributable to Alaska.

LNG Storage Facility Credit

The LNG Storage Facility Credit is a non-transferable, refundable credit for the costs incurred to establish a storage facility for liquefied natural gas. The credit is lesser of $15 million or 50% of costs incurred to establish the facility. It applies to facilities with a minimum storage capacity of 25,000 gallons of LNG, and that are public utilities regulated by the Regulatory Commission of Alaska. It is for facilities placed into service after January 1, 2011.

Oil and Gas Industry Service Expenditures Credit, AS 43.20.049

The Oil and Gas Industry Service Expenditures Credit is a credit of 10% of qualified oil and gas industry service expenditures that are for in-state manufacture or in-state modification of oil and gas tangible personal property with a service life of three years or more. The credit may be applied to corporate income tax liabilities in amounts up to $10 million per taxpayer per year. The credit is effective for expenditures incurred after January 1, 2014. The credit is not transferable but any amount of the credit that exceeds the taxpayer's liability may be carried forward up to five years.

Minerals Exploration Incentive Credit

See "Credits Applicable to Multiple Tax Programs."

Veteran Employment Tax Credit

The Veteran Employment Credit is a non-transferable credit for corporate income taxpayers that employ qualified veterans in the State. A "qualified veteran" is a veteran who was unemployed for more than four weeks preceding the employment date and who was discharged or released from military service not more than ten years before employment date (for a disabled veteran) or not more than two years before employment date (for a veteran who is not disabled). The credit is $3,000 for a disabled veteran or $2,000 for a veteran who is not disabled for employment for a minimum of 1,560 hours during 12 consecutive months following the veteran's employment date. For seasonal employment, the credit is $1,000 for a veteran employed for a minimum of 500 hours during three consecutive months following the employment date.

Credits Applicable to