taxnotes® state

Volume 108, Number 6 ■ May 8, 2023

# Things Heat Up in Juneau

by Jonathan E. Iversen

Reprinted from *Tax Notes State*, May 8, 2023, p. 513

© 2023 Tax Analysts. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

# Things Heat Up in Juneau

**by Jonathan E. Iversen**

Jonathan E. Iversen

Jonathan E. Iversen is the managing partner of Stoel Rives LLP's office in Anchorage, Alaska. He provides tax planning and tax structuring advice and represents clients in tax audits and appeals. His practice emphasizes Alaska state and local taxation. Previously, Iversen served as director of the Alaska Department of Revenue's Tax Division.

In this installment of Alaska Tax: The Last Frontier, Iversen reviews recent tax bills introduced in the Legislature, including S.B. 114, which would impose a new income tax and substantially increase the oil and gas production tax.

Copyright 2023 Jonathan E. Iversen. All rights reserved.

As of this writing, we are finally starting the transition from winter to spring in Anchorage. It is the period that Alaskans refer to as breakup, typically a period of warmer temperatures and more sunshine. The snow becomes softer and heavier, with slush the norm in parking lots. We can finally see asphalt streets that have been hidden by snow and ice for months. And although it is warmer, it is also a messy time of the year, characterized by road grit, often muddy conditions, and treacherous potholes.

And things are heating up in Juneau as well, not just with warmer weather, but also with legislative activity. The state budget is a perennial source of debate for the Legislature, and the Alaska Department of Revenue issued its spring 2023 revenue forecast March 21. Compared with the fall 2022 revenue forecast, DOR predicted decreased oil prices for Alaska North Slope (ANS) oil by $3.20 per barrel for fiscal 2023 and $8 per barrel for fiscal 2024.[1] DOR also reduced its forecast of ANS oil production by 6,500 barrels per day for fiscal 2023 and by 7,200 barrels per day for fiscal 2024.[2] Given how reliant Alaska's revenues are on oil, the comparatively less rosy forecasts resulted in reductions in forecast unrestricted general fund revenue by $246 million for fiscal 2023 and $679 million for fiscal 2024, as well as reductions for predicted revenue for later years.[3]

In at least partial response to the revised revenue outlook, a number of legislators have introduced bills to increase existing taxes or impose new taxes. Some of these pieces of legislation have had hearings and are getting substantial attention from current and potential taxpayers. The regular legislative session is well over the halfway point, having started January 17, with a duration limited to 121 days by the Alaska Constitution.[4] It is unclear how much traction any tax increase will get this session, and with roughly a month left any substantial changes appear unlikely. In any event, several proposals are particularly troubling for taxpayers.

## Tax Legislation

Some of the tax bills introduced this session are summarized below.

H.B. 70 would add an exemption from general property taxation for certain properties owned or operated by an organization incorporated under state law that is exempt from taxation under IRC section 501(c). This includes parking lots used for

[1] Alaska Department of Revenue, Tax Division, "Spring 2023 Revenue Forecast" (Mar. 20, 2023).

[2] *Id.*

[3] *Id.*

[4] Alaska Const. Art. II, section 8.



For more *Tax Notes® State* content, please visit www.taxnotes.com.

© 2023 Tax Analysts. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

parking or another use as long as it is permitted without charge. The bill also would create an exemption for real and personal property of a store that (1) deals exclusively in donated inventory that is distributed without cost as part of a program to provide needy people with food, shelter, clothing, or healthcare without charge; or (2) sells merchandise below market value to support a literacy program or a program to provide needy people with food, shelter, clothing, or healthcare without charge. An organization that owns property exempt from taxation under the bill may still qualify for the exemption if it leases the property to another organization incorporated under state law that is exempt from taxation and (1) that organization uses the property for an activity that is exempt under the bill; (2) the lease payments are not the owner's dominant profit motive; and (3) the amount the owner charges is incidental to and reasonably necessary for the exempt use of the property and does not exceed its operational requirements.

H.B. 84/S.B. 77 would allow municipalities to fully exempt economic development properties from property taxes by removing a limitation. This proposed legislation would also allow municipalities to levy a tax on "blighted" properties that are heavily deteriorated and can reduce property tax and the value of neighboring properties. This "blight tax" would impose a higher tax on these properties, which would later be reduced when the property is remediated so that it is no longer considered blighted. The bill leaves it to local governments to define blighted and what is considered "remediated," and to establish the tax rate, but each municipality that uses this tax must adopt ordinances to impose it.

Alaska's corporate income tax has nine tax brackets and a maximum tax rate of 9.4 percent on taxable income over $222,000.[5] H.B. 109 would remove eight of the nine tax brackets and leave a single tax rate, so that corporations with taxable income over $25,000 would be taxed at a flat 2 percent rate.

Alaska imposes an excise tax of $50 per ounce on the sale or transfer of marijuana from a cultivation facility to a retail store or marijuana product manufacturing facility.[6] H.B. 119 would reduce the tax levied on the cultivator to $12.50 per ounce. The bill would also add a 3 percent tax on the sale of marijuana and marijuana products from a retail marijuana store to a consumer.

H.B. 134 would prohibit a borough, city, or the state from levying a tax on the transfer of real property.

H.B. 142 would impose a 2 percent tax on all sales of goods and services purchased in Alaska. It would allow the Legislature to share half the tax revenue with municipalities that meet certain criteria, including not having property taxes over 10 mills.

H.B. 144 would repeal the sunset of the education tax credit.

H.B. 156 would impose a tax on the income of resident individuals, trusts, and estates, and on income of nonresident individuals, trusts, and estates derived from or connected with a source in the state. The tax would be 2 percent of an individual's taxable income over $200,000. There would also be a tax of $20 per year on each individual who has wages, net earnings from self-employment, or combined wages and net earnings from self-employment in the state. The tax on trusts and estates would be $20 plus 2 percent of taxable income over $200,000.

S.B. 89 would (1) raise the minimum age to buy, sell, or possess tobacco and electronic smoking products from 19 to 21; and (2) establish a sales tax on closed electronic smoking products and vapor products of 25 percent of the sales price.

S.B. 114 would impose a new income tax and would substantially increase the oil and gas production tax, Alaska Stat. section 43.55.

The new income tax would be imposed on a "qualified entity" at a rate of 9.4 percent on "qualified taxable income" over $4 million per year. This would not apply to corporations paying the corporate income tax under Alaska Stat. section 43.20.011, but instead is intended to tax a qualified entity, which is defined as a partnership, sole proprietorship, or S corporation. Qualified taxable income is defined as income from oil and gas production or transportation in Alaska.

[5] Alaska Stat. section 43.20.011(e).

[6] Alaska Stat. section 43.61.010(a).



For more *Tax Notes® State* content, please visit www.taxnotes.com.

© 2023 Tax Analysts. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

To understand S.B. 114's potential impact on the oil and gas production tax, it is helpful to have a basic understanding of this unique and complex tax structure. In general, Alaska's production tax is levied on the net revenue of oil and gas production from leases or properties in the state.[7] The calculation of net revenue begins with the destination (market) value less the pipeline and marine transportation costs to get from the point of production to the destination market. The result of this first step is the gross value at the point of production (GVPP), often referred to as wellhead value. The operating and capital costs of oil and gas exploration, development, or production upstream of the point of production are then subtracted from the GVPP to reach net revenue.[8] Net revenue is then multiplied by the tax rate, and the result is reduced by credits.

Alaska Stat. section 43.55.024(i) provides a credit of $5 per taxable barrel for certain taxable North Slope oil produced from comparatively newer fields. To be eligible, the taxable production must satisfy certain statutory criteria. The $5-per-barrel credit is available for oil and gas produced from each property only for a certain period. For oil or gas first produced from a lease or property after 2016, the reduction is available from the date of commencement of regular production from that lease or property and expires after three years (consecutive or nonconsecutive) in which average annual ANS West Coast price is more than $70 per barrel, or after seven years, whichever occurs first. For oil or gas first produced from a lease or property before 2017, the reduction ceases on the earlier of 2023 or after three years (consecutive or nonconsecutive) in which average annual ANS West Coast price is more than $70 per barrel.

ANS oil production that does not qualify for the $5-per-barrel credit qualifies for a production tax credit under Alaska Stat. section 43.55.024(j), often referred to as the sliding scale credit or per-barrel credit. The credit amount decreases as oil prices rise, resulting in higher effective tax rates at higher oil prices. The maximum credit is $8 per barrel of taxable oil if the average GVPP for the month is less than $80 per barrel. If the average is greater than $80 and less than $90 per barrel, the credit is $7 per barrel. The amount of credit per barrel drops by $1 for each $10 incremental increase in GVPP, and is zero if the average GVPP is $150 per barrel or higher. Thus, this credit integrates an element of progressivity into the production tax.

The original version of S.B. 114 would have added an element of ring-fencing to the oil and gas production tax, such that for unitized oil and gas properties on the North Slope, the tax would be calculated at the unit level. The result would limit the use of upstream capital and operating expenditures and carried-forward losses because they could be used only in the calculation of production taxes for that unit's production. The ring-fencing alone would have added a tremendous amount of complexity to an already complicated tax structure and was removed from S.B. 114 by the Senate Finance Committee in mid-April.

S.B. 114 would also reduce the Alaska Stat. section 43.55.024(j) per-barrel sliding scale credit for production from North Slope legacy fields by $3 per barrel at each increment, so that the highest level of credit would be $5 rather than $8 per barrel when the GVPP is less than $80 per barrel. The credit would still be reduced by $1 per barrel for each $10 increase in the GVPP, so that the lowest level of credit would be $1 per barrel when the GVPP is from $110 to less than $120 per barrel.

The bill would also limit the use of the $5-per-barrel credit and sliding scale credits earned under Alaska Stat. section 43.55.011(i) and (j) by North Slope producers for each barrel of oil produced to the amount of the producer's capital expenditures for the lease, property, or unit for the calendar year. This would represent a substantial constraint on producers' ability to use these credits.

S.B. 120 would expand the education credits that are available for use against a variety of state taxes. The credit now is 50 percent of contributions. This bill would revise the credit amounts to (1) 50 percent of contributions of not more than $100,000; (2) 100 percent of the next $200,000 of contributions; and (3) 50 percent of the amount of contributions that exceed $300,000. The maximum amount of credits would be increased from $1 million per tax year to $5 million.

[7] Alaska Stat. sections 43.55.011(e) and 43.55.020(e).

[8] Alaska Stat. sections 43.55.150 and 43.55.160.



For more Tax Notes® State content, please visit www.taxnotes.com.

### On the Horizon

It seems likely that the level of legislative activity surrounding tax proposals will continue to be fairly brisk until the regular session ends in mid-May. It is also highly likely that, as usual, the budget will not be finalized until the very end of the session. Taxpayers (and potential taxpayers) and budget hawks will be watching closely. ■

taxnotes®
Federal | State | International

Want to be renowned in the tax community?
Write for Tax Notes.

If you do, you will:

- Receive exposure in the world's leading tax publication
- Join a network of the best and brightest minds in tax

taxnotes.com/acquisitions

Your byline here.

© 2023 Tax Analysts. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.



For more *Tax Notes*® *State* content, please visit www.taxnotes.com.