

1982 Crude Oil Windfall Profit Tax, Third Quarter

By Michael Alexander*

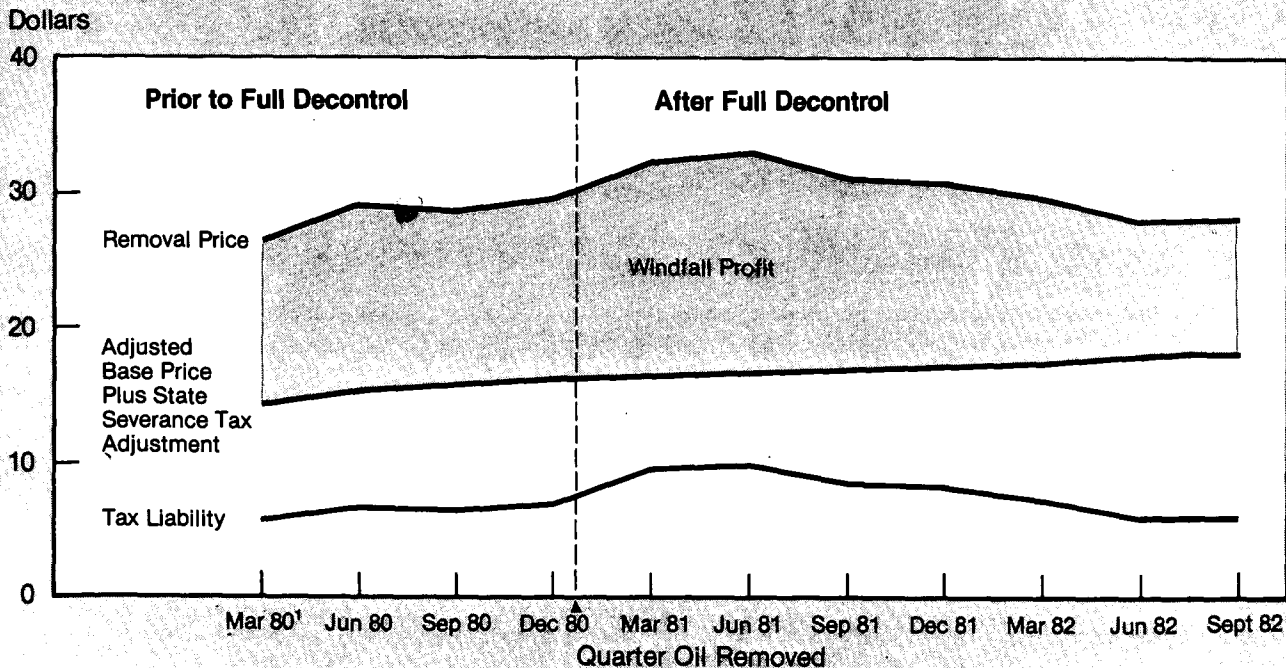
The third quarter of 1982 marked the first time in over a year that windfall profit tax liability (before adjustments) increased from the previous quarter. The increase, although slight, was the result of an increase of almost 2 percent for the average removal price per barrel of domestic crude oil and an increase in the volume of oil removed. To a great extent, the price of domestic crude oil can be tied to the price of foreign crude oil, which increased by more than 2 percent for the same period [1].

Windfall profit, defined as the removal value less the sum of the adjusted base value and State severance tax adjustment, increased by \$200 million from the second quarter to the third quarter of 1982. The increased profit, a result of a rise in the removal price of oil (generally the price for which the oil is sold) and an increase of 20 million barrels of oil removed, caused the windfall profit tax liability before adjustments to rise from the second quarter of 1982 by \$121 million or almost 3 percent. The average windfall profit tax per barrel increased from \$6.01 to \$6.03, which was still significantly lower than the high of \$9.94 reached in the second quarter of 1981.

This increase was a result of the reversal in the declining trend of the average removal price. The average removal price for the third quarter of 1982 increased by \$.46 to \$28.47 per barrel. The average price for foreign crude oil increased from \$30.53 for the second quarter of 1982 to \$31.22 for the third quarter [1].

Shown in the table below is windfall profit tax liability before and after adjustments. Because of a large (\$445 million) negative adjustment, the windfall profit tax liability after adjustments showed a decrease of \$29 million or less than a 1 percent change from the previous quarter. The trend of declining windfall profit tax liability has existed since the second quarter of 1981. These adjustments were necessary as a result of errors in withholding during previous quarters or from the net income limitation. The net income limitation accounted for almost 97 percent of the adjustments for the third quarter of 1982. (The net income limitation provision limits the windfall profit to 90 percent of the net income per barrel of oil and can be estimated by certain taxpayers

Components of Windfall Profit Tax Liability: Averages per Barrel by Quarter Oil Removed



NOTE: Because of price controls during 1980, there were cases where the removal price was less than the adjusted base price and no Form 6047 was filed. The data in the figure are based on information reported.

¹One month only.

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for the current quarter.) Should under- or over-withholding occur, the depositing or withholding agent (usually the first purchaser) is responsible for correcting that error to the extent possible by adjusting the amounts withheld in succeeding quarters. These adjustments are also reflected in the table below. Additional over-withholding of windfall profit tax due to error or the net income limitation which has not been corrected by the withholding agent can be claimed as a refund or credit by producers on their income tax returns.

Based on returns of taxpayers who provided complete detail on how the windfall profit tax is computed [2], tier one oil has always dominated production. For the quarter ended September 1982, tier one oil (which consists of all domestically produced crude oil other than oil specifically classified as tier two or tier three, or explicitly exempted from the tax) represented 65 percent of the total production. Tier two oil, consisting of oil produced from stripper well property and oil from economic interests in a Naval Petroleum Reserve held by the United States, represented 13 percent of the total production. Tier three oil, which consists of heavy oil, incremental tertiary oil and newly discovered oil (70 percent of tier three) accounted for 22 percent of total production as shown below. Newly discovered oil, which has an annual declining tax rate beginning in 1982 and ending in 1986, has had the largest consistent growth in barrels of oil removed since June 1981. The increase for the current quarter for newly discovered oil was 10.8 million barrels or 53 percent of the total increase for all tiers of oil.

Windfall Profit Tax Before and After Adjustments
(Millions)

Quarter Ending	Tax Before Adjustments	Adjustments	Tax After Adjustments
Total	\$51,427	-\$2,610	\$48,817
Mar. 1980 ^{1/}	788	---	788
June 1980	2,842	-21	2,821
Sept. 1980	3,413	-88	3,325
Dec. 1980	3,918	-927	2,991
Mar. 1981	6,953	+242	7,195
June 1981	7,253	-107	7,146
Sept. 1981	6,344	-251	6,093
Dec. 1981	6,007	-497	5,510
Mar. 1982	5,222	-221	5,001
June 1982	4,283	-295	3,988
Sept. 1982	4,404	-445	3,959

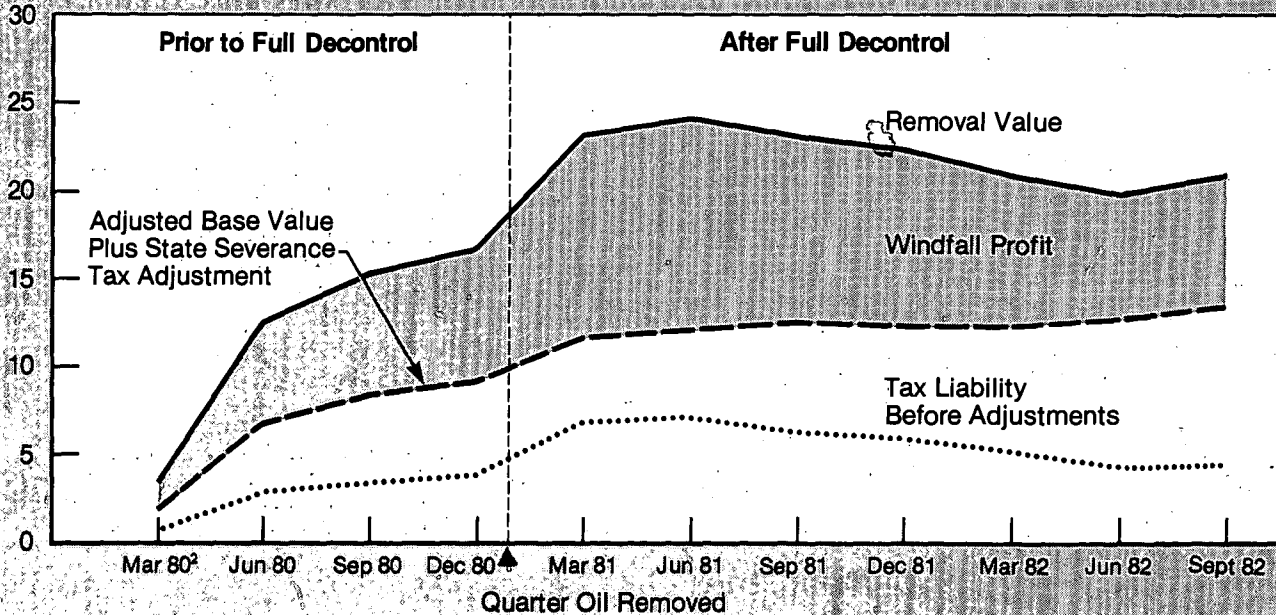
Percentage of Oil Production by Tier of Oil

Quarter Ending	Tier One	Tier Two	Tier Three
June 1981	70	14	16
Sept. 1981	69	14	17
Dec. 1981	69	13	18
Mar. 1982	68	13	19
June 1982	67	13	20
Sept. 1982	65	13	22

^{1/} One month only.

Components¹ of Windfall Profit Tax Liability Before Adjustments: Aggregate Values By Quarter Oil Removed

Billions of Dollars



¹Some returns report windfall profit tax liability only; therefore, data for removal value, adjusted base value and state severance tax adjustment have been adjusted to reflect totals as if all returns reported this detail.

²One month only.

DATA SOURCES AND LIMITATIONS

The Quarterly Federal Excise Tax Return, Form 720, is the form on which the windfall profit tax is reported. Form 6047, Windfall Profit Tax, shows how the tax is computed and is filed as an attachment to Form 720. Tabulations in this article are based on the Form 6047. Returns are due two months after the end of the quarter in which the oil is removed. Data are based on all returns with a tax liability of \$1 million or more before adjustments and a 10 percent sample of all other returns.

Sampling and nonsampling errors were controlled by a variety of methods. Missing returns were requested from the service centers. However, some returns may have been omitted due to time and resource constraints. Attempts were made to correct imbalances in taxpayer entries for the components of windfall profit; if this proved impossible, an out-of-balance return was treated as a return on which the components were not reported, and therefore only the liability for each tier was tabulated. A number of verification checks were performed at all stages of manual data abstraction and computer tabulation.

The SOI Bulletin also includes data on excise tax collections. The excise tax collection figures show the liability after adjustments, as reported on Form 720, from returns entered into the IRS' computerized Business Master File (BMF) each quarter. A number of considerations affect comparisons of data from these two sources. As mentioned above, returns are not due until two months after the close of the taxable quarter; however, the interval between the close of the taxable period and the final recording of the return often varies, so that the quarterly BMF totals usually represent several taxable periods. On the other hand, the data presented here have been tabulated for specific taxable periods. As a result, the two sets of statistics are not directly comparable.

DEFINITIONS

Brief definitions of the terms used in the tables are given below.

Adjusted Base Price.--The base price multiplied by the inflation adjustment, which is derived from the Gross National Product (GNP) "implicit price deflator."

Adjustments to Liability.--Corrections applied to the current quarter's liability in order to correct for the net income limitation and over- and under-withholding in previous quarters.

Base Price.--For tier one oil, the upper tier ceiling price, as defined by Department of Energy price control regulations, which would have applied to the oil had it been produced and sold in May 1979, reduced by 21 cents. For tiers two and three oil, the base prices were \$15.20 and \$16.55, respectively, adjusted for grade and quality.

Crude Oil.--The term applies only to natural crude petroleum and does not include synthetic petroleum, such as oil from shale or tar sands. It does, however, include natural gas liquids treated as crude oil under the June 1979 energy pricing regulations issued by the Department of Energy.

Exempt Alaskan Oil.--Oil from a reservoir other than the Sadlerochit reservoir that has been commercially exploited by any well north of the Arctic Circle; and oil produced north of the divides of the Alaska and Aleutian Ranges, and at least 75 miles from the nearest point of the Trans-Alaskan Pipeline System.

Exempt Charitable Oil.--Oil produced from economic interests held by qualified charitable medical facilities, educational institutions, and child care organizations (as defined in Internal Revenue Code section 170), if such interest was held on January 21, 1980, and at all times thereafter; and oil produced from interests held by a church on January 21, 1980, if, prior to January 22, 1980, the net proceeds of such oil were dedicated to the support of a medical facility, educational institution, or child care facility.

Exempt Governmental Oil.--Oil produced from an economic interest held by a state or political subdivision (including agencies and instrumentalities), the net income from which is used for public purposes.

Exempt Indian Oil.--Oil produced from mineral interests held by or on behalf of Indian tribes or individuals on January 21, 1980, which is one of the following: (a) production received by Indian tribes and individuals from Tribal Trust Lands (the title to such land is held by the United States in trust for the tribes), (b) production from land or mineral interests held by an Indian tribe eligible for services provided to Indians by the Secretary of the Interior, or (c) oil the proceeds from which are paid into the U.S. Treasury to the credit of tribal or native trust funds pursuant to law. This exemption also applies to production of any Alaskan Native Corporation prior to 1991, including wholly-owned subsidiaries of the native Indian corporation as clarified by IRS on September 3, 1983.

Exempt Royalty Oil.--Qualified royalty owners are exempt from the windfall profit tax on two barrels of oil per day for each day of the calendar quarter for oil removed after December 31, 1981. For 1985 and thereafter, three barrels per day will be exempt.

Net Income Limitation.--The windfall profit on a barrel of oil may not exceed 90 percent of the net income attributable to the barrel.

Removal Price.--Generally, the price for which a barrel of oil is sold. In some instances, a constructive sale price is used.

Sadlerochit Oil.--Crude oil production from the Sadlerochit reservoir in the Prudhoe Bay oil field in Alaska.

State Severance Tax Adjustment.--A state severance tax is a tax imposed by a state with respect to the extraction of oil. The windfall profit is reduced by the amount by which the severance tax exceeds that which would have been imposed had the oil been valued at its adjusted base price.

Stripper Oil.--In general, oil from a property for which the average daily production per well has been 10 barrels or less for any consecutive 12-month period after 1972.

Tier One Oil.--All domestically-produced crude oil other than any oil classified in tier two or three, or explicitly exempted by law from the tax. This includes the bulk of domestic oil from reservoirs proven to be productive before 1979.

Tier Two Oil.--Any oil which is from a stripper well property within the meaning of the June 1979 Department of Energy pricing regulations and oil from a U.S. economic interest in a Naval Petroleum Reserve. Note that the Crude Oil Windfall Profit Tax Act of 1980 defined Tier Two Oil as from a "National" Petroleum Reserve. This was amended to read "Naval" Petroleum Reserve by the Technical Corrections Act of 1982.

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Tier Three Oil, Heavy Oil.--All crude oil which is (1) produced from property which had a weighted average gravity of 16.0 degrees or less on the American Petroleum Institute (API) scale, corrected to 60 degrees Fahrenheit, for the last month of production prior to July 1979, or (2) oil from a property with a weighted average gravity of 16.0 degrees API or less, corrected to 60 degrees Fahrenheit, for the taxable period.

Tier Three Oil, Incremental Tertiary Oil.--Production in excess of a base level on a property on which a qualified tertiary recovery project (one which utilizes one of several specific chemical, fluid or gaseous recovery methods to extract oil not recoverable using standard techniques) has been undertaken. The non-incremental oil (i.e., the amount of production up to the base level) remains in the otherwise applicable tier.

Tier Three Oil, Newly Discovered Oil.--Crude oil that is sold after May 31, 1979, and that is produced from (1) an outer continental shelf area for which the lease was entered into on or after January 1, 1979, and from which there was no production in Calendar Year 1978 or (2) an on-shore property developed after Calendar Year 1978.

Windfall Profit.--The excess of the removal price of the barrel of oil over the sum of the adjusted base price and the State severance tax adjustment.

NOTES AND REFERENCES

- [1] U.S. Department of Commerce, Bureau of Economic Analysis, "Commerce News," November 4, 1982.
- [2] At the inception of the windfall profit tax, taxpayers were not required to complete the detail of the Form 6047, which shows how the tax is computed. However, taxpayers were required to provide full information as of January 1981.
- [3] U.S. Department of Commerce, Bureau of Economic Analysis, Survey of Current Business.
- [4] Belal, Carol and Clark, Phil, "Windfall Profit Tax Liability for 1980," SOI Bulletin, Volume 1, No. 2, pages 50-54.
- [5] Joint Committee on Taxation (Staff), "General Explanation of the Crude Oil Windfall Profit Tax Act of 1980", U.S. Government Printing Office, 1981.

Table 1.--Windfall Profit Tax Liability by Oil Tier and Tax Rate For Quarter Ending September 1982 Aggregate Components of Windfall Profit

[Money amounts are in millions of dollars]

Oil tier and tax rate	Number of barrels of oil (000's)	Removal value	Adjusted base value	State severance tax adjustment	Windfall profit	Tax liability before adjustments
	(1)	(2)	(3)	(4)	(5)	(6)
Returns with tax liability shown by oil tier and tax rate, total.....	692,075	19,709	12,282	384	7,043	4,174
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	304,351	9,133	4,770	178	4,185	2,929
Taxed at 50 percent.....	30,150	940	488	27	425	213
Tier one, Sadlerochit oil:						
Taxed at 70 percent.....	115,001	2,416	1,950	75	391	274
Taxed at 50 percent.....	-	-	-	-	-	-
Tier two oil:						
Taxed at 60 percent.....	53,173	1,595	1,013	26	556	334
Taxed at 30 percent.....	39,002	1,199	768	18	413	124
Tier three oil (taxed at 30 percent):						
Newly discovered oil ¹	104,883	3,297	2,400	54	843	232
Incremental tertiary oil.....	12,342	380	273	5	102	30
Heavy oil.....	33,174	750	621	1	128	39
Returns with total tax liability only.....	-	-	-	-	-	231 ²

¹Newly discovered oil is taxed at 27.5 percent beginning in 1982.

²Also includes \$23 million for returns that reported by tier and type, but did not report data for columns 1-5.

NOTE: Detail may not add to total because of rounding.

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Table 2.--Windfall Profit Tax Liability For Returns Reporting Components of Windfall Profit by Oil Tier and Tax Rate For the Quarter Ending September 1982 Average Daily Production and Average Dollars per Barrel

Oil tier and tax rate	Daily production (000's) (barrels)	Removal price	Adjusted base price	State severance tax adjustment	Windfall profit	Tax liability before adjustments
	(1)	(2)	(3)	(4)	(5)	(6)
All returns, total.....	7,523	28.47	17.74	.55	10.18	6.03
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	3,308	30.00	15.67	.58	13.75	9.62
Taxed at 50 percent.....	328	31.17	16.17	.89	14.11	7.04
Tier one, Sadlerochit oil:						
Taxed at 70 percent.....	1,250	21.01	16.95	.65	3.41	2.37
Taxed at 50 percent.....	-	-	-	-	-	-
Tier two oil:						
Taxed at 60 percent.....	578	29.98	19.05	.48	10.45	6.27
Taxed at 30 percent.....	424	30.73	19.68	.46	10.59	3.17
Tier three oil (taxed at 30 percent):						
Newly discovered oil ¹	1,140	31.43	22.88	.51	8.04	2.21
Incremental tertiary oil.....	134	30.77	22.11	.43	8.23	2.46
Heavy oil.....	361	22.60	18.70	.01	3.89	1.16

¹Newly discovered oil is taxed at 27.5 percent beginning in 1982.

NOTE: Detail may not add to total because of rounding.

Table 3.--Windfall Profit Tax Liability by Oil Tier and Tax Rate For January - September 1982 Aggregate Components of Windfall Profit

[Money amounts are in millions of dollars]

Oil tier and tax rate	Number of barrels of oil (000's)	Removal value	Adjusted base value	State severance tax adjustment	Windfall profit	Tax liability before adjustments
	(1)	(2)	(3)	(4)	(5)	(6)
Returns with tax liability shown by oil tier and tax rate, total.....	2,032,440	58,537	35,185	1,196	22,156	13,184
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	915,534	28,165	14,221	585	13,359	9,351
Taxed at 50 percent.....	88,593	2,822	1,415	84	1,323	662
Tier one, Sadlerochit oil:						
Taxed at 70 percent.....	351,029	7,016	5,653	209	1,154	808
Taxed at 50 percent.....	27	1	-	-	1	-
Tier two oil:						
Taxed at 60 percent.....	157,181	4,830	2,972	82	1,776	1,066
Taxed at 30 percent.....	105,170	3,323	2,052	54	1,217	361
Tier three oil (taxed at 30 percent):						
Newly discovered oil ¹	287,540	9,183	6,448	162	2,573	711
Incremental tertiary oil.....	31,306	997	678	16	303	90
Heavy oil.....	96,060	2,202	1,746	3	453	137
Returns with total tax liability only.....	-	-	-	-	-	727 ²

¹Newly discovered oil is taxed at 27.5 percent beginning in 1982.

²Also includes \$70 million for returns that reported by tier and type, but did not report data for columns 1-5.

NOTE: Detail may not add to total because of rounding.

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Table 4.--Windfall Profit Tax Liability For Returns Reporting Components of Windfall Profit by Oil Tier and Tax Rate For January - September 1982 Average Daily Production and Average Dollars per Barrel

Oil tier and tax rate	Daily production (000's) (barrels)	Removal price	Adjusted base price	State severance tax adjustment	Windfall profit	Tax liability before adjustments
	(1)	(2)	(3)	(4)	(5)	(6)
All returns, total.....	7,444	28.80	17.31	.58	10.91	6.49
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	3,354	30.75	15.53	.63	14.59	10.21
Taxed at 50 percent.....	325	31.85	15.96	.94	14.94	7.46
Tier one, Sadlerochit oil:						
Taxed at 70 percent.....	1,286	20.00	16.11	.59	3.30	2.30
Taxed at 50 percent.....	(¹)	28.66	15.26	.63	12.77	6.39
Tier two oil:						
Taxed at 60 percent.....	576	30.73	18.90	.52	11.30	6.78
Taxed at 30 percent.....	385	31.64	19.50	.52	11.62	3.44
Tier three oil (taxed at 30 percent):						
Newly discovered oil ²	1,053	31.98	22.39	.56	9.02	2.49
Incremental tertiary oil.....	115	31.94	21.62	.53	9.78	2.93
Heavy oil.....	352	22.94	18.15	.03	4.76	1.43

¹Less than 500 barrels.²Newly discovered oil is taxed at 27.5 percent beginning in 1982.

NOTE: Detail may not add to total because of rounding.

Table 5.--Exempt Oil Volume by Tier and Category, Quarter Ending September 1982 (Thousands of barrels)

	Total	Tier one	Tier two	Tier three		
				Newly discovered oil	Incremental tertiary oil	Heavy oil
	(1)	(2)	(3)	(4)	(5)	(6)
Total.....	36,575	19,599	5,073	11,190	332	382
Exempt governmental interest.....	18,187	14,877	796	2,168	160	186
Exempt charitable interest.....	1,051	606	277	110	42	16
Exempt Indian oil.....	1,643	569	482	580	3	10
Exempt Alaskan oil.....	6,166	109	-	6,056	-	-
Exempt Royalty oil.....	9,528	3,438	3,517	2,275	127	171

NOTE: Detail may not add to total because of rounding.

Table 6.--Exempt Oil Volume by Tier and Category, January - September 1982 (Thousands of barrels)

	Total	Tier one	Tier two	Tier three		
				Newly discovered oil	Incremental tertiary oil	Heavy oil
	(1)	(2)	(3)	(4)	(5)	(6)
Total.....	106,474	59,471	13,652	31,510	863	979
Exempt governmental interest.....	54,902	45,148	2,501	6,365	408	481
Exempt charitable interest.....	3,355	1,837	852	452	170	44
Exempt Indian oil.....	4,445	1,695	1,398	1,317	8	28
Exempt Alaskan oil.....	19,021	632	245	18,141	1	1
Exempt Royalty oil.....	24,751	10,159	8,655	5,235	275	426

NOTE: Detail may not add to total because of rounding.