

Windfall Profit Tax, First Quarter, 1983

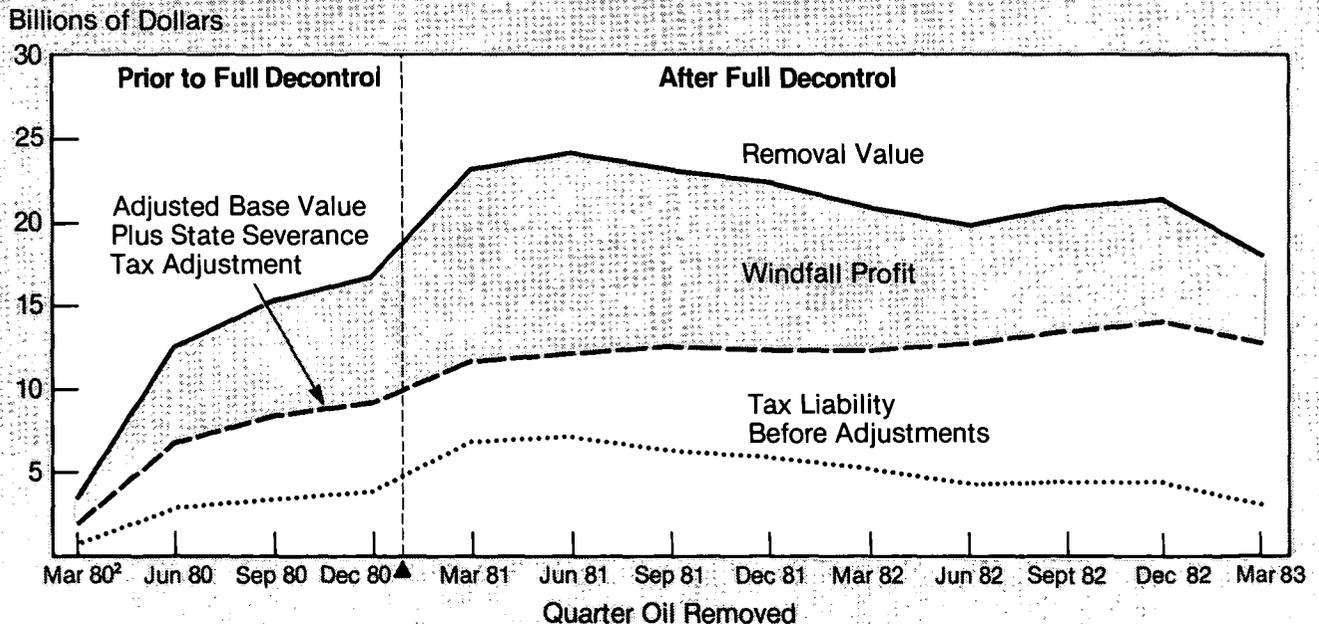
By Michael Alexander*

The first quarter of 1983 continued the downward trend in the windfall profit tax liability that has existed since the first quarter of 1981. The reported windfall profit tax liability for the first quarter of 1983 amounted to slightly more than \$3 billion after adjustments, bringing the total since the enactment of the Crude Oil Windfall Profit Tax Act to almost \$56 billion.

Windfall profit, defined as the removal value less the sum of the adjusted base value and State severance tax adjustment, decreased by \$2 billion or 29 percent from the fourth quarter of 1982 to the first quarter of 1983. This decrease in windfall profit can be attributed

to a combination of factors which include declining prices, a decrease in oil production and tax law changes. The average removal price (generally the price for which oil is sold) declined from \$28.67 per barrel to \$26.84 per barrel. The number of barrels of oil declined from 616 million to 585 million. The decline in the barrels of oil subject to the windfall profit tax resulted in part from a decline in domestic production in response to the price decrease and the exemption under the Economic Recovery Tax Act of 1981 (ERTA) of oil removed from stripper wells by independent producers beginning in 1983. More than 21 million barrels of stripper oil were claimed for the exemption for the first quarter of 1983.

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



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.

Tax liabilities also declined because the tax rate for newly discovered oil was reduced under ERTA from 27.5 percent for 1982 to 25 percent for oil removed in 1983, which accounted for a decrease in windfall profit tax of almost \$14 million.

Shown in the table below is windfall profit tax liability before and after adjustments. Tax liabilities, depending on the identity of the first purchaser, can be deposited up to 90 days after the close of the month the oil is removed [see Definitions]. The windfall profit tax liability after adjustments decreased almost \$700 million from the previous quarter. These adjustments were necessary as a result of errors in withholding during previous quarters or, more frequently, from the application of the net income limitation. The net income limitation adjustment amounted to -\$200 million while adjustments to previous quarters was almost \$7 million resulting in a total adjustment of -\$193 million for the current quarter. (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 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.

Windfall Profit Tax Before and After Adjustments
(Millions of Dollars)

Quarter Ending	Tax Before Adjustments	Total Adjustments	Tax After Adjustments
Total	\$59,187	-\$3,437	\$55,743
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
Dec. 1982	4,440	-634	3,806
Mar. 1983	3,320	-193	3,127

^{1/} One month only.

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 March 1983, 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 68 percent of 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 9 percent of the total production. The decrease in production of tier two oil was more than 32 million barrels from the fourth quarter of 1982 to the first quarter of 1983. This decrease can be attributed to the allowance of independent stripper oil as exempt oil under certain conditions beginning in 1983. As discussed earlier, exempt stripper oil amounted to more than 21 million barrels for the first quarter of 1983. That oil would have been subject to the windfall profit tax as tier two oil prior to 1983. Tier three oil, which consists of heavy oil, incremental tertiary oil and newly discovered oil (66 percent of tier three), accounted for 23 percent of total production as shown below.

Percent 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
Dec. 1982	65	12	23
Mar. 1983	68	9	23

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 Statistics of Income 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.

Deposit Requirements.--The timing of any first purchaser to deposit amounts withheld depends upon the identity of the first purchaser. Major refiners, other than independent refiners, are required to make semimonthly deposits of the withholding tax. All other first purchasers are required to make withholding deposits no later than 45 days after the oil is removed from the premises, except independent refiners who purchase oil under delayed payments contracts. They are required to make deposits by the first day of the third month beginning after the month of removal.

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, 1982.

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.

Exempt Stripper Oil.--Oil removed from stripper wells after 1982 may qualify for exemption from the windfall profit tax if the following conditions are met:

- (1) The oil must be removed from a stripper well property after 1982;
- (2) The oil must be produced by an independent producer;
- (3) The oil must be attributable to the independent producer's working interest in the property; and
- (4) The stripper well property must not be a property transferred by a nonindependent producer on or after July 23, 1981.

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 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.

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] At the inception of the windfall profit tax (March 1980), taxpayers were not required to complete the detail of the Form 6047, which shows how the tax is computed. However, taxpayers have been required to provide full information as of January 1981.
- [2] Joint Committee on Taxation (Staff), General Explanation of the Crude Oil Windfall Profit Tax Act of 1980, U.S. Government Printing Office, 1981.
- [3] See also Belal, Carol and Clark, Phil, "Windfall Profit Tax Liability for 1980," Statistics of Income Bulletin, Volume 1, Number 2, pp. 50-54.
- [4] See also Coleman, Michael, "Crude Oil Windfall Profit Tax for 1981," Statistics of Income Bulletin, Volume 2, Number 2, pp. 41-46.
- [5] See also Alexander, Michael, "Crude Oil Windfall Profit Tax for 1982," Statistics of Income Bulletin, Volume 3, Number 2, pp. 35-40.

Table 1.--Windfall Profit Tax Liability by Oil Tier and Tax Rate For Quarter Ending March 1983 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.....	585,286	15,714	10,635	247	4,832	2,899
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	259,564	7,584	4,260	138	3,186	2,218
Taxed at 50 percent.....	23,431	705	389	19	297	149
Tier one, Sadlerochit oil:						
Tax at 70 percent.....	116,123	2,051	1,897	21	133	93
Taxed at 50 percent.....	-	-	-	-	-	-
Tier two oil:						
Taxed at 60 percent.....	46,240	1,365	914	20	431	237
Taxed at 30 percent.....	4,357	132	89	2	41	12
Tier three oil (taxed at 30 percent):						
Newly discovered oil ¹	89,540	2,736	2,135	40	561	136
Incremental tertiary oil.....	17,770	543	415	7	121	36
Heavy oil.....	28,261	598	537	(2)	61	18
Returns with total tax liability only.....	-	-	-	-	-	421 ³

¹Newly discovered oil is taxed at 25.0 percent beginning in 1983.²Less than \$500,000.³Includes \$29 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.

Table 2.--Windfall Profit Tax Liability For Returns Reporting Components of Windfall Profit by Oil Tier and Tax Rate For Quarter Ending March 1983 Average Daily Production and Average Dollars per Barrel

Oil tier and tax rate	Daily production (000's) (barrels)	Removal value	Adjusted base price	State severance tax adjustment	Windfall profit	Tax liability before adjustments
	(1)	(2)	(3)	(4)	(5)	(6)
All returns, total.....	6,362	26.84	18.17	.42	8.25	4.95
Tier one, other than Sadlerochit oil:						
Taxed at 70 percent.....	2,821	29.21	16.41	.53	12.27	8.54
Taxed at 50 percent.....	255	30.10	16.61	.80	12.69	6.34
Tier one, Sadlerochit oil:						
Taxed at 70 percent.....	1,262	17.66	16.33	.18	1.15	.79
Taxed at 50 percent.....	-	-	-	-	-	-
Tier two oil:						
Taxed at 60 percent.....	503	29.51	19.76	.43	9.32	5.12
Taxed at 30 percent.....	47	30.38	20.40	.57	9.41	2.80
Tier three oil (taxed at 30 percent):						
Newly discovered oil ¹	973	30.55	23.83	.44	6.28	1.51
Incremental tertiary oil.....	193	30.55	23.35	.39	6.81	2.03
Heavy oil.....	307	21.15	18.98	-	2.17	.64

¹Newly discovered oil is taxed at 25.0 percent beginning in 1983.

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

Table 3.--Exempt Oil Volume by Tier and Category, Quarter Ending March 1983
(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.....	58,103	17,777	26,876	12,200	571	679
Exempt governmental interest.....	17,220	13,527	643	2,226	295	529
Exempt charitable interest.....	908	459	300	125	16	7
Exempt Indian oil.....	949	437	277	222	6	7
Exempt Alaskan oil.....	7,021	39	-	6,981	-	-
Exempt Royalty oil.....	10,750	3,315	4,401	2,644	254	136
Exempt Stripper oil.....	21,255	-	21,255	-	-	-

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