

HOUSE FINANCE COMMITTEE
May 5, 2006
9:53 A.M.

CALL TO ORDER

Co-Chair Meyer called the House Finance Committee meeting to order at [9:53:06 AM](#).

MEMBERS PRESENT

Representative Mike Chenault, Co-Chair
Representative Kevin Meyer, Co-Chair
Representative Bill Stoltze, Vice-Chair
Representative Richard Foster
Representative Mike Hawker
Representative Jim Holm
Representative Reggie Joule
Representative Mike Kelly
Representative Beth Kerttula
Representative Carl Moses
Representative Bruce Weyhrauch

ALSO PRESENT

Representative Ethan Berkowitz; Representative Paul Seaton;
Representative Les Gara; Representative Norman Rokeberg;
Representative Ralph Samuels; Representative Carl Gatto;
Robynn Wilson, Director, Division of Tax, Department of
Revenue; Dan Dickinson, Consultant, Tax Division, Department
of Revenue; Heather Brakes, Staff, Senator Gene Therriault;
Paul Lisankie, Director, Division of Workers' Compensation;
Robert Mintz, Attorney contracting with the Department of
Law

SUMMARY

CS SB 169(JUD)

An Act relating to release of information in individual workers' compensation records; and providing for an effective date.

HCS CS SB 169(FIN) was reported out of Committee with a "do pass" recommendation and with zero note #2 by the Department of Labor & Workforce Development.

CS SB 305(FIN) am

An Act repealing the oil production tax and the gas production tax and providing for a production tax on oil and gas; relating to the calculation of the gross value at the point of production of oil

and gas and to the determination of the value of oil and gas for purposes of the production tax on oil and gas; providing for tax credits against the production tax on oil and gas; relating to the relationship of the production tax on oil and gas to other taxes, to the dates those tax payments and surcharges are due, to interest on overpayments of the tax, and to the treatment of the tax in a producer's settlement with the royalty owners; relating to flared gas, and to oil and gas used in the operation of a lease or property under the production tax; relating to the prevailing value of oil and gas under the production tax; relating to surcharges on oil; relating to statements or other information required to be filed with or furnished to the Department of Revenue, to the penalty for failure to file certain reports for the tax, to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue as applicable to the administration of the tax; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the tax, and to the deposit of tax money collected by the Department of Revenue; amending the definitions of 'gas,' 'oil,' and certain other terms for purposes of the production tax, and as the definition of the term 'gas' applies in the Alaska Stranded Gas Development Act, and adding further definitions; making conforming amendments; and providing for an effective date.

CS SB 305(FIN) am was HEARD & HELD in Committee for further consideration.

#SB169

CS FOR SENATE BILL NO. 169(JUD)

An Act relating to release of information in individual workers' compensation records; and providing for an effective date.

9:53:49 AM

HEATHER BRAKES, STAFF, SENATOR GENE THERRIAULT, summarized the intent of SB 169, which stipulates that an employee's name, address, social security number and telephone number contained in their Medical or Rehabilitation records on file with the Division of Worker's Compensation, are not public records subject to public inspection.

The bill allows an employee to authorize the disclosure of such personal information by signing a declaration on a form provided by the division. It would protect the privacy of individuals who have filed a claim under the Workers' Compensation Act.

Ms. Brakes noted that the bill had been introduced in 2005, to prohibit the Division of Workers' Compensation from assembling or providing information relating to individual records outside the scope of the Workers' Compensation Act. The section was incorporated into another bill and enacted through Chapter 10, FSSLA 2005. In a recent case, Kuebler v. Lisankie, the Alaska Superior Court found that statute ambiguous. It was found that public right to access information outweighed an individual's right to privacy, absent was a solid argument from the State in that litigation. The Court found that the State had not submitted solid legislative intent or history on the matter.

Ms. Brakes summarized that SB 169 is an attempt to clarify the Legislature's intent.

[9:56:06 AM](#)

PAUL LISANKIE, DIRECTOR, DIVISION OF WORKERS' COMPENSATION, offered to answer questions of the Committee.

Co-Chair Meyer MOVED to ADOPT Amendment #1, Page 2, Line 6, following, "address", inserting "social security number". Vice Chair Stoltze OBJECTED.

Ms. Brakes explained that had been an oversight in the previous version and the Department of Law recommends that language be included.

Vice Chair Stoltze WITHDREW his OBJECTION. There being NO further OBJECTION, Amendment #1 was adopted.

[9:57:42 AM](#)

Vice Chair Stoltze MOVED to REPORT HCS CS SB 169 (FIN) out of Committee with individual recommendations and with the zero note. There being NO OBJECTION, it was so ordered.

HCS CS SB 169 (FIN) was reported out of Committee with a "do pass" recommendation and with zero note #2 by the Department of Labor & Workforce Development.

[9:58:37 AM](#)

#SB305
CS FOR SENATE BILL NO. 305(FIN) am

An Act repealing the oil production tax and the gas production tax and providing for a production tax on oil and gas; relating to the calculation of the gross value at the point of production of oil and gas and to the determination of the value of oil and gas for purposes of the production tax on oil and gas; providing for tax credits against the production tax on oil and gas; relating to the relationship of the production tax on oil and gas to other taxes, to the dates those tax payments and surcharges are due, to interest on overpayments of the tax, and to the treatment of the tax in a producer's settlement with the royalty owners; relating to flared gas, and to oil and gas used in the operation of a lease or property under the production tax; relating to the prevailing value of oil and gas under the production tax; relating to surcharges on oil; relating to statements or other information required to be filed with or furnished to the Department of Revenue, to the penalty for failure to file certain reports for the tax, to the powers of the Department of Revenue, and to the disclosure of certain information required to be furnished to the Department of Revenue as applicable to the administration of the tax; relating to criminal penalties for violating conditions governing access to and use of confidential information relating to the tax, and to the deposit of tax money collected by the Department of Revenue; amending the definitions of 'gas,' 'oil,' and certain other terms for purposes of the production tax, and as the definition of the term 'gas' applies in the Alaska Stranded Gas Development Act, and adding further definitions; making conforming amendments; and providing for an effective date.

Representative Hawker MOVED to ADOPT work draft #24-GS2052\N, Chenoweth, 5/4/06, as the version of the bill before the Committee. Representative Kerttula OBJECTED for discussion purposes.

[10:00:06 AM](#)

ROBYNN WILSON, DIRECTOR, DIVISION OF TAX, DEPARTMENT OF REVENUE, highlighted the comparative revenues of the Petroleum Production Tax (PPT) bill as received through the Governor and the Department of Revenue. (Copy on File).

Ms. Wilson explained the key points, which provides a tax & credit rate of 20% and a progressivity tax based on net. The base allowance credit provision was retained from the House Resources Committee (HRC) version. The Cook Inlet oil & gas is treated differently.

[10:04:40 AM](#)

Ms. Wilson pointed out the general tax rate of 20% with $\frac{3}{4}$ revenue exclusion in Cook Inlet oil. In the Senate Finance Committee (SFC) version, value exclusion on gas revenue (GRE) had been included. The Senate addressed Cook Inlet oil by providing a special tax rate of 5% on the net; however, technical concerns were voiced, which left no provision for cost allocations. The House Finance Committee (HFC) version removes the 5% net and uses the GRE with $\frac{3}{4}$ exclusion, providing a 5% effective tax rate.

[10:06:30 AM](#)

DAN DICKINSON, CONSULTANT, TAX DIVISION, DEPARTMENT OF REVENUE, observed that because of net versus gross, the effect lowers the tax rate on Cook Inlet oil and would make less than 5%.

[10:07:04 AM](#)

Ms. Wilson pointed out that in the draft before the Committee, Cook Inlet gas was treated differently, using a tax ceiling of 19 cents. The credit rate remains at 20%; the private royalty rate is 5% on oil and 1.67% on gas, and includes a provision for receiving a commissioner's report. The gas revenue value exclusion (GRE) in the Senate version was incorporated, providing $\frac{2}{3}$ of the gross value excluded on gas.

[10:08:17 AM](#)

Representative Kerttula asked if that meant $\frac{1}{3}$ of the 20% tax. Ms. Wilson referenced Section 160, which divides the net value, indicating that $\frac{2}{3}$ of the net value would be excluded and the remaining $\frac{1}{3}$ taxed at the 20%, except in Cook Inlet.

Representative Kerttula asked about the Cook Inlet credits. Ms. Wilson explained that it is a statewide tax system and the credits can be used anywhere within the State.

[10:09:09 AM](#)

Ms. Wilson discussed progressivity, based on the net and in contrast to the HRC version, where it is based on gross. The trigger point & slope were increased.

[10:09:48 AM](#)

Representative Hawker asked if the trigger point would move up or down "dollar-wise". Ms. Wilson said the trigger point was brought down from \$45 to \$35 dollars net.

Co-Chair Meyer asked at current oil prices, what would the effective tax rate be if it were imposed. Ms. Wilson replied at \$70 dollars, it would be calculated at 25%.

Representative Kerttula questioned the reason for determining the progressivity on the net rather than on the gross. Ms. Wilson replied it was clearly a policy call. A progressivity based on net recognizes costs better than on the gross; however, if placed on gross, it could accommodate better the differences between oil and gas. If there was a windfall profit piece dependant on the price of oil, a progressivity based on gross could be a better plan.

Mr. Dickinson agreed and pointed out several effects as costs increase and on the gross, there could be a smaller margin at the \$20 dollar price.

Representative Kerttula reiterated that net value had been used to calculate everything else. She suggested it would be simpler to use the same value for progressivity. Mr. Dickinson argued that in terms of simplicity, the proposed concept results in the same tax base for the 20% & for the increase.

[10:13:41 AM](#)

Ms. Wilson continued, the progressivity is based on the net and that valuable oil and gas in the State means that there would be no special gas progressivity.

Representative Joule identified certain costs and the inclusion of the progressivity twice. Ms. Wilson informed that had been a different measure and would not be deducted twice. The bill before the Committee provides for two different measures - the Petroleum Production Tax (PPT) rate and progressivity, both taken against the same net value.

[10:15:39 AM](#)

Ms. Wilson identified the deductibility of the progressivity tax. Under all the bills, progressivity is a separate tax and cannot be deducted for net value. This transition was originally called the "claw back", evolving during the legislative process. The version before the Committee adopts the Senate language, providing a five-year look back for capital expenditures and a 2-for-1 recouping, equaling 20% credit.

The version before the Committee adopts a seven-year rolling sunset, which means that if a company were not yet commercially producing, their seven years would not start until the beginning of their commercial production.

She addressed the allowance based on barrels. The version before the Committee retains a \$12 million dollar credit, based on current investment. The credit is only available for up to ½ of the current investment.

[10:18:46 AM](#)

Representative Hawker suggested that a fixed credit amount would be a better solution as the other option punishes small producers. Co-Chair Chenault explained that the intent was to look at "gold plating" without affecting the smaller producers. The HFC version looks to adjust that.

[10:19:46 AM](#)

Ms. Wilson commented that the base allowance provides for a 10-year sunset, creating a rolling sunset. The safe harbor language was adopted from the Senate version with a 95% required, annual true up; if paid monthly, there would be no interest on that amount. If a company pays less, there is interest on the unpaid balance. If the company does not pay the full amount, there would be interest but no penalty.

Co-Chair Meyer asked why there would be no penalty. Ms. Wilson responded, there are penalty provisions in the general administration section and that interest would be sufficient.

[10:21:26 AM](#)

Ms. Wilson pointed out an effective date of July 1, 2006. Also, during the first six months, the company has the option to pay under the old Economic Limit Factor (ELF) system.

Representative Hawker worried that it would provide only six months to the Department to get regulations in place. He asked assurance if that was possible. Ms. Wilson could not provide 100% certainty, however, noted that the Department expects to hire extra regulation writing staff.

[10:23:01 AM](#)

Representative Joule asked if the Department of Revenue would be the only Department providing audits. Ms. Wilson responded that in the transitional provision, the primary 'push' would be writing regulations by the Department of Revenue. She acknowledged that the Department of Natural Resources has employees for auditing the values.

Mr. Dickinson added that the Department of Natural Resources will use the standard in current law to look at gross value. The change in net moves it to up-stream costs. Any

additional obligations resulting from the legislation will be addressed by the Department of Revenue.

[10:24:53 AM](#)

Ms. Wilson noted that the spill surcharge, referred to as "split-nickel" results in two cents suspended and three cents collected. In the version before the Committee, it maintains the amount of five cents, but decreases it to one cent suspended and collects four cents.

Representative Kerttula asked if the Department of Environmental Conservation had seen the provision. Mr. Dickinson replied, there had been no analysis on that portion of the bill.

[10:26:28 AM](#)

Ms. Wilson pointed out that the surcharge treatment would not be creditable or deductible and is the same as in the Senate version.

The version before the Committee extends the SB 185 exploration credit for ten years. It fixes language in current statute regarding the \$20 million dollar Cook Inlet limit. Under the bill, there is no deduction or credit for abandonment of old facilities.

Representative Kerttula interjected that "old" would not be allowed but the new production would be. Ms. Wilson agreed.

Representative Kerttula questioned if abandonment issues had been addressed more than twice. Ms. Wilson stated that the language had been improved from the Senate version but not expanded to that extent.

Representative Kerttula asked if abandonment costs had been figured into exploration costs. Mr. Dickinson said yes; yet, commented that mediation costs created a large uncertainty and are costs included in the full cycle.

Representative Kerttula did not understand how they could be determined and requested back up. Mr. Dickinson noted there had been past estimates and that the difficulty in estimation does not mean it would be left out. Representative Kerttula voiced her concern.

[10:30:30 AM](#)

Representative Kelly asked about the 185 credit & the extension of the sunset. Ms. Wilson explained that under the PPT, foreign exploration expenditures could be claimed. Under SB 185, a producer would be allowed a 40% credit, based on mileage-distance from current wells. Any dollar

for exploration costs could not be claimed twice. Mr. Dickinson referenced Page 7, Line 30, which clarifies the four programs. Ms. Wilson noted that was additional language and a change from the House Resource Committee (HRC) version.

[10:32:51 AM](#)

Ms. Wilson discussed the extent the credits could be used. They cannot be used to offset the progressivity tax, rather against the PPT tax. The version of the bill before the Committee allows credits to be transferable. Only 20% of the purchaser's liability can be offset.

The HRC version provides for up to \$10 million dollars of refundable credits; the version before the Committee does not provide for refundable credits. A credit would be available at the end of the year for any annual loss based on the tax rate.

[10:34:19 AM](#)

Representative Kerttula inquired how many times a single expenditure could be deducted. Ms. Wilson replied that under the PPT bill, a capital expenditure could be deducted and receives a 20% credit. She added, it also comes off in the federal taxation.

Representative Kerttula inquired what the total deductible percentages would be. Ms. Wilson replied, a top marginal rate of 35% was used for federal tax and in the worldwide arena, the deduction could be a portion based on business in Alaska compared to everywhere else.

Representative Kerttula requested more information regarding those numbers.

Representative Hawker pointed out different tax systems applied to the same taxpayers and did not believe they could receive compounded deductions. He refuted the idea of "double dipping".

Mr. Dickinson pointed out that a deduction could lower the tax. The company is allowed to take the deduction, but those costs can be used only one time.

[10:38:19 AM](#)

Representative Kerttula asked about the carry-forward time limit and how the State could protect against using that in low oil years. Mr. Dickinson explained that at the end of the tax, there would be a point when the costs overwhelm the ability to produce. He acknowledged that if prices fall,

PPT revenues could be reduced to zero, but when prices rise, the State again would be collecting revenues.

Representative Kerttula advised there was no language inclusion to protect against that scenario. Mr. Dickinson noted that there is no guarantee for receiving revenue when investments are not profitable. The proposed system is a profit-based tax.

Representative Kerttula indicated the problem with a roll-forward. Mr. Dickinson reiterated that profits are not a year-by-year thing. To determine the actual investment, it is important to determine the amount made in consecutive years.

Representative Kerttula reiterated concern with the carry-forward protections generating revenue. Mr. Dickinson stated that the Administration has been careful in addressing those concerns by including the property taxes. The proposal offers four different revenue-generating avenues.

[10:42:15 AM](#)

Ms. Wilson pointed out language removed from the HRC version, regarding the gross value by the Department of Natural Resources. She anticipated an amendment to restore that language, as it places responsibility on the Department to determine excess lost tax.

Representative Kerttula asked how the point-of-production definition works.

ROBERT MINTZ, ATTORNEY, CONTRACTING WITH THE DEPARTMENT OF LAW, explained that the main change reflected in the version of the bill before the Committee is the refinement of the definition of gas treatment. There was concern raised by the industry that gas treatment was overly defined because it included field dehydration. The version of the bill before the Committee, clarifies that fuel dehydration is not a part of gas treatment.

[10:45:10 AM](#)

Representative Kerttula asked if that was the only reference to gas treatment, now upstream. Mr. Mintz said yes and noted other refinements in the language such as the definition of the gas-processing plan. The bill contains a definition of gross value at the point of production.

Ms. Wilson continued, the Senate version contained a provision allowing the Department of Revenue to write regulations incorporating provisions of the Internal Revenue Code #482, which deals with the transfer pricing issues. In

the federal arena, it could come up with transactions between a domestic company and their foreign affiliates.

[10:47:34 AM](#)

Ms. Wilson mentioned catastrophic oil spills, which the Governor's original bill had not addressed. In the HRC version, it was not deductible and that language was removed from the Senate version. The proposed version does not include catastrophic oil spill language, language defined in Statute. The language in the HRC version addresses a spill in marine waters, which is removed and would be deductible. Oil spills could be deductible if they occur on the lease and not through fraud or negligence.

Mr. Mintz noted it is important to understand how the bill is intended to work. The number of non-deductible items is not an exhaustive list. They are only examples of specific costs. If not included, then one returns to the fundamental definition, which is "direct, ordinary, necessary costs of exploring or producing oil and gas". Clean-up costs would sometimes be deductible and would not be listed as an exclusion.

[10:50:54 AM](#)

Representative Kerttula said that the State would continue to participate in the 470 Fund to help clean up spills. She urged further clarity on that section.

[10:51:23 AM](#)

Ms. Wilson noted additional language in the Senate version, regarding exploration credits that the Department of Natural Resources would provide. The language was incorporated into the version of the bill before the Committee. She noted additional clarifying language regarding regulations after industry practice.

[10:52:43 AM](#)

Representative Kerttula requested a comparison, including the Senate Resources Committee (SRC) version. Co-Chair Chenault recommended that be made available.

AT EASE: [10:53:52 AM](#)
RECONVENE: [10:54:00 AM](#)

[10:54:05 AM](#)

Ms. Wilson proceeded with an overview of the bill.

Page 2, Lines 16-25, provides intent language added from the Senate version clarifying that the Department of Environmental Conservation would reduce program costs.

Page 3, Line 29, highlights the general tax rate of 20%.

Page 4, Lines 23-31, clarifies the progressivity language. Subsection (G) provides the slope factor percentage of .256%.

[10:55:37 AM](#)

Page 6, Line 2, illustrates the trigger point; \$35 dollars is the net value. She compared the resulting price index. Ms. Wilson pointed out language on the Cook Inlet gas, Lines 9-13, intended not to exceed 19 cents. That number was taken from the March average gas ELF in Cook Inlet.

Mr. Dickinson added that the (J-K) formula at net, averages the tax rate and that there are value shifts in making the calculation.

[10:58:06 AM](#)

Ms. Wilson continued Page 6, Section 7, Lines 6-18, provides language for the "safe harbor" true-up @ 95%.

Page 8, Line 2, indicates a credit rate of 20%. Lines 12-29, provides language in which the Department of Natural Resources provides exploration data.

Page 10, Lines 30-31, highlights the transitional provisions of the 2 for 1, carrying that language onto Page 12. Page 11 indicates the five-year look back; the 2 for 1 is listed on Lines 13-19.

Ms. Wilson continued, Lines 22-28 indicates the 7-year sunset. Mr. Dickinson interjected information regarding sunset needs. The companies would be in a position to claim production expense and would need a window to make that claim. The intent makes a transitional investment. It places a new producer on the same footing as a company producing before the bill became effective.

[11:01:04 AM](#)

Ms. Wilson referenced Page 12, Lines 4-17, language taken from the Senate version, in which the producer receives a credit on a facility subject to regulation. Also, the producer would support all rate proceedings for tariffs. She pointed out that there was a piece in the Senate version regarding audits, which was not included in the version before the Committee.

Representative Hawker recognized that language came from the Senate and understood the need for a regulated facility, but thought that Section 2 was problematic. He asked about applying it to all circumstances, which makes a definitive statement regarding discount service costs.

[11:04:09 AM](#)

Mr. Dickinson agreed with Representative Hawker, acknowledged the uncertainties involved with the issue. Representative Hawker mentioned parties receiving credit. He asked if the Department of Revenue would have to be included in each transaction with the industry. Mr. Dickinson replied they would be involved with every transaction involving physical assets receiving credit. Representative Hawker worried about the fiscal costs associated with that.

[11:06:22 AM](#)

Representative Weyhrauch interjected that it appears to give the consumer a break. Mr. Dickenson agreed.

Representative Kerttula thought companies could come forward and file evidence. She maintained that it is not onerous.

Mr. Dickinson advised that the State would have to regulate the profits and rate of returns. Representative Kerttula countered that situation could be unfair. Mr. Dickinson agreed that it might be a "good goal", but the language does not identify that.

[11:09:11 AM](#)

Ms. Wilson continued, Page 12, Lines 30-31, removes old language and is consistent with the Senate version. Mr. Dickinson explained the removed language references a sunset provision.

Ms. Wilson pointed out that Page 13, Line 16, provides the 10-year extension in which SB 185 appears.

Page 15, the amendments contained on Lines 19-28, corrects a statutory concern regarding the Cook Inlet credit. Representative Hawker requested clarification.

Ms. Wilson explained that the original intent was that no additional credits would be granted if Cook Inlet reached \$20 million dollars. The statutory language states that credits would not be granted, implying that they would not be granted anywhere. That language was adjusted. The other concern dealt with the October date. The amendment sets a more fair approach and provides another year.

[11:12:16 AM](#)

Representative Hawker pointed out the "no cap" on the North Slope. He questioned if there should be a cap placed on Cook Inlet exploration efforts.

[11:12:54 AM](#)

Ms. Wilson explained that Page 19, Section 25, allows for the Department to use RSA values. She requested that language be amended to include provisions determining cost effectiveness. Representative Hawker noted support for that solution. Mr. Dickinson offered to work with Representative Hawker.

Representative Kelly pointed out that there had been a lot of work done on the RSA and wondered how the goal of "acceptable language" would be achieved. Mr. Dickinson replied the Administration would appreciate making the concept work for everyone.

[11:15:56 AM](#)

Ms. Wilson referenced Page 20, Lines 8-9, which provides the GRE, language taken from the Senate version. Lines 6-8 indicate a value exclusion for Cook Inlet oil.

Representative Kelly realized it would be challenging to satisfy needs for all sized fields. He recommended further work to determine those areas as well as the community subsidies.

SB 305 was HELD in Committee for further consideration.

[11:18:47 AM](#)

RECESSED:

The meeting was RECESSED at 11:19 A.M.